Federal Accounting Standards Advisory Board

November 20, 2007

Memorandum

To: Members of the Board

From: Melissa L. Loughan

Through: Wendy M. Payne, Executive Director

Subj: **Federal Entity—TAB B**[1]

At the September Board meeting, the Board approved three general principles that would be relied upon in establishing the boundaries of the federal reporting entity. The broad principles are the federal reporting entity includes all organizations that:

- the federal government is directly financially accountable for or owns;
- the federal government exercises control over; or
- the nature and significance of their relationships with the federal government are such that the exclusion would cause the government's financial statements to be misleading or incomplete.

Staff has continued developing the outline paper on the boundaries of the reporting entity. The paper now includes specific, detailed criteria for each of the broad areas identified as well as an expanded introduction that includes a discussion of component reporting entities. The Board materials for the December meeting includes the outline paper as well as an Appendix with reference materials presented at previous Board meetings.

The goal for the December Board meeting will be to obtain the Board's feedback on the criteria and other aspects of the outline paper. Specifically, staff requests the Board's input on the following questions which are included in the outline paper (see page numbers noted):

- Does the Board agree with the Introduction? (page7)
- Are there additional areas that should be covered in the Introduction? (page 7)
- Does the Board agree with the basic premises of the Statement? (page 9)
- Does the Board wish to suggest additional premises? (page 9)

[1] 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.

- Does the Board agree with expanding financially accountable to include ownership? (page 11)

- Does the Board have additional comments on the financially accountable general principle or the narrative? (page 11)

- Does the Board agree with the definition and discussion of control? (page 16)

- Does the Board agree with the discussion and indicators noted for determining whether control exists? (page 16)

- Does the Board agree with the discussion and examples of situations of where control does not exist? (page 16)

- Does the Board have additional comments on the control general principle or the narrative? (page 16)

- Does the Board agree with including this third general principle and the areas noted? (page 18)

- Does the Board wish to offer other possible areas that should be considered in this area? (page 18)

- Does the Board agree with the exceptions noted? (page 19)

- Does the Board wish to offer other possible exceptions that should be considered? (page 19)

- Would the Board like to suggest other possible unique relationships or organizations that should be considered? (page 24)

- Does the Board have initial thoughts on whether these should be incorporated into the standard or perhaps as an Appendix--Case Studies? Should each type be looked at separately to determine if it is part of the federal reporting entity and if not, what disclosures (if any) would be appropriate? (page 24)

Based on the feedback from the Board, staff will revise the outline paper to incorporate suggested changes. Staff also plans to continue researching the quasi government / hybrid organizations that will be considered in the project. Staff also plans to move forward by forming a task force to share the outline paper for comment. The task force will include members from the CFO, OIG, and IPA as well as specific representatives from quasi government / hybrid organizations (such as FFRDCs), and intelligence agencies because of their unique nature.

Please feel free to contact me at 202-512-5976 or by email at loughanm@fasab.gov to discuss any comments or questions you may have.

OUTLINE
Proposed Standards
The Reporting Entity and Consolidation

Introduction

Defining the boundaries for each reporting entity is very important in financial reporting. Most would agree that accounting information pertains to entities and entities use financial reports to communicate information to people concerned or interested in the entity. Therefore, the primary reason for defining the reporting entity is to ensure that users of general purpose federal financial reports (GPFFR) will be provided with complete financial information about the entity and its involvements.

Clearly defining the boundaries of the reporting entity enables users to understand the organizations encompassed by the entity. The structure of the federal government has become increasingly complex and, as such, it is important to identify components and organizations that would be consolidated in the GPFFR of the U.S. government and in each component entity's financial statements.

Reporting on a consolidated basis aggregates the individual financial statements of organizations comprising a reporting entity. Consolidation is a method of accounting that combines the accounts of those organizations on a uniform basis of accounting and eliminates balances and transactions among the organizations.

Consolidation highlights that although the federal government and its component entities and other organizations may be separate legal entities, together they make up a single economic entity. The ultimate aggregation of entities is into the entire federal government reporting entity--which in reality is the only independent economic entity. Although many component entities prepare their own financial statements, individually those financial statements provide a partial or fragmented view of the federal government. Without a consolidated statement for the entire federal government, it is impossible to get a complete picture of its financial position and operations. A complete and consolidated statement of the federal government allows for sound decision-making and accountability.

At the component entity level, the reporting entity concept is important to both internal and external users. Clearly defining the reporting entity allows government officials to monitor activities undertaken by diverse component entities. Users can make the best use of the information when it is clear what is included and what is excluded from GPFFRs. Identifying the entities for inclusion in the federal government's financial statements is critical to creating transparent reports to support accountability. As a democracy, elected officials are to be held accountable to the public and financial statements provide a means of doing so.[1] In order to achieve accountability, the content and structure of the GPFFR should be clear, complete and comprehensible to citizens.

Organization of the Federal Government

The federal government is an extremely complex organization. Although there are other perspectives[2], such as a budget perspective, in understanding the composition of the federal government, an organizationally based approach appears most appropriate in defining reporting entities for GPFFRs. This approach supports accountability in organizations and sub-organizations. An organizationally based approach in defining reporting entities provides accountability because there is a management responsible for controlling and deploying resources, producing outputs and outcomes and thereby would be accountable. In addition, the scope with an organizational approach would provide meaningful financial statements and there would likely be users of them.

The fundamental organization of the U.S. federal government is established by the Constitution. At the highest level, the U.S. federal government is composed of the executive, legislative, and judicial branches. Within each branch are many different organizations that manage resources and are responsible for operations. These include departments and major agencies, which are generally divided into smaller organizational units with a wide variety of titles including bureaus, administrations, corporations, boards and commissions. Many of these are further divided into even smaller organizations. On the other hand, there are small agencies for which division

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[1] SFFAC 1, par. 74

[2] SFFAC 2, par. 13-28 discusses the budget and program perspective of the federal government, as well as the intertwining of the perspectives.

into smaller organizations or units is generally not necessary or appropriate. Additionally, there are many other types of organizations that must be considered when establishing the boundaries of the U.S. federal government and its component entities for GPFFR purposes. In addition to the departments, major agencies, and smaller organizational units of the three branches of the federal government, there are other types of organizations that should be considered. These include government sponsored enterprises, federally funded research and development centers, public-private partnerships, special purpose entities, joint ventures, and other quasi-governmental organizations. To ensure consistency in federal financial reporting, it is important to identify the types of organizations that should be considered, as well as the organizational structure of the government entities.

Defining Reporting Entities

As noted, the primary reason for defining reporting entities is to ensure that users of GPFFR are provided with complete financial information about the reporting entity and its involvements. Other reasons for understanding what the reporting entity entails include:

- Ensure that for the aggregation of information at each reporting level no organization is omitted and to provide for consolidations and/or combinations of information from reporting units at the same level, as appropriate;

- Assist in making comparisons among comparable reporting entities by reducing the possibility of unintended or arbitrary exclusions or inclusions of organizations;

- Assist in making comparisons among alternative ways to provide similar services or products;

- Facilitate evaluating performance, responsibility, and control, especially where one agency is the provider or recipient of services attributable to or financed by another agency.

Reporting Entity

A reporting entity is an entity that issues GPFFR. It issues reports because

1. There is a statutory or administrative requirement to prepare stand alone financial statements; or

2. It chooses to prepare stand alone financial statements because of one or more of the following characteristics:
    a. it is reasonable to expect there are users of the GPFFR that would benefit
    b. the scope would provide a meaningful representation and demonstrate accountability
    c. it would be helpful for managing government operations and there is a management responsible for controlling and deploying resources

Reporting entities in the federal government include the federal reporting entity and its components, component reporting entities.

Federal Reporting Entity

The federal reporting entity is the largest reporting entity in the federal government. The federal reporting entity encompasses all the organizations existing within the federal government, which is the executive, legislative and judicial branches. The federal reporting entity is made up of the component reporting entities and entities not reporting. Meaning, the federal reporting entity is the consolidation (net of eliminations) of the component reporting entities and entities not reporting. For purposes of GPFFR, the federal reporting entity also may include other types of organizations.

