



April 15, 2011

Memorandum

To: Members of the Board

From: Ross Simms, Assistant Director

Through: Wendy M. Payne, Executive Director

Subj: Federal Reporting Model – TAB E<sup>1</sup>

## **MEETING OBJECTIVE**

The objective of the meeting is to determine whether the Board agrees with staff's proposal to enhance the conceptual framework for the reporting model while concurrently developing requirements for a new basic financial statement.

## **BRIEFING MATERIALS**

Attachment 1 – Staff Proposal

Attachment 2 - Pro Forma Illustrations

Attachment 3 – Examples of Analyst Presentations

Attachment 4 – Board Member Email: Possible Reporting Model Project on Improving Display Understandability and Usefulness

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<sup>1</sup> The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations

## BACKGROUND

FASAB initiated the reporting model project to determine necessary improvements to the existing federal reporting model. To determine how best to improve the model while balancing the cost and benefit of its decisions, the Board sought input from users and the financial reporting community and organized a task force to consider enhancements to the model. The task force focused on the government-wide level because this was the level that users would likely begin their search for financial information about the federal government. Upon completion of reviewing this level, the task force prepared a report with recommendations for FASAB and its sponsors and the Board discussed the report and recommendations during the December 2010 meeting. Also, during the February 2011 meeting, the Board discussed an analysis of the recommendations that could likely be addressed by FASAB. Subsequently, the Board noted that many of the task force proposals could be implemented voluntarily by preparers and experimentation would be needed before the Board could consider addressing other proposals. Review of the component entity level reporting model remains.

In addition, during its deliberations on social insurance, FASAB determined that a new basic statement should be developed. In February 2009, the Board began deliberating comments in response to the exposure draft (ED), *Social Insurance Accounting, Revised*. One of the broad issues raised in response to the ED concerned the appropriateness of reporting the closed group measure for social insurance, as a concept, and/or its display on the balance sheet or any basic financial statement or anywhere in the financial report. The Board discussed options for a basic financial statement presentation and subsequently, in April 2009, decided to either modify the balance sheet or develop a new basic financial statement. The options were as follows:

- Add a separate section to the bottom of the balance sheet that presents sustainability amounts.
- Retain the balance sheet as is and create a new financial statement that combines the balance sheet amounts and social insurance amounts. The new statement would have two columns, one for the balance sheet amounts and one for social insurance amounts.

At that time, there was strong support for creating a new statement that combines the balance sheet and social insurance amounts in one presentation.

Later, during the August 2009 meeting, the Board determined that a new basic statement would require another ED and another cycle of due process for the Social Insurance standard. Consequently, the Board decided to issue the social insurance standard without a new basic financial statement and integrate the work on a new basic statement with the reporting model project.

Attachment 1 presents the staff proposal for enhancing the conceptual framework for the reporting model while concurrently developing a new basic financial statement. Also, Attachment 2 provides pro forma illustrations of basic financial statements that the Board

had been considering and Attachment 3 provides examples of how some citizen intermediaries are reporting the federal government's fiscal challenges. Additionally, for your consideration, Attachment 4 provides an email message from Board member Tom Allen on the subject, "Possible Reporting Model Project on Improving Display Understandability and Usefulness." In the email, Mr. Allen discusses some of his thoughts on improving the understandability of our financial statements.

## **QUESTIONS FOR BOARD MEMBERS**

1. Do you agree or disagree with the overall staff proposal to enhance the conceptual framework while concurrently developing a new basic financial statement?
2. If you agree with the staff proposal, are there additional issues you believe should be addressed by the effort to enhance the conceptual framework?
3. If you agree with the staff proposal, what are your expectations for the new basic financial statement?
4. If you disagree with the proposal, what do you believe should be the next steps for the reporting model project?

If you have questions or need additional information, please contact me at 202-512-2512 or by email at [simmsr@fasab.gov](mailto:simmsr@fasab.gov) as soon as possible. I will be able to consider and respond to your request more fully in advance of the meeting.

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## **Attachment 1: Staff Proposal**

# Staff Proposal

## Introduction

Improvements to the conceptual framework and financial information requirements may be needed to help ensure that the public is informed of fiscal opportunities and challenges in an understandable manner. Citizens and other user groups appreciated the endeavors of FASAB, its sponsors, and the financial reporting community in reaching out to them and working to provide understandable financial information about the federal government. Financial reporting provides a wide-array of information to help enhance public accountability, such as information on internal control, amounts paid, costs incurred, assets, obligations, and long-term challenges. Also, charts and graphs are used to help communicate the information. However, users need additional help to better understand the federal government's financial wellbeing.

In Statement of Federal Financial Accounting Standards (SFFAS) 37, *Social Insurance: Additional Requirements for Management's Discussion and Analysis*, FASAB acknowledged that additional conceptual guidance and standards are needed. For example, the Basis for Conclusions section states that concepts need to better explain unique federal accounting issues.<sup>2</sup> Also, although FASAB decided to require key measures in a table or other singular format in Management's Discussion and Analysis (MD&A), the Board intends to develop a new basic financial statement.<sup>3</sup>

Staff recommends developing additional conceptual guidance and requirements for a basic financial statement concurrently. Work on the basic financial statement could inform the work on the conceptual guidance. Also, progress on the reporting model to date would help frame discussions on the concepts and the new statement. This approach would enable the Board to fill voids and resolve recurring conceptual concerns, help future Boards by providing a sound framework to use in methodically deciding between alternative approaches, and help the public better understand the financial condition of the federal government.

## Informing the Public

The Board has stated that citizens are the intended audience for the Financial Report of the U.S. Government (CFR)<sup>4</sup> and staff discussions with citizens found that they appreciated the government's efforts to inform them of the government's financial condition. Citizens believed that the CFR is an important document for the general public to access and gain insights on the financial condition of the federal government. Also, members of other user groups provided similar responses. However, users noted that the information being provided was challenging to understand. They noted that

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<sup>2</sup> SFFAS 37, par. A42.

<sup>3</sup> SFFAS 37, par. A48.

<sup>4</sup> Statement of Federal Financial Accounting Concepts (SFFAC) 4, *Intended Audience and Qualitative Characteristics for the Consolidated Financial Report of the U.S. Government*.

charts and graphs were helpful, but some tables and the use of different perspectives (obligation<sup>5</sup>, cash, and accrual bases and cash and economic projections) were challenging to grasp.

The public wants to know how well the federal government performed in achieving its financial goals and what are the future benefits and challenges that government leaders are expecting. Conceptual guidance and additional requirements could help lead to more understandable financial information that would address the public's questions.

### **Conceptual Voids and Matters Needing Additional Clarification**

During previous efforts to develop financial information requirements, conceptual voids and matters requiring additional clarification have been noted but remain unresolved. For example, over the course of developing the information requirements for social insurance, the Board noted that the conceptual guidance could better explain why:

- the power to tax is not an asset but nonetheless is relevant to assessing the sustainability or the financial condition of the federal government;
- current deficits are indeed bad but that the problem is actually long-range rather than short-range;
- the timing of a cash flow problem is important; and
- the point estimates on the balance sheet have limitations for assessing financial condition.<sup>6</sup>

It appeared that FASAB decided not to address such matters during that time because it would require re-exposing the social insurance ED and delaying the social insurance standard.

