



Federal Accounting Standards Advisory Board

January 3, 2007

Memorandum

To: Members of the Board

From: Ross Simms, Assistant Director

Eileen Parlow, Assistant Director

Through: Wendy M. Comes, Executive Director

Subj: Conceptual Framework: The Federal Financial Report (TAB B)¹

At the November 2006 Board meeting, the Board reviewed an outline of a proposed concepts statement on the federal financial report and provided staff with comments. In addition, Board members believed that the Board could begin to consider how to report performance information and staff could address the issue as part of this project.

Staff has incorporated Board member comments in the revised outline and prepared a paper on ways the Board could begin developing the performance reporting segment of the project. The revised outline showing tracked changes is provided as Attachment I and the paper on performance reporting is provided as Attachment II. The objective for the meeting is to discuss the outline and staff plans for performance reporting.

As part of the FASAB's strategic directions, the Board decided that the Operating Performance objective should be its highest priority in the near-term. Because of the interrelated nature of the financial reporting objectives, efforts in achieving the Operating Performance objective permits progress on the other objectives. The objective concerns the government's responsibility to be accountable to citizens for managing resources and providing services economically and efficiently and for effectiveness in achieving goals.² Accordingly, performance reporting is a key aspect of the Operating Performance objective.

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.

² Statement of Federal Financial Accounting Concepts 1, *Objectives of Federal Financial Reporting*, par. 123.

Recently, with the completion of the fiscal year (FY) 2006 annual reporting process, the financial reporting community has been engaged in much discussion on how performance reporting could be improved. In addition, two organizations, the National Academy of Public Administration and the Association of Government Accountants conducted research on financial management and reporting issues and recently issued reports identifying areas for improvement in performance reporting.³ Two subjects evolved from the discussion and research that may be of particular interest to the Board. The subjects are: 1) the need to establish different levels of reporting information; and 2) the need for improvements in integrating cost information with performance reporting. Constituents raised concerns that the Performance and Accountability Reports (PAR) have grown too voluminous and agencies are not developing cost information to integrate with performance reporting, such as reporting the cost of specific programs and the amount spent on achieving results.

Staff also noted these concerns during the staff roundtable meetings on the objectives of financial reporting. The roundtable participants' suggestions for addressing the issues involved considering other types of reports and guidance other than a standard. Given that the Board was in the process of reviewing its role in relation to the objectives of financial reporting, staff suggested that the Board consider the topics during a strategic planning exercise. However, the Board decided to develop and issue the strategic directions document rather than formally engage in strategic planning.

Considering the present level of interest in these topics and the demand for performance information, staff suggests that the Board revisit the issues by utilizing roundtables for the PAR issues and an educational session for the cost accounting issue. Staff believes that timely guidance on levels of reporting would help facilitate consistency in reporting and help users advance their understanding of the cost of federal programs and the results they achieve. To research the PAR and different levels of reporting topic, staff plans to conduct roundtable meetings with financial reporting experts and users. The roundtable meetings provide an outreach opportunity to inform constituents on Board activities and obtain feedback on possible solutions to issues. Should the Board decide to pursue this topic and the roundtable approach, Appendix I provides a proposed plan for conducting the meetings.

Staff also believes that this may be an opportune time to consider an educational session on SFFAS 4 and cost accounting. The session could serve dual purposes – to inform constituents and obtain feedback on how FASAB can assist in improving progress. The session could emphasize the value of developing cost information and have presentations of best practices in implementing managerial cost accounting and linking that information to performance reporting. Experts and leaders from federal as well as state and local governments could be invited to share their knowledge. In addition, staff plans to review the Statement of Net Cost as part of the Financial Report project. The session could provide feedback on enhancements to the statement and staff would consider this feedback during the review. Should the Board decide to pursue this suggestion, staff could provide the Board with a plan for the education session at the March 2006 Board meeting.