Component Reporting Entities

A component reporting entity is an entity[3] within the federal government that issues GPFFR. Component reporting entity is used broadly to refer to reporting entities within the federal government that prepare GPFFR. Examples of component reporting entities include executive departments, most independent agencies, and government corporations.

Component reporting entities would also include sub-components (organizations that are part of a larger entity) that prepare GPFFR. Often financial statements that present aggregations of information for organizations such as an administration or a bureau are more useful than statements at the higher component level. Such statements can provide a better understanding of the financial results and status of the many individual organizations and programs constituting a department or major agency. Therefore, sub-components often will prepare financial statements. An example may include a bureau of a larger department that prepares stand alone financial statements. Other examples may include commercial functions, revolving funds, and/or other accounts for which financial statements will be prepared.

Entities Not Reporting

Inevitably there are certain entities at all tiers of the federal government (component and sub-component) that do not issue GPFFR. For example, certain components of the judicial and legislative branches do not report and are not compelled to do so. In addition, certain sub-components may choose not to issue GPFFR although other sub-components within a component do so. However, although the entities may not issue their own stand-alone financial statements, the entities should provide the necessary information to ensure the larger reporting entity and ultimately the federal reporting entity are complete.

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[3] The term “entity” is a general term used to refer to any legal, administrative or organizational structure or unit.

Boundaries of the Reporting Entity

Clearly defining the boundaries of a reporting entity ensures that the financial statements contain all the information essential for fair presentation of the financial position and results of operations of the reporting entity and excludes information that would not result in fair presentation. Defining the boundaries also ensures consistency and completeness in what reporting entities encompass.

Assessing whether an entity should be included within a reporting entity is often difficult and requires the exercise of professional judgment and the consideration of many factors and indicative characteristics.

The boundaries of the reporting entity and therefore what should be included in consolidated financial statements are critical because the decision whether to include or exclude organizations can impact the financial statements and the picture they provide to users. In fact, some would consider establishing the boundaries of the reporting entity (and what's included in the consolidated financial statements) as much an impact on the federal government's financial reporting as any other issue.

Determining the boundaries of the reporting entity helps to identify which organizations will be encompassed by the reporting entity's GPFFR. While drawing the boundaries may be difficult, it provides an opportunity to identify federal organizations and sharpen the focus on the activities and relationships in which the federal government actively participates.

The federal reporting entity includes all organizations within the three branches of the federal government. The federal reporting entity also includes all organizations that

- the federal government is directly financially accountable for or owns;
- the federal government exercises control over; or
- the nature and significance of their relationships with the federal government are such that the exclusion would cause the government's financial statements to be misleading or incomplete.

Likewise, a component reporting entity includes all organizations that

- the component is directly financially accountable for or owns;
- the component exercises control over; or
- the nature and significance of their relationships with the component are such that the exclusion would cause the component's financial statements to be misleading or incomplete.

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

Staff believes it is important to include some discussion of the organization of the federal government, reporting entities, federal reporting entity, component reporting entities, and entities not reporting in the Introduction. The discussion is much more conceptual and does not appear to fit within the body of the standard.

Does the Board agree with the Introduction?

Are there additional areas that should be covered in the Introduction?

BASIC PREMISES FOR THE STATEMENT

- Does not prescribe specifics of which organizations are in or out, instead provides general principles and criteria for each.

The purpose of this Statement is to provide criteria and guidance as to what would be encompassed in a federal reporting entity by clearly defining the boundaries of the reporting entity. This Statement presents a principles-based approach to determining which organizations should be included in the reporting entity because of the wide and varying relationships of the federal government. This Statement does not try to define which reporting entities must prepare and issue financial statements. That authority and responsibility resides with Congress and the heads of organizations within the three branches of the federal government.

- Substance of the relationship is determining factor, regardless of legal form of relationship.

In applying the criteria in this Statement, it is necessary to determine the substance of the relationship between the federal government and organizations that are not within the three branches of the federal government. The nature of certain relationships may not be completely reflected by their legal form. While some organizations may have a certain legal form, it is important not to allow the form to cloud the determination of whether an organization is included or excluded from the reporting entity. The use of professional judgment is required to determine if an organization should be included in the reporting entity.

- Decisions are made at the reporting date based on legislative framework regardless of federal government's ability to change it in the future.

The determination of whether an organization is within the boundaries of the reporting entity is based on conditions (legislation) that exist at the reporting date, because accrual-basis financial statements are based on transactions or events that already have occurred. Therefore, the power of the federal government to subsequently change those conditions and thus change the nature of its relationship with an organization in the future, does not change the boundary of the reporting entity at the reporting date.

- References to reporting entity include the federal reporting entity and its component reporting entities as the boundaries are the same.

As noted, the general principles defining the boundaries for the federal reporting entity and the component reporting entities are the same. Throughout this Statement, the term reporting entity would include both the federal reporting entity and component reporting entities.

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

Staff believes it is important to set out high level premises for the Statement.

Does the Board agree with the basic premises of the Statement?

Does the Board wish to suggest additional premises?

Standards

The reporting entity should comprise the organizations that it is directly financially accountable for or owns.

The reporting entity should naturally include all the organizations for which it is directly financially accountable. Evidence that the reporting entity would be directly financially accountable for an organization includes the following:

- The organization appears in the President's budget and/or
- The organization is owned by the reporting entity.

SFFAC 1, *Objectives of Federal Financial Reporting,* provides the Budgetary Integrity Objective that includes "Federal financial reporting should assist in fulfilling the government's duty to be publicly accountable for monies raised…" A reporting entity is financially accountable for all organizations encompassed in its budgetary reporting requirements. It would include all organizations that are in the President's budget because they directly receive federal funding through legislation.

This boundary is perhaps one of the most straight-forward as users are interested in the government's accountability for those funds and specifically, knowing how efficiently the policies of the federal government were carried out with respect to the resources entrusted to it. Therefore, an organization that is included in the *Budget of the United States Government Analytical Perspectives* section currently entitled *Federal Programs by Agency and Account* should be considered part of the federal reporting entity, as well as part of the component entity with which it appears. However, an appropriation to a federal entity that finances a subsidy to a non-federal entity would not necessitate inclusion of the non-federal entity because the non-federal entity is not directly responsible for meeting budgetary reporting requirements.

Financially accountable would also include organizations that are owned by the reporting entity, particularly if the ownership is of the organization and not just the property. Ownership includes ownership created under any arrangement and is therefore not restricted to relationships that arise solely through legal ownership. Ownership is also established by considering who is at risk if the organization fails, or identifying for whom the organization’s employees work.

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

Staff has expanded the financially accountable general principle to also include ownership. Some standard setters view ownership and financially accountable as a form of control. Although staff does agree that it can be a form of control, staff believes that financially accountable and ownership should be assessed separately. This approach first looks at the budgetary responsibility and ownership. For example, this would be a defendable approach to including the judicial branch in the federal reporting entity, as it would be more appropriate than saying it is controlled.

Does the Board agree with expanding financially accountable to include ownership?

Does the Board have additional comments on the financially accountable general principle or the narrative?

The reporting entity should comprise the organizations it exercises control over.

For purposes of this standard, control is defined in terms of the relationship between the reporting entity and another organization (the controlled organization). Whether the reporting entity controls an organization is a question that must be determined by reference to the definition of control established in this standard. This determination will require the application of professional judgment. Additionally, along with the substance of the relationship in each case, there are certain indicators of control that should be considered in determining whether the reporting entity controls an organization.

Control

For purposes of defining the boundaries of the reporting entity, control is the power to govern the financial and operating policies of another organization with expected benefits (or the risk of loss) to the reporting entity from the other organization's activities.

Control must be assessed at the reporting date regardless of the reporting entity's ability to change it in the future. In determining if control exists, it is necessary to determine the substance of the relationship between the reporting entity and the organization as it may not be completely reflected by their legal form.