In addition, while existing financial statements present “complementary” perspectives to address the reporting objectives, some Board members have expressed concern that information on the face of some existing financial statements do not link mathematically (articulate).<sup>7</sup> Concerns about financial statement articulation have been expressed in various FASAB deliberations. For example, when the Board deliberated stewardship reporting requirements in August 2000, it was noted that the challenge would be defining how the financial statements would articulate. Although significant progress has been made since that time, the matter of articulation continues to be raised as new

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<sup>5</sup> The obligation basis is primarily used to control spending. It measures economic events when goods are ordered or contracts awarded. This basis is not used for recognizing revenues, such as taxes, or the use of property, plant, and equipment (depreciation).

<sup>6</sup> SFFAS 37, par. A42.

<sup>7</sup> It should be noted that the President's Commission on Budget Concepts deliberated using different bases for the U.S. budget and determined that different budgets would be confusing and impede governmental decision-making. See *Report on the President's Commission on Budget Concepts*, U.S. Government Printing Office, Washington, October 1967.

statements are added to the reporting model and their fundamental use not described in the concepts. Some current observations are as follows:

- Citizen intermediaries are aggregating long-term cash flow projections with accrued liabilities to help citizens learn about the federal government's financial condition (see Attachment 3 for examples). Citizen intermediaries are citizens' primary source for financial information about the federal government and they use measures presented in the CFR to help citizens analyze the nation's fiscal challenges. In recent periods, some citizen intermediaries have presented analyses that combine amounts presented in the accrual basis balance sheet with the long-term projections presented in the statement of social insurance (SOSI) rather than viewing the financial statements like one would view a dashboard.<sup>8</sup> Considering that the balance sheet is intended to show information as of a particular time, while long term projections are intended to provide insights about the future, financial reporting concepts do not explain whether aggregating the amounts are appropriate. Consequently, additional conceptual guidance could help citizen intermediaries understand how the different financial statements should be used in their analyses.
- The SOSI does not articulate with the balance sheet and the SOSI's elements are defined independently of the elements in accrual basis financial statements.
- The relationship between fiscal gap and the balance sheet should be discussed to help users understand the reason why the different perspectives are needed.
- The current conceptual framework does not discuss all the basic financial statements for the government-wide and component levels and how the financial statements fundamentally relate to each other. For instance, Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display*, does not discuss the purpose of the SOSI and statement of long-term fiscal projections and how those statements fundamentally relate to the balance sheet and other statements.
- Financial and budgetary accounting should be brought closer together so that financial statements can be more useful. Other countries use the same basis for budget and financial reporting because public attention is focused on the budget and accrual accounting would not be used to inform decisions unless the budget also used accrual accounting.
- Some executives and managers did not seem to understand how financial statements could be helpful. Understanding the purpose and links among the financial statements could help them monitor performance and develop strategic plans.

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<sup>8</sup> Dashboards provide various metrics that are not necessarily intended to be aggregated such as speed, fuel level, and temperature.



Moreover, some executives and managers did not appear to be aware that the discipline required to prepare financial statements contributes to providing them with accurate data for timely decision-making. They did not seem to understand that meeting the requirements of a set of accounting standards requires systems with common data definitions, classification structures, and on-going control activities to ensure reliability of the data. Properly developed systems can provide data for controlling spending, managing cash, monitoring operating performance, and ultimately enhancing accountability. Because FASAB's constituency includes internal as well as external users, clarifying this role of financial statements is important.

Addressing the conceptual voids and matters needing additional clarification could assist the Board in determining how well the financial reporting objectives are being achieved and help inform development of any new basic statement(s). Also, knowledge of these concepts could help users better understand the purpose of the various financial statements and the information they provide. A better understanding of the financial statements could assist users in selecting, analyzing, and interpreting the information they need. Consequently, enhancing the conceptual framework could enhance the usefulness of the financial statements.

## **New Basic Statement**

Regarding a new basic statement, FASAB was in the process of considering various options (See Attachment 2 for pro forma illustrations) and issues such as the following:

1. Should the new basic statement be combined with the balance sheet or should it be a separate, additional statement with the current balance sheet continuing as it is?

Members expressed tentative preferences for the following options:

- Combine the balance sheet and summary information about social insurance (see Attachment 2, Illustration 2a – Balance Sheet and Social Insurance Section and Illustration 2b – Balance Sheet and Social Insurance Section with gross domestic product (GDP) percentages).
  - Develop a new basic statement separate from and not affecting the balance sheet that would include some or all balance sheet amounts as well as social insurance amounts (see Attachment 2, Illustration 1 – Overall Perspective Table from FY 2004 Financial Report, for example).
2. If presented together on a statement or table, should the amounts for social insurance "responsibilities/commitments" and liabilities be added together?

The Board discussed whether “responsibilities” or “commitments” and liabilities should be added together. Some argued that these amounts should be added because everyone who publicly discusses these amounts adds them together. They cited the Peterson report (see Attachment 3, Excerpt from *State of the Union’s Finances: A Citizen’s Guide*), former Comptroller General Walker’s presentations, and a previous version of the CFR (see Attachment 2, Illustration 1).

Others countered that these amounts are fundamentally different, that they are “apples and oranges”; and/or, that proper context is needed; and/or, that readers can add them up if they want to, because the new statement would present the amounts in close proximity. Some members said there is a substantial difference between private parties aggregating these amounts and the federal government aggregating them. The latter connotes the imprimatur of the federal government. The Board’s discussion in June 2009 seemed to indicate a preference for a non-additive approach.

3. Should SFFAC 5, *Definitions of Elements & Basic Recognition Criteria*, be amended to define concepts for “responsibilities” or “commitments”?

In April, 2009, staff recommended amending SFFAC 5 to provide a conceptual basis for the “responsibilities” and “commitments” – two terms used in the social insurance ED that some respondents questioned. The staff argued that the absence of a conceptual foundation for what appear to be fundamental elements detracts from the standard. The social insurance ED had not tried to present a conceptual basis for these terms, proposing instead that concepts for “commitments” follow in due course in other FASAB projects. Many respondents found this point unpersuasive or ignored it.

Alternatively, at the April 2009 meeting, a Board member mentioned an approach where the standard would not use the terms “responsibilities” and “commitments” per se and therefore not introduce any new elements or concepts. Instead, social insurance amounts would be presented, for example, under the heading “social insurance” or “social insurance summary” or other similar terminology, in which case new concepts would not be needed. The member noted that the amounts already exist on the SOSI, new “statement of changes in social insurance amounts,” and “statement of long-term projections.” However, the Board has not felt the need to develop concepts for them.