³ *Moving From Scorekeeper to Strategic Partner: Improving Financial Management in the Federal Government*, National Academy of Public Administration, October 2006, p. 21. (<http://www.napawash.org/index.html>). *PAR: The Report We Love to Hate*, Association of Government Accountants, June 2006, p. 16. (<http://www.agacgm.org/research/publications>).

Please feel free to contact us (Ross at 202-512-2512 or by email at simmsr@fasab.gov and Eileen at 202-512-7356 or by email at parlowe@fasab.gov) to discuss any comments or questions you may have.

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OUTLINE OF PROPOSED CONCEPTS STATEMENT KEY COMPONENTS OF THE FEDERAL FINANCIAL REPORT

- 1) Transmittal Letter
- 2) Preamble
 - a) Provide an overview of concepts statements as in the preamble used in the elements concepts statement
- 3) Table of Contents
- 4) Executive Summary
 - a) What is the Board proposing?
 - i) Within the framework of general purpose federal financial reports (GPFFR)¹ that contain financial statements for component entities and the Federal Government as a whole, this Concepts Statement would:
 - (1) Establish criteria for determining when a means of communicating information (management's discussion and analysis (MD&A), financial statements, disclosures, required supplementary information (RSI) other than MD&A, and other accompanying information (OAI)) should be used in meeting the reporting objectives; and
 - (2) Describe the financial statements used to present the elements critical to meeting financial reporting objectives and explain what constitutes a full set of financial statements.
 - b) Why is the Board making this proposal?
 - i) Need to enhance existing concepts, address emerging issues, and incorporate concepts relied upon that are not yet in a concepts statement
 - (1) Existing concepts² describe the GPFFR and identify the types of communication methods that may be used within the report. Those methods include MD&A, statements, disclosures, RSI other than MD&A, and OAI. In addition, the concepts suggest different types of statements that may be used to communicate information about an entity.

Given that there are several broad financial reporting objectives each with sub-objectives that require a variety of information, several financial statements and other communication methods may be used to help achieve the objectives. However, the concepts are currently not explicit in discussing what constitutes a full set of financial statements, how the statements articulate, align, or bridge,

¹ The term general purpose federal financial report, abbreviated "GPFFR," is used as a generic term to refer to the report that contains the entity's financial statements that are prepared and audited pursuant to the CFO Act of 1990, as amended.

² SFFAC 2, *Entity and Display*, and SFFAC 3, *Management's Discussion and Analysis*

and the “lines” that separate each method of communication necessary for achieving the financial reporting objectives. Discussing these matters would help provide guidance on how to determine the appropriate communication method to use. As a result, clarification is needed to help the Board and constituents in selecting the financial statements and other communication methods most appropriate for presenting information within GPFRRs. [To facilitate understanding of the federal reporting model and the interrelationship of the reporting objectives and sub-objectives, staff plans to discuss how types of statements contribute to the objectives in Section 8.c.v.]

(2) Emerging issues

Since the issuance of the initial concepts, substantial progress has been made in federal financial reporting and the community of federal financial report users, preparers, and auditors has grown. Along with the progress and growing community came various issues that the concepts needed to address, such as the reporting of sustainability information and the reporting of financial and performance information in Performance and Accountability Reports (PAR)

(a) Evolution of sustainability reporting

- (i) The nation’s large and growing long-term fiscal imbalance warrants the attention of the American public, the President, and Congress
- (ii) Citizens, the Congress, and other users of the financial statements need information to understand and evaluate the current status and longer-term sustainability of federal programs
- (iii) Need to address financial reporting objectives:
 - 1. Federal financial reporting should provide information that helps the reader to determine:
 - a. Whether the government's financial position improved or deteriorated over the period.
 - b. Whether future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due.