As noted, the ability to govern the financial and operating policies is an important element of federal government control. There are a variety of ways that the federal government governs the financial and operating policies of an organization, such as:

- The federal government establishes the organization's fundamental purpose and limits the ability of the organization to make future changes;
- The federal government directs the financial and operating policies on an on-going basis; or
- The federal government has authority to veto or modify the financial and operating policies established by an organization.

Control does not require the federal government to have responsibility for the management of the day-to-day operations of the other organization. It is the federal government's authority to determine the policies governing those activities that indicates control. All relevant aspects and implications of each relationship would be considered in determining whether or not control exists.

It is assumed that where the federal government has the power to govern the financial and operating policies of an organization, it expects to receive a financial or non-financial benefit and/or be exposed to the risk of loss.

Determining Whether Control Exists

Determining whether control exists will require the application of professional judgment. The federal government achieves its objectives through a wide range of organizations which individually will fall somewhere along a continuum. At one end of the continuum, it will be clear that an organization does not have the power to act independently and is controlled by the federal government. At the other end, the organization will have the power to act independently and, while the federal government may have a level of influence on the organization, it will be clear that it does not have control. Along the continuum, consideration needs to be given to the nature of the relationship between the federal government and the organization in order to determine whether control exists.

As noted, determining whether the federal government controls another organization requires the application of professional judgment and a careful consideration of the surrounding facts and circumstances, the substance of the relationship and the definition of control. There are certain indicators of control that should be considered in determining whether the federal government controls an organization. These indicators provide strong evidence of control, however; the absence of one of these specific indicators does not lead to a presumption that control is not present. The assessment of whether control exists should include consideration of all the facts and circumstances of a particular relationship.

There are certain indicators that provide more persuasive evidence of control. Control generally exists when the federal government:

- Has the authority to unilaterally appoint or remove a majority of the governing board members of another organization;
- Has the authority to govern or direct the governing body on the financial and operating policies of the organization or holds a voting majority that allows it to govern the financial and operating policies of the organization;
- Has ongoing access to another organization's assets or has the ability to direct the ongoing use of those assets, or has ongoing responsibility for losses; and
- Has the authority to unilaterally dissolve the organization thereby having access to the assets and responsibility for the obligations.

Other indicators that provide evidence that control exists when the federal government has the power to:

- Provide significant input into the appointment of members of the governing body of the organization or being involved in the appointment or removal of a significant number of members;
- Appoint or remove key executives or personnel;
- Establish or amend the organization's mission;
- Approve the budgets or business plans for the organization;
- Establish limits or restrictions on borrowing and investments of the organization;
- Ability to veto, overrule, or modify governing board decisions or otherwise significantly influence normal operations;
- Restrict the capacity to generate revenue of the organization, especially the sources of revenue;
- Require audits and preparation of other financial reports; and
- Establish or amend management policies.

For each indicator that applies in a particular circumstance, the degree of federal government influence would determine its importance as evidence of control. In weighing the evidence, it would be necessary to consider the indicators collectively as well as individually. The degree of importance of the indicators of control, further depends on the particular circumstances in each case. In some situations, a particular indicator may provide a high degree of evidence of control whereas, in other situations, the importance of the same indicator may not be as significant.

Situations Where Control Does Not Exist

Much of the focus of the reporting entity standard is on control and determining whether it exists. It is also important to distinguish what doesn't constitute control. Control would not be inferred from:

- Regulatory powers;
- Constitutional responsibility; or
- Purchase power.

The federal government has the power to regulate the behavior of many organizations by use of its sovereign and legislative powers. The federal government has the power to regulate the behavior of many organizations by imposing conditions or sanctions on their operations. However, the governing bodies of the regulated organizations make decisions within the regulatory framework. Regulatory powers do not constitute control for purposes of defining the boundaries of the reporting entity because the government's interest in these organizations extends only to the regulatory aspects of the operations.

Control does not stem simply from the federal government's constitutional responsibility for a certain activity. When the federal government has constitutional responsibility for a certain activity, it does not mean the federal government controls all the organizations performing such activities. The nature of the relationship between the federal government and the organization performing the activity is the determining factor.

Purchase power does not constitute control for purposes of defining the boundaries of the reporting entity. Additionally, certain organizations may be economically dependent on the federal government but ultimately retain discretion as to whether it will accept funding or do business with the federal government. For example, many not-for-profits rely on the federal government funding but that does not mean they are controlled by the federal government. Although the federal government may be able to influence the organization which is dependent on its funding or business through purchase power, the federal government does not govern the organization's financial and operating policies. Therefore, purchase power does not constitute control for purposes of defining the boundaries of the reporting entity.

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

The discussion of control is one of the biggest areas of the standard and one of the most difficult to apply as it involves much professional judgment. Staff attempted to stress this throughout. Staff used SFFAC 2 discussion of indicators as a starting point. Staff also performed a thorough review of other standard setters discussion of control—definition and indicators. The approach selected is most similar with that of the IPSASB and the PSAB of CICA while it is still consistent with other standard setters. However, it should be noted that most of the other standard setters have an active project on the reporting entity which includes a focus on control.

Does the Board agree with the definition and discussion of control?

Does the Board agree with the discussion and indicators noted for determining whether control exists?

Does the Board agree with the discussion and examples of situations of where control does not exist?

Does the Board have additional comments on the control general principle or the narrative?

The reporting entity should comprise the organizations for which the nature and significance of their relationships with the federal government are such that the exclusion would cause the government's financial statements to be misleading or incomplete.

There are instances where organizations may not meet either of the first two broad characteristics listed above, yet the nature and significance of the relationship is such that excluding them would make the GPFFR misleading or incomplete. For example, there may be instances when, for political or other reasons, an organization is not listed in the "Federal Programs by Agency and Account" and it may be difficult to provide sufficient evidence the federal government controls the organization, yet the GPFFR would be misleading or incomplete if they were excluded.

Criteria for determining whether an organization not listed in the "Federal Programs by Agency and Account" and not controlled by the federal government is nevertheless part of the reporting entity are as follows:

- TBD by working with task force, possibilities

- The organization is an integral part of the federal government's exercise of its sovereign power to carry out federal functions. Evidence of sovereign powers are the power to collect compulsory payments, e.g., taxes, fines, or other compulsory assessments; use police powers; conduct negotiations involving the interests of the United States with other nations; or borrow funds for government use.

- The organization carries out federal missions and objectives.

- The organization determines the outcome or disposition of matters affecting the recipients of services that the federal government provides.

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

Staff notes that there are instances where organizations may not meet either of the first two broad characteristics listed above, yet the nature and significance of the relationship is such that excluding them would make the GPFFR misleading or incomplete. Staff believes the task force may be helpful in identifying other potential areas. The areas included above are consistent with SFFAC 2.

Does the Board agree with including this third general principle and the areas noted?

Does the Board wish to offer other possible areas that should be considered in this area?

EXCLUSIONS –There are certain situations where organizations meeting the broad principles and criteria would be excluded from the reporting entity. Organizations would be excluded in the following situations:

- *Temporary existence of one of the above criteria.* Organizations should be excluded if one of the conditions or criteria is for the short-term or temporary. Meaning, organizations should only be included in the reporting entity when the criteria being met, is likely to remain in existence for a time, it is more than fleeting. For example, the federal government may have temporary control of an organization with no plan of continuing but instead plans to relinquish control.

- *Severe restrictions that prevent the federal government from controlling.* The federal government may be subject to severe restrictions that may prevent it from truly controlling or benefiting from the relationship or activity.

- *The organizations and functions pertain to monetary policy.* In the United States, the organization and functions pertaining to monetary policy are traditionally separated from and independent of the other central government organizations and functions in order to achieve more effective monetary and fiscal policies and economic results. For example, the Federal Reserve System would not be considered part of the federal reporting entity.

- *Others….TBD after task force meeting and sharing of draft paper.*

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

Staff notes that there are exceptions to principles and criteria. Staff believes the task force may be helpful in identifying other potential exceptions. The exceptions included above are consistent with SFFAC 2 and the majority of other standard setters.