Upon further consideration, the staff recommended the approach described in the preceding paragraph. This allowed the Board to realize what it had accomplished with respect to new MD&A, financial statements, and disclosures guidance, rather than delaying that realization while analyzing another set of issues. Amending SFFAC 5 would have required re-exposure of the social insurance ED.

4. Should the social insurance project amend SFFAC 2 to include display concepts for a new “basic” statement?

In April, 2009, the staff recommended expanding the display concepts to include the new financial statements. This approach would require amending SFFAC 2 and re-exposing the social insurance ED. Having SFFAC 2 address all the financial statements seemed desirable.

However, as mentioned above with respect to amending SFFAC 5, not amending SFFAC 2 at that time allowed the Board to finalize what it had accomplished with respect to new MD&A, financial statements, and disclosures guidance.

5. Should the statement include more than social insurance amounts, especially, should it include the "rest of government" or other long-term projections/"fiscal sustainability" amounts)?

The staff believed that the Board did not support including non-social insurance amounts in the new basic statement.

6. What social insurance amounts [closed group measure or open group measure] should be presented on the new basic statement?

Staff recommended using the open group measure in the new statement. This was consistent with the Board’s decision not to present a line item on the statement of net cost for the change in either the open or closed group measure.

The reporting model project will consider the options and issues the Board has been considering with respect to the new statement.

## **Planned Approach**

The objective of this phase of the reporting model project would be to develop a basic statement to help citizens better understand the financial condition of the federal government while concurrently enhancing the existing conceptual framework. The project would begin by continuing to focus on the government-wide level because the Board has noted that financial condition requires information “about the national economy and society, as well as about the government itself.” Also, because the Board has noted that some financial condition information may be needed when reporting on

selected programs,<sup>9</sup> insights gained from the government-wide level analysis would be used to determine the need for financial statement improvements at the component entity level.

In addition, as discussed earlier, the voids and needs for clarification in concepts involve both government-wide and component level financial statements. Accordingly, the conceptual guidance would address both levels.

The following table shows the best-case scenario of how the project would progress to concurrently address a concepts statement and a new basic financial statement.

| Step   | Concepts Statement | New Basic Financial Statement | Completion Date |
|--|--------------------|-------------------------------|-----------------|
| 1. Determine the scope of the concepts statement - develop an outline of key questions that should be addressed by a concepts statement. | X                  |                               | June 2011       |
| 2. Discuss outline of key questions for a proposed concepts statement with FASAB.  | X                  |                               | June 2011       |
| 3. Consult experts and other standards-setters as needed and develop an initial draft basic financial statement.                         |                    | X                             | August 2011     |
| 4. Discuss initial draft basic financial statement with FASAB.   |                    | X                             | August 2011     |
| 5. Discuss initial outline for a proposed concepts statement with FASAB  | X                  |                               |                 |
| 6. Consider FASAB input and revisit outline and basic financial statement.   | X                  | X                             | September 2011  |
| 7. Discuss final outline of concepts statement with FASAB.   | X                  |                               | October 2011    |
| 8. Discuss revised basic financial statement with FASAB.   |                    | X                             |                 |
| 9. Present pre-ballot draft – basic financial statement  |                    | X                             | December 2011   |
| 10. Discuss proposed concepts statement with FASAB.  | X                  |                               |                 |

<sup>9</sup> SFFAC 1, par. 236.

| Step   | Concepts Statement | New Basic Financial Statement | Completion Date |
|--|--------------------|-------------------------------|-----------------|
| 11. Present ballot draft – basic financial statement       |                    | X                             | February 2012   |
| 12. Discuss proposed concepts statement with FASAB.        | X                  |                               |                 |
| 13. Present pre-ballot draft - proposed concepts statement | X                  |                               | March 2012      |
| 14. Present ballot draft – proposed concepts statement     | X                  |                               | April 2012      |
| 15. Issue ED – basic financial statement                   |                    | X                             | May 2012        |
| 16. Issue ED - concepts statement                          | X                  |                               |                 |

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## **Attachment 2 - Pro Forma Illustrations**

**Attachment 2 – Pro Forma Illustrations – Illustration 1**

Illustration 1 – Overall Perspective Table from FY 2004 Financial Report

| Overall Perspective<br><br>(billions of dollars)               | 2004      |                       |            | 2003      |                       |            | \$ Change  |
|--|-----------|-----------------------|------------|-----------|-----------------------|------------|------------|
|  | Balance   | Additional            | Combined   | Balance   | Additional            | Combined   |            |
|  | Sheet     | Respon-<br>sibilities | Amounts    | Sheet     | Respon-<br>sibilities | Amounts    |            |
| ASSETS   |           |                       |            |           |                       |            |            |
| Inventory, cash  | \$ 359    |                       | \$ 359     | \$ 372    |                       | \$ 372     | \$ (13)    |
| Property, plant & equipment                                    | 653       |                       | 653        | 658       |                       | 658        | (5)        |
| Loans receivable   | 221       |                       | 221        | 221       |                       | 221        | 0          |
| Other  | 165       |                       | 165        | 154       |                       | 154        | 11         |
| Total Assets   | \$ 1,398  |                       | \$ 1,398   | \$ 1,405  |                       | \$1,405    | \$ (7)     |
| LIABILITIES & NET RESPONSIBILITIES                             |           |                       |            |           |                       |            |            |
| Social Insurance   |           |                       |            |           |                       |            |            |
| Medicare (Parts A, B, D)                                       |           | (24,615)              | (24,615)   |           | (15,006)              | (15,006)   | (9,609)    |
| Social Security  |           | (12,552)              | (12,552)   |           | (11,742)              | (11,742)   | (810)      |
| Other (RR Retirement)  |           | (112)                 | (112)      |           | (110)                 | (110)      | (2)        |
| Subtotal, Social Ins.  | 0         | (37,279)              | (37,279)   | 0         | (26,858)              | (26,858)   | (10,421)   |
| Fed. empl. & vets. Pensions/benefits                           | (4,062)   |                       | (4,062)    | (3,880)   |                       | (3,880)    | (182)      |
| Federal debt held by the public                                | (4,329)   |                       | (4,329)    | (3,945)   |                       | (3,945)    | (384)      |
| Other liabilities  | (716)     |                       | (716)      | (675)     |                       | (675)      | (41)       |
| Other responsibilities   |           | (903)                 | (903)      |           | (862)                 | (862)      | (41)       |
| Total Liabilities & Net<br>Responsibilities                    | (\$9,107) | (\$38,182)            | (\$47,289) | (\$8,500) | (\$27,720)            | (\$36,220) | (\$11,069) |
| Total Assets minus Total Liabilities &<br>Net Responsibilities | (\$7,709) | (\$38,182)            | (\$45,891) | (\$7,095) | (\$27,720)            | (\$34,815) | (\$11,076) |