(b) Evolution of performance and accountability reports (PARs) that contain financial and performance related information

- (i) CFO Act agencies prepare a PAR
- (ii) PAR consists of many reports related to financial and program performance previously issued separately
- (iii) Need effective linkage of financial and performance information
 - 1. SFFAS 4 and cost accounting (i.e., cost of performance)
 - 2. Possible task force with agencies already using cost accounting to link financial information to program performance
 - 3. Seek advice from GASB on its work on service efforts and accomplishments
- (iv) Next generation PAR - possible suggestions
 - 1. condense, streamline, focus
 - 2. split into 2 submissions:
 - a. corporate annual report (MD&A and key statements), and
 - b. detailed financial statements and performance data linked (preferably on-line)

3. PAR and its on-line detail becomes a useful tool for decision-making
- (3) Concepts relied upon but not included in concepts statements - summarize the Board's consideration of concepts used in developing standards such as
- (a) Implementation Guide to SFFAS 7, *Accounting for Revenue and Other Financing Sources*
 - (b) SFFAS 25, *Reclassification of Stewardship Responsibilities and Eliminating the Current Services Assessment*
 - (c) SFFAS 26, *Presentation of Significant Assumptions for the Statement of Social Insurance: Amending SFFAS 25*
 - (d) SFFAS 29, *Heritage Assets and Stewardship Land*
 - (e) SFFAS 32, *Consolidated Financial Report of the United States Government Requirements: Implementing Statement of Federal Financial Accounting Concepts 4 "Intended Audience and Qualitative Characteristics for the Consolidated Financial Report of the United States Government,"*
 - (f) Others
- ii) The concept statement would provide useful guidance to the Board and its constituents
- (1) Important roles of the conceptual framework are :
- (a) describing the statements used to present elements;
 - (b) identifying means of communicating information; and
 - (c) describing when a means should be used.
- (2) Concepts would help those affected by or interested in standards to understand better the purposes, content, and characteristics of information provided in federal financial reports
- c) How would this proposal improve financial reporting?
- i) Enhance the framework regarding financial statements and other communication methods
- (1) Help the Board and constituents in understanding the functions and limitations of financial statements and other communication methods relate within GPFFRs.
 - (2) Assist the Board and constituents in understanding how financial statements and other communication methods relate.
 - (3) Assist in selecting appropriate means of communicating information within GPFFRs.
- ii) Facilitate the understandability, consistency, and comparability of financial reporting
- d) How does this proposal contribute to meeting the federal financial reporting objectives?

- i) Describe financial statements that would contribute to meeting the financial reporting objectives
- ii) Providing guidance on communication methods would contribute to consistency in reporting and assist users in understanding the location and nature of information in financial reports. This also contributes to the overall objective of demonstrating accountability and providing useful information as well as helping to achieve specific objectives of budgetary integrity, operating performance, stewardship, and internal control.

5) Acronyms

6) Questions for Respondents

- 7) Introduction – This concept statement describes the financial statements that should be presented in GPFFRs that contain financial statements of component entities and the Federal Government as a whole. This statement also describes the relationship of MD&A, financial statements, disclosures, RSI other than MD&A, and OAI and provides conceptual guidance for selecting the vehicle appropriate for the information to be reported.

(Also, provide background on why the statement is needed, such as the need for enhancements to existing concepts, such as SFFAC 2 and SFFAC 3).

8) Proposed Concepts

a) GPFFRs in general (covers both component entity level and government-wide reporting)

i) Description of GPFFRs

(1) Role, purpose, and limitations

ii) Relationship of GPFFRs to the federal financial reporting objectives described in SFFAC 1

iii) Information that a complete financial report should provide. Currently, SFFAC 1, par. 250-264 summarizes the following based on the financial reporting objectives

(1) Information on the sources and uses of budgetary resources

(2) Information about operations and the related resources

(3) Information about the government's assets

(4) Information about the government's liabilities and financial responsibilities

(5) Information that addresses concerns with the future

(6) Information that addresses financial controls

iv) In the Federal Government, there are several types of reporting entities (organizations, suborganizations, programs, and the government as a whole) and several financial reporting objectives (budgetary integrity, operating performance, stewardship, and systems and control). Each reporting objective can be met to a certain degree by the statements prepared by or for one type of entity and to a greater or lesser degree by the statements prepared by or for the other types of

reporting entities. Meeting the reporting objectives in their totality requires financial statements from all the types of reporting entities. (SFFAC 2, par. 56)