Does the Board agree with the exceptions noted?

Does the Board wish to offer other possible exceptions that should be considered?

Federal Government’s Unique Relationships (Quasi Government / Hybrid Organizations)

In recent years, the federal government has increased the use of hybrid organizations for the implementation of public policy. These hybrid organizations are federally related entities that possess legal characteristics of both the governmental and private sectors. The federal government’s use of these unique, “quasi government “or “hybrid organizations” have grown in number, size and importance. The one common characteristic of these quasi government entities is that they are *not* agencies of the United States as that term is defined in Title 5 of the *U.S. Code*.[4] However, the accountability and transparency of these organizations are important as well as determining whether they should be included within the boundary of the federal reporting entity and/or its component entities.

The following organizations will be considered and evaluated against the general principles and criteria for the boundaries of the federal reporting entity:

- Quasi official agencies
- Government-sponsored enterprises (GSEs)
- Federally funded research and development centers
- Agency-related nonprofit organizations
- Joint ventures or public/private partnerships
- Congressionally chartered nonprofit organizations
- Bailout entities
- Others

[4] The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics, CRS Report for Congress RL30533 , Summary

Quasi official agencies—The National Archives and Records Administration (NARA) provides the following defining characteristic for quasi official agencies in that they “are not agencies under the definition of 5 U.S.C. 105 but are required by statute to publish certain information on their programs and activities in the Federal Register.”[5] *The United States Government Manual, 2006-2007* contained the following for quasi official agencies: Legal Services Corporation, the Smithsonian Institution, State Justice Institute and the United States Institute of Peace.

Government-sponsored enterprises (GSEs)—GSEs are defined by Congress in enabling legislation. Congress defined the term GSE for budgetary purposes in the Omnibus Reconciliation Act of 1990 as

> a corporate entity created by a law of the United States that —
> (A) (i) has a Federal charter authorized by law;
> (ii) is privately owned, as evidenced by capital stock owned by private entities or individuals;
> (iii) is under the direction of a board of directors, a majority of which is elected by private owners;
> (iv) is a financial institution with power to —
> (I) make loans or loan guarantees for limited purposes such as to provide credit for specific borrowers or one sector; and
> (II) raise funds by borrowing (which does not carry the full faith and credit of the Federal Government) or to guarantee the debt of others in unlimited amounts; and
> (B) (i) does not exercise powers that are reserved to the Government as sovereign (such as the power to tax or to regulate interstate commerce);
> (ii) does not have the power to commit the Government financially (but it may be a recipient of a loan guarantee commitment made by the Government); and
> (iii) has employees whose salaries and expenses are paid by the enterprise and are not Federal employees subject to title 5.[6]

Some have argued that the above definition omits an essential characteristic — a GSE “benefits from an implicit federal guarantee to enhance its ability to borrow money.”[7] Congress created GSEs to help make credit more readily available to sectors of the economy believed to be disadvantaged in the credit markets. The following GSEs — Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), and the Federal Agricultural Mortgage Corporation (Farmer

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[5] United States Government Manual, 2006-2007 p. 555

[6] 104 Stat. 1388-607, Sec. 13112; 2 U.S.C. 622(8).

[7] The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics, CRS Report for Congress RL30533 , CRS-9

Mac) —are investor owned. The Federal Home Loan Bank System and the Farm Credit System — are owned cooperatively by their borrowers. The Financing Corporation and the Resolution Funding Corporation are also organizations that were given GSE status. It should be noted that one well-known GSE, Sallie Mae (Student Loan Marketing Association), recently shed its GSE status and become a wholly private firm. [8]
While the details may vary from one instance to the next, Congress provides that GSEs typically have four characteristics: private ownership; implicit federal guarantee of obligations; activities limited by congressional charter; and limited competition.[9]

Federally Funded Research and Development Centers (FFRDCs)—The FFRDC[10] is a hybrid organization designed to meet a federal need through the use of private organizations. The great strength of FFRDCs appears to lie in their flexibility to assemble teams of technical experts on a project basis. FFRDCs are often difficult to hold accountable. They can have an advantage in competing with private firms for contracts: as nonprofit corporations, they are exempt from most taxation; their facilities and equipment are owned or financed, for the most part, by the federal government, and they receive fees for operating expenses without having to assume business risks or costs associated with competing for most federal work.[11] Federal management of FFRDCs is based upon the Federal Acquisition Regulation (FAR). The FAR provides guidelines to be followed in establishing, organizing, and managing FFRDCs and limits agencies' use of FFRDCs to meet "some long-term research or development need which cannot be met effectively by existing in-house or contractor resources."[12]

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[8] Ibid, CRS-9

[9] Ibid, CRS-10

[10] FFRDCs is a World War II and postwar phenomenon because in World War II there was a national emergency requirement that scientific and engineering talent be rapidly assembled and put to work. After the war, DOD was reluctant to part with this talent and sought ways to keep them in service to the government. The decision to establish private, nonprofit corporations to do contract work and these corporations would be largely dependent on the federal government contract projects. (The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics, CRS Report for Congress RL30533 , CRS-14)

[11] The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics, CRS Report for Congress RL30533 , CRS-16

[12] FAR , 35.017

Agency-related nonprofit organizations—Agency-related nonprofit organizations are organizations that share a legal relationship with a department or agency of the federal government. Over the years, departments and agencies have found it useful and advantageous to ask Congress to create, or authorize a department to create, nonprofit organizations to perform functions that the department itself finds difficult to integrate into its regular policy and financial processes. An example could include when a department or agency receives gifts of real property and monetary gifts. The National Park Foundation is the most prominent example of such an organization, but there are others, such as the National Fish and Wildlife Foundation.

There are many different types of relationships with organizations that may share some sort of legal relationship. The federal government may create organizations with predominately a private-sector legal characteristic to implement government policies and regulations. For example, the Securities Investor Protection Corporation (SIPC) and the Public Company Accounting Oversight Board (PCAOB) are agents of and accountable to the government through the Securities and Exchange Commission (SEC). The SIPC is a non-profit corporation under D.C. law, but it is effectively a subsidiary of the SEC because its bylaws are subject to the SEC's adoption, amendment, or rejection. The SIPC also had borrowing authority and a line of credit from Treasury. Likewise, the PCAOB is a non-profit corporation under the DC Nonprofit Corporation Act. However the members of the PCAOB are appointed by the SEC and may be removed for good cause. Also, the rules of the PCAOB are subject to the approval of the SEC.[13]

Public-private partnerships or joint ventures –Public-private partnerships are just what the name implies. It is a contractual relationship where the resources, risks, and rewards of both the public agency and a private company are combined for greater efficiency, better access to capital, and improved compliance with a range of government regulations regarding the environment and workplace. The public's interests are fully assured through provisions in the contracts that provide for on-going monitoring and oversight.[14]

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[13] The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics, CRS Report for Congress RL30533 , CRS-20

[14] The National Council of Public-Private Partnerships Top Ten Facts about PPPs

<u>Congressionally chartered nonprofit organizations</u>-- Congressionally chartered nonprofit organizations also referred to as “title 36 corporations.” [15] They represent chartering by Congress of private organizations with a patriotic, charitable, historical, or educational purpose. Examples include the Big Brothers and Sisters of America and the American Legion.

<u>Bailout entities</u>-- The federal government occasionally bails out, i.e., guarantees or pays debt, for a privately owned entity whose failure could have an adverse impact on the nation's economy, commerce, national security, etc. As a condition of the bail out, the federal government frequently obtains rights similar to those that would indicate control. The existence of these rights does not make the bailed out entity part of the federal reporting entity or any of the component reporting entities. Disclosure of the relationship with the bailed out entities and any actual or potential material costs or liabilities would be appropriate.

<u>Others</u>—TBD from additional research and task force.