## Illustration 2a – Balance Sheet and Social Insurance Section

| United States Government  |                   |                   |
|---|-------------------|-------------------|
| Balance Sheet and Social Insurance Summary                                | 2008              | 2007              |
| September 30, 2008, and September 30, 2007                                | (billions)        |                   |
| ASSETS  |                   |                   |
| Cash and other monetary assets (Note 2)                                   | \$ 424.5          | \$ 128.0          |
| Accounts and taxes receivable, net (Note 3)                               | 93.0              | 87.8              |
| Loans receivable, net (Note 4)  | 263.4             | 231.9             |
| Inventories and related property, net (Note 5)                            | 289.6             | 277.1             |
| Property, plant, and equipment (Note 6)                                   | 737.7             | 691.1             |
| Securities and investments (Note 7)                                       | 79.6              | 99.8              |
| Investments in govt. sponsored enterprises (Note 8)                       | 7.0               |                   |
| Other assets (Note 9)   | 79.9              | 65.4              |
| <b>Total assets</b>   | <b>\$ 1,974.7</b> | <b>\$ 1,581.1</b> |
| Stewardship Land and Heritage Assets (Note 24)                            |                   |                   |
| LIABILITIES   |                   |                   |
| Accounts payable (Note 10)  | \$ 73.3           | \$ 66.2           |
| Federal debt securities held by the public and accrued interest (Note 11) | 5,836.2           | 5,077.7           |
| Fed. employee and veteran benefits payable (Note 12)                      | 5,318.9           | 4,769.1           |
| Environmental and disposal liabilities (Note 13)                          | 342.8             | 342.0             |
| Benefits due and payable (Note 14)  | 144.4             | 133.7             |
| Insurance program liabilities (Note 15)                                   | 77.8              | 72.7              |
| Loan guarantee liabilities (Note 4)                                       | 72.9              | 69.1              |
| Keepwell payable (Note 8)   | 13.8              |                   |
| Other liabilities (Note 16)   | 298.1             | 256.4             |
| <b>Total liabilities</b>  | <b>12,178.2</b>   | <b>10,786.9</b>   |
| Contingencies (Note 19) and Commitments (Note 20)                         |                   |                   |
| NET POSITION  |                   |                   |
| Earmarked funds (Note 21) (Restated)                                      | 704.6             | 620.2             |
| Non-earmarked funds (Restated)  | (10,908.1)        | (9,826.0)         |
| <b>Total net position</b>   | <b>(10,203.5)</b> | <b>(9,205.8)</b>  |
| <b>Total liabilities and net position</b>                                 | <b>\$ 1,974.7</b> | <b>\$ 1,581.1</b> |
| SOCIAL INSURANCE  |                   |                   |
| Social Security (see Statement of Social Insurance)                       | (\$6,555)         | (\$6,763)         |
| Medicare (see Statement of Social Insurance)                              | (36,311)          | (34,085)          |
| Other social insurance (See Statement of Social Ins.)                     | (104)             | (100)             |
| <b>Total social insurance</b>   | <b>(\$42,970)</b> | <b>(\$40,948)</b> |

## Attachment 2 – Pro Forma Illustrations – Illustration 2b

### Illustration 2b – Balance Sheet and Social Insurance Section with GDP Percentages

| <b>United States Government</b>                                 |  | 2008              |               | 2007              |               |
|---|--|-------------------|---------------|-------------------|---------------|
| <b>Balance Sheet and Social Insurance Summary</b>               |  | Balance           | GDP           | Balance           | GDP           |
| <b>September 30, 2008 and 2007</b>                              |  | Sheet             | %             | Sheet             | %             |
| <b>ASSETS</b>   |  | (billions)        |               |                   |               |
| Cash and other monetary assets (Note 2)                         |  | \$425             |               | \$128             |               |
| Accounts and taxes receivable, net (Note 3)                     |  | 93                |               | 88                |               |
| Loans receivable, net (Note 4)                                  |  | 263               |               | 232               |               |
| Inventories and related property, net (Note 5)                  |  | 290               |               | 277               |               |
| Property, plant, and equipment (Note 6)                         |  | 738               |               | 691               |               |
| Securities and investments (Note 7)                             |  | 80                |               | 100               |               |
| Investments in Government sponsored enterprises (Note 8)        |  | 7                 |               |                   |               |
| Other assets (Note 9)   |  | 80                |               | 65                |               |
| <b>Total assets</b>   |  | <b>\$1,975</b>    | <b>13.7%</b>  | <b>\$1,581</b>    | <b>11.3%</b>  |
| Stewardship Land and Heritage Assets (Note 24)                  |  |                   |               |                   |               |
| <b>LIABILITIES</b>  |  |                   |               |                   |               |
| Accounts payable (Note 10)                                      |  | \$ 73             |               | \$ 66             |               |
| Fed. debt securities held by public & accrued intrst. (Note 11) |  | 5,836             |               | 5,078             |               |
| Federal employee and veteran benefits payable (Note 12)         |  | 5,319             |               | 4,769             |               |
| Environmental and disposal liabilities (Note 13)                |  | 343               |               | 342               |               |
| Benefits due and payable (Note 14)                              |  | 144               |               | 134               |               |
| Insurance program liabilities (Note 15)                         |  | 78                |               | 73                |               |
| Loan guarantee liabilities (Note 4)                             |  | 73                |               | 69                |               |
| Keepwell payable (Note 8)                                       |  | 14                |               |                   |               |
| Other liabilities (Note 16)                                     |  | 298               |               | 256               |               |
| <b>Total liabilities</b>  |  | <b>\$ 12,178</b>  | <b>84.5%</b>  | <b>\$ 10,787</b>  | <b>77.3%</b>  |
| Contingencies (Note 19) and Commitments (Note 20)               |  |                   |               |                   |               |
| <b>NET POSITION</b>   |  |                   |               |                   |               |
| Earmarked funds (Note 21) (Restated)                            |  | 705               |               | 620               |               |
| Non-earmarked funds (Restated)                                  |  | (10,908)          |               | (9,826)           |               |
| <b>Total net position</b>                                       |  | <b>(10,203)</b>   | <b>-70.8%</b> | <b>(9,206)</b>    | <b>-66.0%</b> |
| <b>Total liabilities and net position</b>                       |  | <b>\$1,974</b>    | <b>13.7%</b>  | <b>\$1,581</b>    | <b>11.3%</b>  |
| <b>SOCIAL INSURANCE</b> (see Statement of Social Insurance)*    |  |                   |               |                   |               |
| Social Security   |  | (\$6,555)         | -1%           | (\$6,763)         | -1%           |
| Medicare  |  | (36,311)          | -5%           | (34,085)          | -4%           |
| Other social insurance  |  | (104)             |               | (100)             |               |
| <b>Total social insurance</b>                                   |  | <b>(\$42,970)</b> | <b>-6%</b>    | <b>(\$40,948)</b> | <b>-6%</b>    |

\*Amounts equal estimated present value of projected revenues and expenditures for scheduled benefits over the next 75 years. GDP % represent the percentage of the present value of GDP over the 75 years.