- v) Key components of the Performance and Accountability Report (Currently, SFFACs 2 and 3 provide the following components which may serve as a starting place)

- (1) Agency Head Message
- (2) MD&A (as RSI)
- (3) Performance Section
- (4) Financial Section
 - (a) CFO Letter
 - (b) Auditor's Report
 - (c) Financial Statements and Notes
 - (d) Required Supplementary Stewardship Information (RSSI)
 - (i) Stewardship Investments remains as the final item in this category
 - (e) RSI (other than MD&A)
- (5) Other Accompanying Information (OAI)

Include illustration to show the components of a GPFFR and its relationship to all financial reporting and all information used in decision-making and assessing accountability

- b) Responsibility for Financial Reporting
- i) Discuss management's responsibility for financial reporting and related assertions.
 - (1) Management's responsibility is currently found in auditing literature Statement on Auditing Standards (SAS) 106, *Audit Evidence*
 - (2) Management is responsible for assertions that are implicit in financial reporting. Assertions have an important role in determining what is presented in financial statements. Some examples of assertions include:
 - (a) Occurrence – transactions and events that have been recorded have occurred and pertain to the entity.
 - (b) Completeness – all transactions and events that should have been recorded have been recorded.
 - (c) Accuracy – amounts and other data relating to recorded transactions and events have been recorded appropriately
- c) MD&A
- i) Overall description (SFFAC 3)
 - (1) Financial and performance Information (i.e., required in SFFAS 15)
 - (2) User friendly display of overall performance and financial information
 - (3) Useful as a stand-alone highlights document for a novice reader with little technical background (see Circular A-136 section III)
 - ii) Relationship to the objectives of financial reporting including systems, controls and legal compliance containing management's statement of assurance over internal controls per Circular A-123.
 - (1) Component entity
 - (2) Federal Government
 - iii) Purposes and Limitations
 - (1) Component entity
 - (2) Federal Government

d) Financial Statements

- i) Overall description (SFFAC 1 and SFFAC 2, par. 54)
- ii) Relationship to the objectives of financial reporting
 - (1) Component entity
 - (2) Federal Government
- iii) Purposes and limitations
 - (1) Component entity
 - (2) Federal Government
- iv) Usefulness of financial statements (individually and collectively)
 - (1) Classification and aggregation in financial statements
 - (2) Complementary nature of financial statements
- v) Describe the types of individual financial statements (for each statement, discuss purpose of the statement and how it contributes to the reporting objectives, the information (see items listed in 8.a.iii) it provides to help achieve the financial reporting objectives) and how the financial statements relate to one another (see GAO-05-958SP). The existing set of financial statements may provide a starting point for consideration. They include:
 - (1) Component entities
 - (a) balance sheet
 - (b) statement of net cost
 - (c) statement of changes in net position
 - (d) statement of budgetary resources
 - (e) statement of financing
 - (f) statement of custodial activities, if applicable
 - (g) statement of social insurance, if applicable
 - (2) Federal Government
 - (a) balance sheet
 - (b) statement of net cost (starting with gross cost)
 - (c) reconciliation of net operating revenue (or cost) and unified budget surplus (or deficit)
 - (d) statement of operations and changes in net position
 - (e) statement of changes in cash balance from unified budget and other activities
 - (f) statement of social insurance

e) Disclosures

- i) Overall description
- ii) Relationship to the objectives of financial reporting
 - (1) Component entity
 - (2) Federal Government