STAFF COMMENTS AND QUESTIONS FOR THE BOARD:

Staff wanted to present some of the unique relationships and organizations that will be considered as we move forward with this project. Staff also believes that we will continue to gain a better understanding of these relationships through our task force.

Would the Board like to suggest other possible unique relationships or organizations that should be considered?

Does the Board have initial thoughts on whether these should be incorporated into the standard or perhaps as an Appendix--Case Studies? Should each type be looked at separately to determine if it is part of the federal reporting entity and if not, what disclosures (if any) would be appropriate?

[15] CRS Report RL30340, *Congressionally Chartered Nonprofit Organizations (“Title 36 Corporations”): What They Are and How Congress Treats Them*

APPENDIX to Tab B--Federal Entity

This appendix to Tab B Federal Entity includes several reference materials the Board may find helpful. These materials have been presented at previous Board meetings.

High Level Comparison Charts

- Figure 1 Comparison of U.S. Standard Setters Consolidation Criteria
- Figure 2 Comparison of National and International Standard Setters Consolidation Criteria
- Figure 3 Comparison of Definitions of Control of Other Standard Setters

SFFAC No. 2: Entity and Display—Excerpt, paragraphs 1 through 53

High-level Comparison Charts

Figure 1 presents a high-level summary of FASAB's current guidance in SFFAC 2 regarding conclusive and indicative criteria as well as the requirements of the Governmental Accounting Standards Board and the Financial Accounting Standards Board. Figure 2 presents a high-level summary of selected international requirements on the subject. The most apparent shortcoming in the FASAB literature is that it resides entirely in a concept statement. Of the references provided in Figures 1 and 2, FASAB is the only standard setter that has not included in its standards requirements for consolidation.

In reviewing the consolidation requirements, staff notes that with the exception of GASB, **control** is the main consideration factor for most other standard-setters. GASB's focus is financial accountability.

<table>
<tr><th colspan="5">Figure 1: Comparison of U.S. Standards</th></tr>
<tr><th>Country</th><th>Document</th><th>Scope</th><th>Consolidation Requirement</th><th>Definition / Criteria</th></tr>
<tr><td rowspan="3">United States of America</td><td>FASAB Statement of Federal Financial Accounting Concepts No. 2, Entity and Display</td><td>Federal Sector</td><td>Financial Accountability and existence of a Significant Relationship where exclusion would cause the financial statements to be misleading or incomplete. (¶ 38)</td><td>Conclusive criterion
Any organization, program, or budget account, including off-budget accounts and government corporations, included in the Federal budget section currently entitled “Federal Programs by Agency and Account.”
Indicative criteria
It exercises any sovereign power of the government to carry out Federal functions.
It is owned by the Federal Government
It is subject to the direct or continuing administrative control of the reporting entity.
It carries out Federal missions and objectives.
It determines the outcome or disposition of matters affecting the recipients of services that the Federal Government provides.
It has a fiduciary relationship with a reporting entity.</td></tr>
<tr><td>GASB Statement No. 14, The Financial Reporting Entity</td><td>State and Local Government Entities</td><td>Financial Accountability</td><td>A primary government is financially accountable for legally separate components under either of the following circumstances:
a. The primary government appoints a voting majority of the organization’s governing board and (1) it is able to impose its will on that organization or (2) there is potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the primary government.
b. If an organization is fiscally dependent on the primary government. (¶ 20)</td></tr>
<tr><td>FASB Statement of Financial Accounting Standards No. 96</td><td>Private Sector Entities</td><td>Controlling Financial Interest</td><td>The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one company, directly or indirectly, of over fifty percent of the outstanding voting shares of another company is a condition pointing toward consolidation. (¶ 13)</td></tr>
</table>

Figure 2: Comparison of National and International Standards				
Country	**Document**	**Scope**	**Consolidation Requirement**	**Definition / Criteria**
Australia	Australian Accounting Standard AAS 24, *Consolidated Financial Reports*	Private and public sector entities, excluding those at the "whole-of-government" level for each State, Territory and the Federal Government	Control	Control means the capacity of an entity to dominate decision making, directly or indirectly, in relation to the financial and operating policies of another entity so as to enable that other entity to operate with it in pursuing the objectives of the controlling entity. (¶ 18)
Canada	CICA Handbook Section 1590, *Subsidiaries*	Profit-oriented enterprises	Control	Control of an enterprise is the continuing power to determine its strategic operating investing and financing policies without the co-operation of others. (¶ .03)
	Public Sector Accounting Recommendations, Section PS 1300, *Government Reporting Entity*	Federal, provincial, territorial and local governments	Control	Control is the power to govern the financial and operating policies of another organization with expected benefits or the risk of loss to the government from the other organization's activities. (¶ .08)
International Accounting Standards Board	International Accounting Standard IAS 27, *Consolidated Financial Statements and Accounting for Investments in Subsidiaries*	Private sector parent entities	Control	Control is the power to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. (¶ 6)
International Federation of Accountants	International Public Sector Accounting Standard 6, *Consolidated Financial Statements and Accounting for Controlled Entities*	Public sector entities other than Government Business Enterprises	Control	Control is the power to govern the financial and operating policies of another entity so as to benefit from its activities. (¶ 8)

FIGURE 3: DEFINITIONS OF CONTROL FROM OTHER STANDARD SETTERS

DOCUMENT	DEFINTION
Australian AAS 24, *Consolidated Financial Reports*	Control means the capacity of an entity to dominate decision making, directly or indirectly, in relation to the financial and operating policies of another entity so as to enable that other entity to operate with it in pursuing the objectives of the controlling entity. (¶ 18)
CICA Handbook Section 1590, *Subsidiaries*	Control of an enterprise is the continuing power to determine its strategic operating investing and financing policies without the co-operation of others. (¶ .03)
Public Sector Accounting Recommendations, Section PS 1300, *Government Reporting Entity*	Control is the power to govern the financial and operating policies of another organization with expected benefits or the risk of loss to the government from the other organization's activities. (¶ .08)
IPSAS 6, *Consolidated Financial Statements and Accounting for Controlled Entities*	Control is the power to govern the financial and operating policies of another entity so as to benefit from its activities. (¶ 8)
IAS 27, *Consolidated Financial Statements and Accounting for Investments in Subsidiaries*	Control is the power to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. (¶ 6)
FASB, SFAS 96 **NOTE:** FASB & IASB have an active project on reporting entity. The Board also tentatively decided that the control concept should be used to determine the composition of a group entity and combinations.	The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one company, directly or indirectly, of over fifty percent of the outstanding voting shares of another company is a condition pointing toward consolidation. (¶ 13)
	The Boards have tentatively decided that control should be defined at the concepts level, and should contain both (a) a power element and (b) a benefits element, together with a link between the two.

SFFAC No. 2: Entity and Display—Excerpt, paragraphs 1 through 53

Introduction

1. A basic postulate of accounting is that accounting information pertains to entities, i.e., circumscribed legal, administrative, fiduciary, or other organizational structures. Another basic postulate is that entities use financial reports to communicate financial and related information about the entity to persons concerned with the entity.

2. The purpose of this statement of accounting concepts is to provide guidance as to what would be encompassed by a Federal Government entity's financial report. The statement specifies the types of entities for which there ought to be financial reports (hereinafter called reporting entities), establishes guidelines for defining the makeup of each type of reporting entity, identifies types of financial reports for communicating the information for each type of reporting entity, and suggests the types of information each type of report would convey.

3. A statement of financial accounting concepts is intended to guide the members of the Federal Accounting Standards Advisory Board (FASAB) as they deliberate and recommend accounting standards for the Federal Government. It also would be useful to the Office of Management and Budget (OMB), when it carries out its statutory responsibilities for specifying who should prepare financial statements and the form and content of those statements;16 and as broad guidance for preparers, auditors, and users of financial statements of Federal agencies. A statement of financial accounting concepts does not, in and of itself, represent standards that would be considered generally accepted accounting principles for Federal agencies to be followed for the preparation of financial statements.

4. This statement does not try to define which reporting entities must prepare and issue financial statements. That authority and responsibility resides with the Congress, OMB, and other oversight organizations and resource providers.