Attachment 2 – Pro Forma Illustrations – Illustration 3

Illustration 3 – The Bob Dacey Table

| Summary of Financial Condition Measures                              |  |                           |   |                      |
|--|--|---------------------------|---|----------------------|
| Assets & Liabilities, Future Receipts & Spending                     |  |                           |   |                      |
|  | <u>Historical Perspective</u><br><u>"Where We Are Now"</u> |                           | <u>Sustainability Perspective</u><br><u>"Where We Are Headed"</u> |                      |
| <b>Resources</b>   | Assets   | \$ 1,975                  | Future Receipts   | \$ XXX               |
| <b>Responsibilities</b>  | Liabilities  | <u>(12,178)</u>           | Future Spending   | <u>YYY</u>           |
|  | Net  |                           | Excess of Future  |                      |
| <b>Net</b>   | Position   | <u><u>\$ (10,203)</u></u> | Spending over Future  |                      |
|  |  |                           | Receipts  | <u><u>\$ ZZZ</u></u> |
| Revenue & Net Cost, Changes in Future Receipts & Spending            |  |                           |   |                      |
|  | <u>Historical Perspective</u><br><u>"Where We Are Now"</u> |                           | <u>Sustainability Perspective</u><br><u>"Where We Are Headed"</u> |                      |
| <b>Resources</b>   | Revenues   | \$ 2,661                  | Changes in Future   |                      |
|  |  |                           | Receipts  | \$ AAA               |
| <b>Responsibilities</b><br>(alternatively –<br>“Resources<br>Used”?) | Net Cost   | <u>(3,670)</u>            | Changes in Future   |                      |
|  |  |                           | Spending  | <u>BBB</u>           |
|  | Net  |                           | Change in Fiscal  |                      |
| <b>Net</b>   | Operating  |                           | Sustainability  |                      |
|  | Cost   | <u><u>\$ (1,009)</u></u>  |   | <u><u>\$ CCC</u></u> |

Attachment 2 – Pro Forma Illustrations – Illustration 4

Illustration 4 – Key Measures Table from Social Insurance<sup>10</sup>

| <b>Table of Key Measures</b>   |  | <b>(billions of dollars)</b> |             |             |
|--|--|------------------------------|-------------|-------------|
| <b>Costs</b>   |  | 2008                         | 2007        | 2006        |
| <b>Net costs</b>   |  | (\$3,641)                    | (\$3,157)   | (\$3,128)   |
| <b>Total taxes and other revenues</b>  |  | 2661.4                       | 2,627       | 2,441       |
| <b>Net operating cost</b>  |  | (\$276)                      | (\$276)     | (\$450)     |
| <b>Net Position</b>  |  | 2008                         | 2007        | 2006        |
| <b>Assets</b>  |  | \$1,975                      | \$1,581     | \$1,497     |
| <b>Less: Liabilities, comprised of</b>   |  |                              |             |             |
| Federal debt held by the public  |  | 5,836                        | 5,078       | 4,868       |
| Federal employee & veterans benefits   |  | 5,319                        | 4,769       | 4,679       |
| Other liabilities  |  | 1,023                        | 940         | 866         |
| <b>Total liabilities</b>   |  | 12,178                       | 10,787      | 10,413      |
| <b>Net position (assets net of liabilities)</b>  |  | (\$10,204)                   | (\$9,206)   | (\$8,916)   |
| <b>Social Insurance Commitments</b>  |  | 2008                         | 2007        | 2006        |
| <b>Net present value (NPV) for current participants (open group), end of fiscal year</b>       |  | (\$42,970)                   | (\$40,948)  | (\$38,851)  |
| <b>Net present value (NPV) for current participants (open group), beginning of fiscal year</b> |  | (40,948)                     | (38,851)    | (35,689)    |
| <b>Decrease (increase) in NPV for open group</b>   |  | (\$2,022)                    | (\$2,097)   | (\$3,162)   |
| <b>Budget Results</b>  |  | 2008                         | 2007        | 2006        |
| <b>Unified Budget Deficit</b>  |  | (\$455)                      | (\$163)     | (\$248)     |
| <b>Spending in Excess of Receipts</b>  |  | 2008                         | 2007        | 2006        |
| <b>Spending in excess of receipts as of January 1 (see Long-Term Projections Statement)</b>    |  | (\$ XX,XXX)                  | (\$ XX,XXX) | (\$ XX,XXX) |

<sup>10</sup> This Table is from the social insurance exposure draft of November 2008, as amended per the Board's subsequent deliberations.

**Attachment 2 – Pro Forma Illustrations – Illustration 5**

**Illustration 5 – Statement of Social Insurance, Summary Section, Dollars Only**

| <b>Social Insurance Summary</b>  | <b>2008</b> | <b>2007</b> | <b>2006</b> | <b>2005</b> | <b>2004</b> | <b>2003</b> |
|--|-------------|-------------|-------------|-------------|-------------|-------------|
| <i>Contributions and Earmarked Taxes from:</i>   |             |             |             |             |             |             |
| Participants who are receiving benefits or are currently eligible  | \$ 1,333    | \$ 1,260    | \$ 1,312    | \$ 1,178    | \$ 1,071    | \$ 774      |
| Participants who have not attained eligibility age or disability   | (12,369)    | (11,608)    | (10,920)    | (10,160)    | (9,430)     | (7,945)     |
| <i>Contributions and Earmarked Taxes</i>   | (11,036)    | (10,348)    | (9,608)     | (8,982)     | (8,359)     | (7,171)     |
| <i>Expenditures for Scheduled Future Benefits for:</i>   |             |             |             |             |             |             |
| Participants who are receiving benefits or are currently eligible  | 29,851      | 28,342      | 27,160      | 25,081      | 23,767      | 20,274      |
| Participants who have not attained eligibility age or disability   | (67,950)    | (63,056)    | (61,699)    | (56,137)    | (52,687)    | (39,961)    |
| <i>Expenditures for Scheduled Future Benefits</i>  | (38,099)    | (34,714)    | (34,539)    | (31,056)    | (28,920)    | (19,687)    |
| <b>Closed group -- Total present value of future expenditures in excess of future revenue for current participants</b> | (49,135)    | (45,062)    | (44,147)    | (40,038)    | (37,279)    | (26,858)    |
| <i>Contributions and Earmarked Taxes from:</i>   |             |             |             |             |             |             |
| Future participants  | 24,743      | 22,828      | 21,227      | 19,442      | 18,457      | 16,715      |
| <i>Expenditures for Scheduled Future Benefits for:</i>   |             |             |             |             |             |             |
| Future participants  | (18,578)    | (18,714)    | (15,933)    | (15,092)    | (14,542)    | (10,683)    |
| <i>Present value of future expenditures in excess of future revenue for future participants</i>                        | 6,165       | 4,114       | 5,294       | 4,350       | 3,915       | 6,032       |
| <b>Open group -- Total present value of future expenditures in excess of future revenue</b>                            | (\$42,970)  | (\$40,948)  | (\$38,853)  | (\$35,688)  | (\$33,364)  | (\$20,826)  |