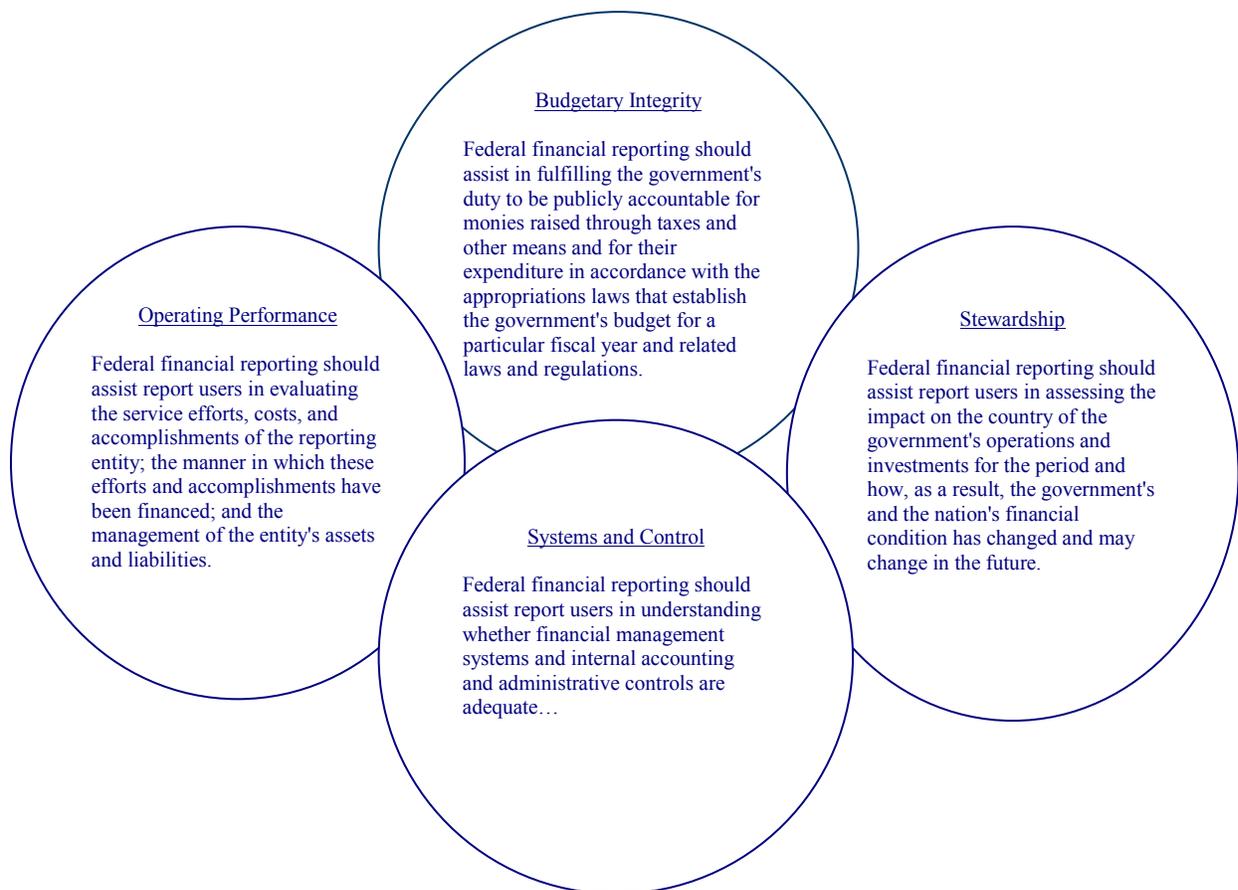
- iii) Purposes and limitations
 - (1) Component entity
 - (2) Federal Government
 - f) RSI (other than MD&A)
 - i) Overall description
 - ii) Relationship to the objectives of financial reporting
 - (1) Component entity
 - (2) Federal Government
 - iii) Purposes and limitations
 - (1) Component entity
 - (2) Federal Government
 - g) OAI
 - i) Overall description
 - ii) Relationship to the objectives of financial reporting
 - (1) Component entity
 - (2) Federal Government
 - iii) Purposes and limitations
 - (1) Component entity
 - (2) Federal Government
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Performance Reporting

Introduction

According to FASAB's *Strategic Directions*, the Board determined that the Operating Performance objective is a primary near-term focus objective. Focusing on the Operating Performance objective permits progress on all of the financial reporting objectives because of their interrelated nature. The Operating Performance objective concerns integrating cost information derived from accrual accounting with performance reporting. In addition, the objective addresses the financing efforts, changes in assets and liabilities over time, and financial sustainability reporting.³ Figure 1 shows each overall financial reporting objective.