5. The specification of reporting entities intends to be suitable for all organizations

[16] OMB specifies the form and content of agency and governmentwide financial statements, pursuant to authority assigned in the Chief Financial Officers Act of 1990, as amended (title 31, U. S. Code, section 3515(d) and section 331(e)(1)) through periodic issuance of OMB Bulletins. OMB intends to base the form and content on the concepts contained in this statement.

within the Executive branch of the Federal Government, including the Departments, independent agencies,17 commissions, and corporations. FASAB does not propose to recommend accounting concepts and standards for the Legislative and Judicial branches. However, the concepts recommended in this statement would be appropriate for those branches.

6. The concepts, as defined in this statement, are intended primarily for the general purpose financial reporting performed by Federal entities. This is the financial reporting that these entities would undertake to help meet the objectives defined in Statement of Federal Financial Accounting Concepts (SFFAC) No. 1, "Objectives of Federal Financial Reporting." These objectives are as follows:

- **Budgetary integrity**. Federal financial reporting should assist in fulfilling the government's duty to be publicly accountable for monies raised through taxes and other means and for their expenditure in accordance with the appropriations laws that establish the government's budget for a particular fiscal year and related laws and regulations.

- **Operating performance**. Federal financial reporting should assist report users in evaluating the service efforts, costs, and accomplishments of the reporting entity; the manner in which these efforts and accomplishments have been financed; and the management of the entity's assets and liabilities.

- **Stewardship**. Federal financial reporting should assist report users in assessing the impact on the country of the government's operations and investments for the period and how, as a result, the government's and the nation's financial conditions have changed and may change in the future.

- **Systems and control**. Federal financial reporting should assist report users in understanding whether financial management systems and internal accounting and administrative controls are adequate to ensure proper execution of transactions, safeguard assets, and support performance measurement.

7. The concepts are also intended, as FASAB's mission statement requires, to help in meeting the financial and budgetary information needs of executive agencies and Congressional oversight groups, and to strengthen the conceptual basis and consistency of Federal accounting data.

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[17] "Independent agencies" is a term used to distinguish agencies that are independent of a Cabinet department from the agencies that are part of the Cabinet departments. Independent agencies report directly to the President and are part of the U. S. Government.

8. The entity and display concepts presented in this statement do not preclude the specification of ad hoc or temporary reporting entities to meet special reporting needs of users of Federal agencies' financial information. Nor do they preclude a reporting entity from preparing special purpose financial reports to meet the specific needs of persons in the reporting entity or in response to requests from persons outside the entity for certain financial information; or from preparing a so-called "popular report," which provides a simplified, highly readable, easily understandable description of a reporting entity's finances. These statements would not necessarily purport to be presented in accordance with generally accepted accounting principles.

Reasons for Defining Reporting Entities

9. The most basic reason for having an explicit understanding of what the reporting entity entails is to ensure that the users of the entity's financial reports are provided with all the information that is relevant to the reporting entity, subject to cost and time constraints. Clearly defining the boundaries of the reporting entity provides the users with a clear understanding of what the reporting entity encompasses. It helps to establish what information is relevant to the financial statements and what information is not.

10. Other reasons for having an explicit understanding of what the reporting entity entails are to:

- Ensure that for the aggregation of information at each reporting level, no entity is omitted, and to provide for consolidations and/or combinations of information from reporting units at the same level, as appropriate;
- Assist in making comparisons among comparable reporting entities by reducing the possibility of unintended or arbitrary exclusions or inclusions of entities;
- Assist in making comparisons among alternative ways to provide similar services or products;
- Be able to distribute costs properly and fully and to properly attribute the responsibility for assets and liabilities; and
- Facilitate evaluating performance, responsibility, and control, especially where one agency is the provider or recipient of services attributable to or financed by another agency.

Structure of the Federal Government

11. The Federal Government is an extremely complex organization composed of

many different components. For accounting and reporting purposes, it may be viewed from at least three perspectives. However, the nature of each type of component and the relationships among the components and perspectives are not always consistent.

Organization Perspective

12. The first type of perspective is the organization perspective. The Federal Government is composed of organizations that manage resources and are responsible for operations, i.e., delivering services. These include the major Departments and independent agencies, which are generally divided into suborganizations, i.e., smaller organizational units with a wide variety of titles, including bureaus, administrations, agencies, services, and corporations. Many of these are further divided into even smaller suborganizations. On the other hand, there are small agencies for which division into smaller units is generally not considered appropriate.

Budget Perspective

13. From another perspective, the government is composed of accounts presented in the budget, hereinafter referred to as budget accounts. Budget accounts are composed of expenditure (appropriations or fund) accounts and receipt (including offsetting receipt) accounts. The size and scope of these accounts varies according to Congressional preference. They can vary from very small accounts, which are useful for constraining management, to very large accounts, which can be used to finance many activities.

14. Budget accounts are not the same as Treasury accounts. The latter are accounts established in the Treasury to, among other purposes, record the appropriations and other budgetary resources provided by statutes and the transactions affecting those accounts. For the most part, budget accounts are aggregations of Treasury accounts. Also, Treasury accounts include deposit accounts as well as budget accounts.

15. Nor are budget accounts the same as the uniform ledger accounts established by the U. S. Government Standard General Ledger (SGL). SGL accounts record specific homogeneous types of transactions and balances that aggregate to specific classifications on the financial statements. They have been established so that agencies can establish control over their financial transactions and balances, meet the basic

financial reporting requirements, and integrate budgetary and financial accounting in the same general ledger.

16. A budget account may coincide with an organization or one or more of its suborganizations. Other times, several budget accounts need to be aggregated to constitute an organization or sub-organization.

17. Budget accounts are classified as federal funds or trust funds. Any account that is designated by the laws governing the federal budget as being a trust fund is so classified. Federal funds comprise the larger group and include all transactions not classified by law as trust funds. Three components make up federal funds: the general fund, special funds, and revolving funds. The definition of each of these categories can be found in the OMB circular A-11 and the GAO Glossary of Terms Used in the Federal Budget Process.

18. Care must be taken in determining the nature of all trust funds and their relationship to the entity responsible for them. A few trust funds are truly fiduciary in nature. Most trust funds included in the budget are not of a fiduciary nature and are used in federal financing in a way that differs from the common understanding of trust funds outside the federal government. In many ways, these trust funds can be similar to revolving or special funds in that their spending is financed by earmarked collections.

19. In customary usage, the term "trust fund" refers to money belonging to one party held "in trust" by another party operating as a fiduciary. The money in a trust fund must be used in accordance with the trust's terms, which the trustee cannot unilaterally modify, and is maintained separately and not commingled with the trustee's own funds. This is not the case for most federal trust funds that are included in the budget—the fiduciary relationship usually does not exist. The beneficiaries do not own the funds and the terms in the law that created the trust fund can be unilaterally altered by Congress.

20. Special funds and trust funds, except trust revolving funds, are aggregates of budget accounts. They normally consist of one or more receipt accounts and one or more expenditure accounts. Among the trust funds, social insurance programs (such as social security and unemployment compensation) have the largest amount of funds and federal employee programs (such as retirement and health benefits) the second largest. Together they make up about 90 percent of all trust fund receipts. Other trust funds

include excise tax financed programs for highway construction, airports and airway operations, and other public works. Like other budget accounts, trust funds are usually the responsibility of a single organization, although sometimes they are the responsibility of more than one organization.

21. Budget accounts are also categorized, as mandated by law and defined by OMB, into functions and subfunctions that represent national needs of continuing national importance and substantial expenditures of resources. Examples of functions are national defense and health.

Program Perspective

22. From a third perspective, the government is composed of programs and activities, i.e., the services the organizations provide and the specific lines of work they perform. Each program and activity is responsible for producing certain outputs in order to achieve desired outcomes.