## Attachment 2 – Pro Forma Illustrations – Illustration 6

Illustration 6 – Statement of Social Insurance, Summary Section, Dollars and GDP Percentages

| <b>Social Insurance Summary</b>   | <b>2008</b> |       | <b>2007</b> |       | <b>2006</b> |       |
|---|-------------|-------|-------------|-------|-------------|-------|
| <i>Participants who have attained eligibility age:</i>  |             |       |             |       |             |       |
| Revenue (e.g., Contributions and earmarked taxes)   | \$ 1,333    | 0.2%  | \$ 1,260    | 0.2%  | \$ 1,312    | 0.2%  |
| Expenditures for scheduled future benefits  | (12,369)    | -1.7% | (11,608)    | -1.7% | (10,920)    | -1.7% |
| Present value of future expenditures in excess of future revenue                              | (11,036)    | -1.6% | (10,348)    | -1.5% | (9,608)     | -1.5% |
| <i>Participants who have attained age 15 up to eligibility age:</i>                           |             |       |             |       |             |       |
| Revenue (e.g., Contributions and earmarked taxes)   | 29,851      | 4.2%  | 28,342      | 4.1%  | 27,160      | 4.2%  |
| Expenditures for scheduled future benefits  | (67,950)    | -9.6% | (63,056)    | -9.2% | (61,699)    | -9.4% |
| Present value of future expenditures in excess of future revenue                              | (38,099)    | -5.4% | (34,714)    | -5.0% | (34,539)    | -5.3% |
| <b>Closed group -- Total present value of future expenditures in excess of future revenue</b> | (49,135)    | -6.9% | (45,062)    | -6.5% | (44,147)    | -6.8% |
| <i>Future participants (under age 15 and births during period):</i>                           |             |       |             |       |             |       |
| Revenue (e.g., Contributions and earmarked taxes)   | 24,743      | 3.5%  | 22,828      | 3.3%  | 21,227      | 3.2%  |
| Expenditures for scheduled future benefits  | (18,578)    | -2.6% | (18,714)    | -2.7% | (15,933)    | -2.4% |
| Present value of future expenditures in excess of future revenue                              | 6,165       | 0.9%  | 4,114       | 0.6%  | 5,294       | 0.8%  |
| <b>Open group -- Total present value of future expenditures in excess of future revenue</b>   | (42,970)    | -6.0% | \$(40,948)  | -6.0% | \$(38,853)  | -5.9% |

## Attachment 2 – Pro Forma Illustrations – Illustration 7

### Illustration 7 – Statement of Social Insurance, Summary Section, GDP Percentages Only

| <b>Social Insurance Summary</b>   | <b>2008</b>  | <b>2007</b>  | <b>2006</b>  | <b>2005</b>  | <b>2004</b>  |
|---|--------------|--------------|--------------|--------------|--------------|
| <i>Participants who have attained eligibility age:</i>  |              |              |              |              |              |
| Revenue (e.g., Contributions and earmarked taxes)   | 0.2%         | 0.2%         | 0.2%         | 0.2%         | 0.2%         |
| Expenditures for scheduled future benefits  | -1.7%        | -1.7%        | -1.7%        | -1.6%        | -1.6%        |
| Present value of future expenditures in excess of future revenue                              | -1.6%        | -1.5%        | -1.5%        | -1.5%        | -1.4%        |
| <i>Participants who have attained age 15 up to eligibility age:</i>                           |              |              |              |              |              |
| Revenue (e.g., Contributions and earmarked taxes)   | 4.2%         | 4.1%         | 4.2%         | 4.1%         | 4.1%         |
| Expenditures for scheduled future benefits  | -9.6%        | -9.2%        | -9.4%        | -9.1%        | -9.1%        |
| Present value of future expenditures in excess of future revenue                              | -5.4%        | -5.0%        | -5.3%        | -5.0%        | -5.0%        |
| <b>Closed group -- Total present value of future expenditures in excess of future revenue</b> | <b>-6.9%</b> | <b>-6.5%</b> | <b>-6.8%</b> | <b>-6.5%</b> | <b>-6.4%</b> |
| <i>Future participants (under age 15 and births during period):</i>                           |              |              |              |              |              |
| Revenue (e.g., Contributions and earmarked taxes)   | 3.5%         | 3.3%         | 3.2%         | 3.1%         | 3.2%         |
| Expenditures for scheduled future benefits  | -2.6%        | -2.7%        | -2.4%        | -2.4%        | -2.5%        |
| Present value of future expenditures in excess of future revenue                              | 0.9%         | 0.6%         | 0.8%         | 0.7%         | 0.7%         |
| <b>Open group -- Total present value of future expenditures in excess of future revenue</b>   | <b>-6.0%</b> | <b>-6.0%</b> | <b>-5.9%</b> | <b>-5.8%</b> | <b>-5.7%</b> |

Illustration 8 – Statement of Changes in Social Insurance Amounts

Statement of Changes in Social Insurance Amounts  
For the Year Ended September 30, 2008

**Open Group**

(in billions of dollars)

|  | Social<br>Security | Medicare<br>HI    | Medicare<br>Parts B &<br>D | Other<br>(e.g., RR<br>Ret.) | Total             |
|--|--------------------|-------------------|----------------------------|-----------------------------|-------------------|
| <b>Net present value (NPV) of future expenditures in excess of future revenue for all participants, beginning of FY 2008</b> | <b>(\$6,763)</b>   | <b>(\$12,292)</b> | <b>(\$21,793)</b>          | <b>(\$100)</b>              | <b>(\$40,948)</b> |
| <b>Reasons for changes in the net present value of future expenditures in excess of future revenue:</b>                      |                    |                   |                            |                             |                   |
| Change in the valuation period   | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Interest on the obligation   | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Changes in demographic data and assumptions  | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Changes in economic data and assumptions   | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Changes in Medicare and other healthcare assumptions   | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Changes in law or policy   | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Changes in methodology and programmatic data   | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Other changes  | XXX                | XXX               | XXX                        | XXX                         | XXX               |
| Subtotal -- change in net present value during period  | 208                | (443)             | (1,783)                    | (4)                         | (2,022)           |
| <b>NPV of future expenditures in excess of future revenue, end of FY 2008</b>  | <b>(\$6,555)</b>   | <b>(\$12,735)</b> | <b>(\$23,576)</b>          | <b>(\$104)</b>              | <b>(\$42,970)</b> |