23. There is no firm definition for the term "program;" it varies in the eye of the beholder. For example, the Highway program could relate to the entire Federal highway program, the program to build interstate highways (in contrast to city streets, secondary roads, etc.), or a program to build a highway between two specific points. Moreover, in accordance with the sequester provisions of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, the House and Senate Appropriations Subcommittees annually define, in the Committee Reports, the meaning of "Programs, Projects, and Activities" as they relate to each of the Appropriations Acts.

24. The term "program" is also often used interchangeably with the terms "function" and "sub-function" (see paragraph 21). Generally, however, the term "function" would be used only for the functions defined in the budget. Otherwise, the term "program" would be used.

Intertwining of the Perspectives

25. The programs are administered by the organizations and financed by the budget accounts. In a few instances, there is a one-to-one relationship among the three perspectives. A single budget account finances a single program and organization.

Thus, the program is carried out only by the single organization and the organization performs only one program.

26. However, most programs are financed by more than one budget account, some of which might not be under the control of the organizational unit administering the program. Some programs are even administered by more than one organization. Likewise, a single organization or budget account could be responsible for several programs. In some instances, a program could also be considered an organizational unit, e.g., the Center for Disease Control and Prevention.

27. Furthermore, some of the support necessary to perform a program is frequently provided by other organizations and/or financed by other budget accounts. Examples are the computer support for a program that is obtained from a central unit within the department, or retirement health costs for a program's current and former employees.

28. This complex situation is the result of the evolution of Federal organizations, programs, and budgetary structures over many years. As Federal missions and programs have expanded and changed, new departments have been created, new organizations have been added to existing departments, and new duties have been assigned to existing organizations on the basis of various considerations. Similarly, the budget structure has evolved in response to the needs of the Congress; its committees and subcommittees; and various initiatives by the President, program managers, and interest groups.

Identifying the Reporting Entity for General Purpose Financial Reporting

29. As stated, reporting entities are entities that issue general purpose financial statements to communicate financial and related information about the entity. For any entity to be a reporting entity, as defined by this Statement of Federal Financial Accounting Concepts, it would need to meet all of the following criteria.

- There is a management responsible for controlling and deploying resources, producing outputs and outcomes, executing the budget or a portion thereof (assuming that the entity is included in the budget), and held accountable for the entity’s performance.
- The entity’s scope is such that its financial statements would provide a meaningful representation of operations and financial condition.

- There are likely to be users of the financial statements who are interested in and could use the information in the statements to help them make resource allocation and other decisions and hold the entity accountable for its deployment and use of resources.

30. Budget accounts, in and of themselves, do not meet the criteria in the preceding paragraph and, therefore, would not be considered a reporting entity for the purposes of issuing general purpose financial statements. Also, the size and scope of the budget accounts across all government agencies lack sufficient consistency for them to be universally considered as the reporting entity. Similarly, programs generally do not meet the criteria in paragraph 29 and, therefore, would not be a considered a reporting entity that prepares general purpose financial statements.

31. On the other hand, organizations, and particularly larger organizations, meet the criteria in paragraph 29. While the occasional overlap of programs and budget accounts among more than one organizational unit could complicate financial reporting, the association of data with the responsibility centers, revenue centers, profit centers, cost centers, etc. which managers typically use for organizing and operating permit the following:

- aggregating information for not only the organization (and suborganizations), but also for one or more of the programs performed by the organization, and one or more of the budget accounts for which the organization is responsible, and
- the subsequent arraying of the information not only by organization, but also by sub-organization, program, and/or budget accounts.

32. This approach to defining the appropriate reporting entities in the Federal Government supports establishment of accountability in the organizations (and suborganizations) while still enabling them to provide information pertaining to their programs.

33. Although a reporting entity might not control all the budget accounts used to finance one or more of the programs it administers, any revenues attributable to or costs incurred on behalf of the programs it administers should be associated with that reporting entity. This notion holds true regardless of whether the reporting entity maintains personnel on a payroll.

34. The departments and major independent agencies are organizational units and therefore would be the primary reporting entities. However, in many instances, financial

statements that present aggregations of information into suborganization entities, i.e., bureaus, administrations, or agencies, may be more useful than statements that present only aggregations into organizational entities. The former can provide a better understanding of the financial results and status of the many individual suborganizations and programs constituting a department or major independent agency. They can reveal instances where programs are carried out by several suborganizations within the department or major independent agency.

35. Similar to other budget accounts, trust funds, special funds, and revolving funds are usually administered by a single organization. For financial reporting purposes, the organization would be the reporting entity; the trust fund or revolving fund would be a component of the organization that administers the fund in the same manner that a suborganization or other type of budget account is a component of the organization. This would not preclude separate reporting for the trust fund, special fund, or revolving fund by the managing organization, nor would it preclude disclosure of trust fund, special fund, or revolving fund information within the organization's report when there is sufficient interest.[18]

36. Likewise, some programs are coterminous, i.e., share the same boundaries, with an organization or sub-organization, while other programs—such as student loan programs—are the component for which resources are deployed, are responsible for achieving objectives, and/or are of great interest to outsiders. In both instances, the financial operations and results of the program might warrant highlighting or even separate reporting by the organization or suborganization which manages the program.

37. Financial statements for organizationally-based reporting entities may be audited and issued to external parties, unaudited and used for internal management purposes,

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[18] For some trust funds, the collection of the revenues is performed by an organizational entity acting in a custodial capacity that differs from the organizational entity that administers the trust fund. In those instances, the organizational entity that collects the revenues would be responsible for reporting only the collection and subsequent disposition of the funds. The organizational entity responsible for carrying out the program(s) financed by a trust fund, or in the case of multiple responsible entities, the entity with the preponderance of fund activity, will report all assets, liabilities, revenues, and expense of the fund, notwithstanding the fact that another entity has custodial responsibility for the assets.

or, perhaps to be more relevant and meaningful, combined with financial statements from other organizationally-based reporting entities.

38. The ultimate aggregation of entities is into the entire Federal Government which, in reality, is the only independent economic entity—although some would say the entire country is the ultimate economic entity. The Federal Government entity would encompass all of the resources and responsibilities existing within the component entities, whether they are part of the Executive, Legislative, or Judicial branches (although, as noted in paragraph 5, FASAB's recommendations pertain only to the Executive Branch). The aggregation would include organizations for which the Federal Government is financially accountable as well as other organizations for which the nature and significance of their relationship with the government (see paragraphs 39 through 50) are such that their exclusion would cause the Federal Government's financial statements to be misleading or incomplete.

Criteria for Including Components in a Reporting Entity

39. Regardless of whether a reporting entity is the U.S. Federal Government, or an organization, suborganization, or program, there can be uncertainty as to what should be included and inconsistency as to what is included in the reporting entity. The identification and application of specified criteria can reduce this uncertainty and inconsistency.

40. The Governmental Accounting Standards Board (GASB) has established criteria for what would be included in a state or local government reporting entity. These criteria relate to financial accountability, which includes appointment of a voting majority of the organization's governing board, together with imposition of will, and financial benefit to or burden on a primary government. These criteria, while in part relevant, must be tailored to the Federal Government environment. First, there are not as many different types of entities in the Federal Government as there are in state and local governments. Second, the Congress and others with oversight authority frequently establish explicit rules for what to include as part of a Federal reporting entity. Finally, as indicated, with the exception of the Federal Government as a whole, all the reporting units are components of a larger entity, namely the Federal Government, rather than independent economic entities.

Conclusive Criterion

41. There are two types of criteria that should be considered when deciding what to include as part of a financial reporting entity. The first is a **conclusive criterion**, i.e., an inherent conclusion that for financial reporting purposes, any organization meeting this criterion is part of a specified larger entity.

42. Appearance in the Federal budget section currently entitled "Federal Programs by Agency and Account" is a conclusive criterion. Any organization, program, or budget account, including off-budget accounts and government corporations, included in that section should be considered part of the U.S. Federal Government, as well as part of the organization with which it appears. This does not mean, however, that an appropriation that finances a subsidy to a non-Federal entity would, by itself, require the recipient to be included in the financial statements of the organization or program that expends the appropriation.

Indicative Criterion

43. There are instances when, for political or other reasons, an organization (including a government corporation), program, or account is not listed in the "Federal Programs by Agency and Account," yet the general purpose financial statements would be misleading or incomplete—in regard to the objectives for Federal financial reporting—if the organization, program, or account were not included therein. These organizations, programs, or accounts would normally be considered to be operating at the "margin" of what would be considered a governmental function in contrast to providing a more basic governmental function. Thus, in addition to the conclusive criterion, there are several **indicative criteria** that should be considered in the aggregate for defining a financial reporting entity in the Federal Government. No single indicative criterion is a conclusive criterion in the manner that appearance in the "Federal Programs by Agency and Account" section of the budget is. Nor can weights be assigned to the indicative criteria. Thus, while the indicative criteria are presented in descending order of importance, judgment must be based on a consideration of all of the indicative criteria.

44. The indicative criteria for determining whether an organization not listed in the "Federal Programs by Agency and Account" section of the budget is nevertheless part

of a financial reporting entity are as follows:

- It exercises any sovereign power of the government to carry out Federal functions. Evidence of sovereign powers are the power to collect compulsory payments, e.g., taxes, fines, or other compulsory assessments; use police powers; conduct negotiations involving the interests of the United States with other nations; or borrow funds for Government use.
- It is owned by the Federal Government, particularly if the ownership is of the organization and not just the property. Ownership is also established by considering who is at risk if the organization fails, or identifying for whom the organization's employees work.
- It is subject to the direct or continuing administrative control of the reporting entity, as revealed by such features as (1) the ability to select or remove the governing authority or the ability to designate management, particularly if there is to be a significant continuing relationship with the governing authority or management with respect to carrying out important public functions (in contrast to selections and designations in which there is little continuing communication with, or accountability to, the appointing official); (2) authority to review and modify or approve budget requests, budgetary adjustments, or amendments or rate or fee changes; (3) ability to veto, overrule, or modify governing body decisions or otherwise significantly influence normal operations; (4) authority to sign contracts as the contracting authority; (5) approval of hiring, reassignment, and removal of key personnel; (6) title to, ability to transfer title to, and/or exercise control over facilities and property; and (7) right to require audits that do more than just support the granting of contracts. (While many of these criteria exist in a client contractor relationship, it is not necessarily intended that an entity's contractor be considered as part of the reporting entity.)
- It carries out Federal missions and objectives.
- It determines the outcome or disposition of matters affecting the recipients of services that the Federal Government provides.
- It has a fiduciary relationship with a reporting entity, as indicated by such factors as the ability of a reporting entity to commit the other entity financially or control the collection and disbursement of funds; and other manifestations of financial interdependency, such as a reporting entity's responsibility for financing deficits, entitlement to surpluses (although not necessarily the assets acquired from failed units), or the guarantee of or "moral responsibility" for debt or other obligations.

45. The entity or any of the above criteria are likely to remain in existence for a time, i.e., the interest in the entity and its governmental characteristics is more than fleeting.

46. In applying the indicative criteria, the materiality of the entities and their relationship with one another should be considered. Materiality should not be measured solely in dollars. Potential embarrassment to any of the entities' stakeholders should also be considered. Thus, a bias toward expansiveness and comprehensiveness would

be justified, particularly if it could contribute to maintenance of fiscal control.[19]

Federal Reserve System

47. In establishing and monitoring monetary policy, the Federal Reserve System, i.e., the Board of Governors of the Federal Reserve System and the Federal Reserve Banks, could be considered as functioning consistent with the indicative criteria presented in paragraph 44. However, in the United States, the organization and functions pertaining to monetary policy are traditionally separated from and independent of the other central government organizations and functions in order to achieve more effective monetary and fiscal policies and economic results. Therefore, the Federal Reserve System would not be considered part of the government-wide reporting entity. Payments made to or collections received from the Federal Reserve System would be reported in the financial statements of the Federal Government. Certain other disclosures might also be appropriate in the financial statement for the entire government.

Government Sponsored Enterprises

48. There are also several Federally chartered but privately owned and operated financial institutions that have been established as financial intermediaries to facilitate the flow of investment funds to specific segments of the private sector. These entities are called government sponsored enterprises (GSE). Examples are the Federal National Mortgage Association, the Farm Credit Banks, and the Federal Home Loan Banks. By law, each of these GSEs is subject to oversight from a specific Federal agency. However, they are not included in the Federal budget section entitled "Federal Programs by Agency and Account." Nor, as currently constituted, do they function in a manner consistent with the indicative criteria presented in paragraph 44. Thus they would not be considered part of the government-wide reporting entity nor the reporting entity to which they have been assigned for oversight.

49. On the other hand, there are "political expectations" associated with the GSEs,

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[19] Any uncertainty as to what to consider as a reporting entity would be resolved by OMB in consultation with the appropriate Congressional committees.

the most significant of which is an expectation that legislation would be enacted to support a GSE experiencing severe financial difficulties. (Political expectations are different than "moral obligations" established by many states. There is no statutory authority that defines whether and how a political expectation would be met. With a moral obligation, the manner in which it may be met is usually explicitly defined in statute.) Therefore, agencies assigned oversight responsibility for a GSE(s) would need to consider making disclosures of the government's relationship with the GSE(s) and other information that would provide an understanding of the possibility of a contingent liability.[20]

Bailout Entities

50. The Federal Government occasionally bails out, i.e., guarantees or pays debt, for a privately owned entity whose failure could have an adverse impact on the nation's economy, commerce, national security, etc. As a condition of the bail out, the Federal Government frequently obtains rights similar to the authorities associated with the indicative criteria presented in paragraph 44. The existence of these rights does not make the bailed out entity part of the Federal Government reporting entity or any of the other reporting entities that are part of the Federal Government. Disclosure of the relationship(s) with the bailed out entity(ies) and any actual or potential material costs or liabilities would be appropriate.

OTHER ASPECTS CONCERNING THE COMPLETENESS OF THE ENTITY

51. The application of specified criteria to delineate the reporting entity is one aspect

[20] The term government sponsored enterprise is also sometimes used in a broader manner to encompass other entities established by the Federal Government to further a public policy and that are also not included in the budget section "Federal Programs by Agency and Account." Examples are the Financing Corporation, Resolution Funding Corporation, Amtrak, and even, on occasion, the American National Red Cross. These entities have varied characteristics and different types of relationships to the Federal Government, and therefore, in some cases, may be included with the above mentioned GSEs in sections or tables of Federal budget documents. These entities need to be judged individually with respect to the indicative criteria presented in paragraph 39 in order to determine whether they should be considered part of a Federal reporting entity.

of ensuring that the users of a reporting entity's financial reports are provided with all the information relevant to the reporting entity. However, because the only independent economic entity is the entire Federal Government, financial resources or free services are often provided from one component in the government to another component without a quid pro quo. For example, a portion of the retirement costs of Federal employees is reported by the Office of Personnel Management rather than the organizational entities employing the persons. Thus, within the parameters explained in paragraphs 52 and 53, it is important to ensure that the reporting entity's financial reports include amounts that are attributable to the reporting entity's activities, even though they are recorded elsewhere. This is particularly important for costs associated with the use of human resources; personnel services are such a major part of most government activities. It is also important for the costs of services provided by other reporting entities, such as computer services provided by another unit.

52. A process in which the reporting entity is billed and pays for the amounts attributable to its activities is normally the most desirable approach for recording and reporting these amounts. However, when this type of direct debiting or crediting is not done, the decision as to whether to capture and report attributable amounts would be based on such criteria as the magnitude of the attributable amounts, the decision usefulness of the information to its likely users, the costs of capturing the data, whether a decision would be made differently as a result of having the information, and whether the information would have a policy impact.

53. It might be appropriate to consider the interest expense inherent in devoting a sum of capital to an organization or program as part of the total costs incurred in operating the organization or performing the program. This principle has already been adopted for the accounting for loans and loan guarantees, whereby a loan program is charged for the cost of capital provided