### **Attachment 3 – Examples of Analyst Presentations**

Example 1: Excerpt from *State of the Union's Finances: A Citizen's Guide*

**MAJOR FISCAL EXPOSURE**

(\$TRILLIONS)

|   | 2000          | 2009          |
|---|---------------|---------------|
| <b>EXPLICIT LIABILITIES</b>                                       | <b>\$6.9</b>  | <b>\$14.1</b> |
| • Publicly-held debt  | 3.4           | 7.6           |
| • Military & civilian pensions & retiree health                   | 2.8           | 5.3           |
| • Other Major Fiscal Exposures                                    | 0.7           | 1.3           |
| <b>COMMITMENTS &amp; CONTINGENCIES</b>                            | <b>0.5</b>    | <b>2.0</b>    |
| • E.g., Pensions Benefit Guaranty Corporation, undelivered orders |               |               |
| <b>SOCIAL INSURANCE PROMISES</b>                                  | <b>13.0</b>   | <b>45.8</b>   |
| • Future Social Security benefits                                 | 3.8           | 7.7           |
| • Future Medicare benefits  | 9.2           | 38.2          |
| • Future Medicare Part A benefits                                 | 2.7           | 13.8          |
| • Future Medicare Part B benefits                                 | 6.5           | 17.2          |
| • Future Medicare Part D benefits                                 | --            | 7.2           |
| <b>TOTAL</b>  | <b>\$20.4</b> | <b>\$61.9</b> |

**NOTE:** Estimates for Medicare and Social Security promises are from the Social Security and Medicare Trustees reports which are as of January 1, 2009 and show unfunded liabilities for the next 75 years. Future promises are discounted to present value based on a real interest rate of 2.9% and CPI growth of 2.8%. The totals above do not include liabilities on the balance sheets of Fannie Mae, Freddie Mac, and the Federal Reserve. Assets of the U.S. government not included. May not add due to rounding.

**SOURCES:** Data from the Department of Treasury, *2009 Financial Report of the United States Government*. Compiled by PGPF.

**Source:** *State of the Union's Finances: A Citizen's Guide*.

Peter G. Peterson Foundation. April 2010.

Example 2: Excerpt from *USA Inc.: A Basic Summary of America's Financial Statements*

## Balance Sheet: USA Inc. Federal Debt + Unfunded Entitlement Liabilities (Social Security + Medicare...) Exceed Stated Assets

|   | F1996           | ... | F2003            | ... | F2009            | F2010            | Comments  |
|---|-----------------|-----|------------------|-----|------------------|------------------|---|
| <b>ASSETS (\$B)</b>                         |                 |     |                  |     |                  |                  |   |
| Cash & Other Monetary Assets                | \$193           |     | \$120            |     | \$393            | \$429            | \$200B cash balance owing to temporary Fed market stabilization initiatives                             |
| Accounts / Loans / Taxes Receivable         | 206             |     | 278              |     | 626              | 783              |   |
| Inventories                                 | 232             |     | 241              |     | 285              | 286              |   |
| Property, Plant & Equipment                 | 969             |     | 658              |     | 784              | 829              |   |
| TARP + GSE Investments                      | --              |     | --               |     | 304              | 254              | Includes \$145B TARP direct loans & equity investment + \$109B in GSEs                                  |
| Other assets                                | 124             |     | 97               |     | 275              | 303              |   |
| <b>Total Assets (\$B)</b>                   | <b>1,724</b>    |     | <b>1,394</b>     |     | <b>2,668</b>     | <b>2,884</b>     | Growth primarily owing to TARP capitalization + Fed liquidity program                                   |
| <b>Y/Y Growth</b>                           | <b>33%</b>      |     | <b>40%</b>       |     | <b>35%</b>       | <b>8%</b>        |   |
| <b>LIABILITIES (\$B)</b>                    |                 |     |                  |     |                  |                  |   |
| Accounts Payable                            | \$162           |     | \$62             |     | \$73             | \$73             | Significant rise in debt owing to on-going budget deficits + stimulus spending                          |
| Accrued Payroll & Benefits                  | --              |     | 100              |     | 161              | 164              |   |
| Federal Debt                                | 3,730           |     | 3,945            |     | 7,583            | 9,060            | Federal employee & veteran benefits rose 3x owing to scheduled annual pay raises + rising benefit costs |
| Federal Employee & Veteran Benefits Payat   | 1,652           |     | 3,880            |     | 5,284            | 5,720            |   |
| Liability to GSEs                           | --              |     | --               |     | 92               | 360              |   |
| Other Liabilities                           | 530             |     | 512              |     | 932              | 979              |   |
| <b>Unfunded Net Entitlement Liabilities</b> | <b>5,415</b>    |     | <b>20,825</b>    |     | <b>45,878</b>    | <b>30,857</b>    | Unfunded entitlement liabilities up 6x between F1996 and F2010.   |
| <b>Y/Y Growth</b>                           | <b>--</b>       |     | <b>16%</b>       |     | <b>7%</b>        | <b>-33%</b>      |   |
| NPV of Unfunded Social Security             | \$3,600         |     | \$4,927          |     | \$7,677          | \$7,947          | Medicare NPV down sharply Y/Y owing to new assumptions from the Healthcare reform legislation           |
| NPV of Unfunded Medicare                    | 1,815           |     | 15,819           |     | 38,107           | 22,813           |   |
| NPV of Unfunded Other Benefits              | --              |     | 79               |     | 94               | 97               |   |
| <b>Total Liabilities (\$B)</b>              | <b>11,488</b>   |     | <b>29,324</b>    |     | <b>60,002</b>    | <b>47,214</b>    | Significant increase from rising levels of debt + unfunded future benefits                              |
| <b>Y/Y Growth</b>                           | <b>--</b>       |     | <b>14%</b>       |     | <b>9%</b>        | <b>-21%</b>      |   |
| <b>NET WORTH (\$B)</b>                      | <b>-\$9,764</b> |     | <b>-\$27,930</b> |     | <b>-\$57,334</b> | <b>-\$44,330</b> | -\$44T of net worth for USA Inc. more than tripled, from -\$10T in 1996                                 |
| <b>Y/Y Growth</b>                           | <b>--</b>       |     | <b>13%</b>       |     | <b>8%</b>        | <b>-23%</b>      |   |

Note: USA Inc.'s balance sheet presented here does not include the financial value of the Government's sovereign powers to tax, regulate commerce, and set monetary policy. It also excludes its control over nonoperational resources, including national and natural resources, for which the Government is a steward. Total liabilities include the net present value (NPV) of unfunded entitlement liabilities like Social Security / Medicare / other payments, which the Treasury Dept. considers 'off-balance sheet' responsibilities. U.S. government fiscal year ends in September. Source: U.S. Department of the Treasury, Financial Report on the U.S. Government, 1996 – 2010.



www.kpcb.com

USA Inc. | Balance Sheet Drilldown 210

Source: USA Inc.: A Basic Summary of America's Financial Statements. February 2011. [www.kpcb.com/usainc](http://www.kpcb.com/usainc)

## Attachment 3: Examples of Analyst Presentations

### Example 3: YouTube Broadcast

**\$78.8 Trillion; United States Debt Obligations exceed world GDP; Monetary Collapse Looming?**



Source: <http://www.youtube.com/watch?v=oVOuCDqSrR8&feature=related>. Accessed April 12, 2011

Example 4: Excerpt from *Financial State of the Union*, KStone Partners, LLC

| <b>U.S. Government's Financial Position<br/>as of September 30, 2008 <sup>(1)</sup></b> |                   |
|---|-------------------|
| <small>(Amounts in Billions of Dollars)</small>   |                   |
| <b>Assets</b>   |                   |
| Cash  | \$ 425            |
| Property, plant & equipment   | 738               |
| Other   | 812               |
| <b>Total Assets</b>   | <b>1,975</b>      |
| <b>Liabilities</b>  |                   |
| Federal debt securities held by the<br>public and accrued interest                      | (5,836)           |
| Federal employee/veterans benefits  | (5,319)           |
| Other   | (1,023)           |
| <b>Total Liabilities</b>  | <b>(12,178)</b>   |
| Net Liability ("Net Position")  | <b>(10,203)</b>   |
| <b>Present Value of Social Insurance<br/>Programs (Closed Group) <sup>(2)</sup></b>     |                   |
| Social Security   | (17,188)          |
| Medicare — Part A   | (13,590)          |
| Part B  | (12,615)          |
| Part D  | (5,605)           |
| Subtotal — Medicare   | (31,810)          |
| Railroad Retirement & Black Lung  | (137)             |
| <b>Total Social Insurance Commitments</b>   | <b>(49,135)</b>   |
| <b>Total Net Liability</b>  | <b>(\$59,338)</b> |
| <small>See footnotes on page 5</small>  |                   |

Source: Financial State of the Union. Found at  
<http://www.kstonepartners.com/secondary.asp?id=45>.  
 Accessed April 11, 2011.

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**Attachment 4: Board Member Email: Possible Reporting Model Project on  
Improving Display Understandability and Usefulness**

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Attachment 4: Board Member Email: Possible Reporting Model Project on Improving Display Understandability and Usefulness

**From:** Tom Allen  
**Sent:** Thursday, April 14, 2011 8:50 PM  
**To:** Simms, Ross E  
**Cc:** Payne, Wendolyn M  
**Subject:** Possible Reporting Model Project on Improving Display Understandability and Usefulness

Ross and Wendy

I mentioned that my preparation for congressional testimony about the value of financial reporting resulted in some thoughts about improving the understandability of our financial statements. I am sorry this has taken so long for me to get to you. I hope you can include this email in the reporting model project papers you will be sending out tomorrow as I would like to see if a majority of board members would like to explore looking at this issue as part of the reporting model project.

I was quite surprised that the reporting model task force recommendations primarily focused on improving the distribution of the financial information rather than starting with focusing on making sure when someone got the information they could clearly understand what it meant. Particularly in terms of the financial position of the federal government improving or deteriorating during the reported fiscal year. I think there is a broad understanding of citizens that answering that question is the primary purpose of audited financial statements for companies, not-for-profits, and governments. I will admit that the scope and nature of the federal government makes it the most difficult to clearly convey the above information but I think the collective skills of the board and staff members can do a better job of this if the board decides this is a project worth tackling. I also understand the task force comments that they wanted to recommend things that could be done quickly which probably precludes changing presentation and their belief that as long as users could drill down, they could answer their own questions. I see such a lack of understanding in the written and verbal comments of citizens, government officials and elected officials that I think FASAB has an obligation to answer the above question clearly on the face of the financial statements so that it can't be misunderstood. Then people can answer any detailed questions they want about the past year and make any comments they want about future years projections as that isn't the responsibility of FASAB.

My approach to the subcommittee [House Committee on Oversight and Government Reform Subcommittee on Government Organization, Efficiency, and Financial Management] request to comment was to look at financial statements published 10 years earlier and show their value in projecting where the organization (in this case federal government) was heading. When I have taught beginning accounting classes, I have always said, that was the value of accrual financial statements over cash basis reporting. And this is also what we told state and local governments at GASB as we proposed full accrual reporting back in the 90's to them. While I had never looked at the 2000 CFR, it turned out it was the last surplus year and I found that the financial statements told a somewhat different story than some of the underlying MD&A, footnotes, and other comments. The \$223 billion budget surplus and \$46 billion accrual based surplus seemed at odds with comments like, "during the 3 surplus years from 1998-2000 the debt subject to the debt limit had increased \$152.2 billion." The auditor's comments that the country was on an unsustainable path seemed at odds with projections of budget surplus in all future years. I couldn't find information on the change in social insurance commitments during 2000 but it grew just under \$4 trillion from 2000 to 2001. I acknowledged to the subcommittee that one may be left wondering how the financial position of the federal government changed during fiscal 2000.

Actually fiscal year 2000 can be explained in a way that all citizens would understand. The simple explanation that social security and medicare tax payments received were more than what was paid out in fiscal year 2000 and, after taking into account all other revenues and expenses of the government during the year, resulted in an accrual surplus of \$46 billion. The \$223 billion budget surplus also resulted from social security and medicare dedicated collections in excess of cash payments during the year for these programs. This is different than the accrual financial statement amount because the budget is

Attachment 4: Board Member Email: Possible Reporting Model Project on Improving Display Understandability and Usefulness

primarily on a cash basis and doesn't recognize amounts to be paid in the future such as employee retirement benefits or veteran care costs that are accrued as they are incurred in accrual based statements.

The other part of the answer to communicating clearly the change in the government's financial position is the growing social insurance commitments which the board decided to deal with in their long term projection reporting. But the board did say at that time that they would look to see how to better explain the impact of growing social insurance commitments in the financial reporting model project. Most troubling to me is the issue of showing an accrual based surplus which resulted from social insurance dedicated collections which were "loaned" to the government. This borrowing is recognized by Congress as borrowing that counts toward the debt limit. And, it results in the issuance of treasury securities. Maybe this is what OMB Director Jacob Lew was referring to in February when he said something about the use of social insurance money masking the growing deficit.

Working on the reporting model project for many years at GASB made me a believer in using two columns to present financial information that was dissimilar and would lose clarity by blending it all together in a single column. FASB came to a similar conclusion in the 90's as they were working on not-for-profit reporting. I believe the use of a 2 column statement (both for the operating statement and statement of financial position) where dedicated collections are reported in 1 column and the rest of government is reported in another would provide the framework to show clearly the impact borrowings or repayments are having on the financial position of the federal government. Borrowings would be shown as borrowings not as revenue, and repayments would be shown as such rather than as expenditures. In the future, Congress will be making adjustments to social insurance expenditures and revenues and a two column financial statement would more accurately reflect the way proposals for change are being communicated to taxpayers. Also, it more clearly reflects the expectations of taxpayers who calculate 2 very different taxes on their tax returns. As a side note, this would also eliminate the need for the earmarked funds project and accomplish the goals of the project in a much clearer fashion.

I know some have argued that it is all just revenue to the government but I have never seen that explanation ever made by an elected official to taxpayers. And, I would say that position is very inconsistent with adding to the debt amount and the issuance of treasury securities. Again Ross I'm sorry for the lateness of this email and I look forward to your and board member comments at the next meeting.

Tom Allen