Figure 1: Interrelated Federal Financial Reporting Objectives



As part of the Financial Report project, the Board has planned topics that will contribute to this objective and permit progress on others. The recent completion of the fiscal year (FY) 2006 agency Performance and Accountability Reports (PAR) and government-

³ FASAB's *Strategic Directions: Clarifying FASAB's Near-Term Role in Achieving the Objectives of Federal Financial Reporting*, November 2006, p. 16.

wide Consolidated Financial Report (CFR) presents an opportunity to explore aspects of one of the topics - performance reporting.

Performance reporting is a planned segment of the Financial Report project. Staff had planned to use a task force approach similar to the approach used for sustainability reporting and defer work on the segment until the sustainability issues are addressed. In the interim, the Board would monitor the progress on the area. However, recently the financial reporting community has engaged in much discussion on how performance reporting could be improved.

Two subjects that have evolved from the discussions are: 1) the need to establish different levels of reporting information; and 2) the need for improvements in integrating cost information with performance reporting. For instance, two organizations, the National Academy of Public Administration (NAPA) and the Association of Government Accountants (AGA), recently issued research reports that discussed ways of enhancing federal financial reporting and included discussions on performance information. Both reports raised concerns related to the size of Performance and Accountability Reports (PAR) and the need for more integration of information reported, such as the cost of specific programs and the amount spent on achieving results.⁴

In addition, during the 2005 staff roundtable discussions on the objectives of financial reporting, participants noted that the size of the PARs has grown to a level that the document has become overwhelming to read and preparers have difficulty communicating information effectively in the document. The participants also believed that the notion of costs of specific programs and activities is not specifically included in agency financial statements. Given this level of current interest in the PARs, the Board could begin to obtain valuable knowledge on reporting issues and the guidance necessary to assist the financial reporting community.

Role of the Board

Given FASAB's GAAP designation, some in the financial reporting community may question whether FASAB should be involved in providing guidance on performance reporting. However, the Board has a history of leadership in this area and, as noted earlier, the Operating Performance objective is a primary near-term focus objective. The Board has been involved in stressing the importance of reporting relationships among budgetary, financial, and performance information and providing related guidance. For instance, in SFFAS 4, the Board noted that, "Proper financial management requires that the three accounting processes [budgetary, financial, and managerial cost] work closely together to provide useful reporting to both internal and

⁴ *Moving From Scorekeeper to Strategic Partner: Improving Financial Management in the Federal Government*, National Academy of Public Administration, October 2006, p. 21. (<http://www.napawash.org/index.html>). *PAR: The Report We Love to Hate*, Association of Government Accountants, June 2006, p. 16. (<http://www.agacgfm.org/research/publications>).

external users.”⁵ Additionally, the Board has discussed the notion of special purpose reports by explaining in SFFAS 4, par. 56,

Federal financial reporting encompasses general and special purpose reports to meet the needs of the four user groups. Information produced by managerial cost accounting appears in or influences both types of reports. As discussed above, managerial cost accounting should provide information for use by both financial accounting and budgetary accounting. That information is used by those processes in producing both general purpose and special purpose reports.

The Board has also acknowledged the broad nature of performance reporting and, given the evolutionary nature of the standards-setting process, the Board noted that the FASAB may desire to expand parts of the financial and performance reporting framework described in SFFAC 1.⁶ SFFAC 1 paragraph 199 states,

Performance reporting is broader than financial reporting, but good financial reporting is essential to support performance reporting. The GASB has identified three broad categories of measures for reporting on performance of state and local governmental entities: those that measure service efforts, those that measure service accomplishments, and those that relate efforts to accomplishments. Although some performance measures may not be clearly assignable to one of these categories, the categories are helpful for understanding how and where financial reporting can contribute to performance reporting by providing relevant financial information.

In addition, given the changes in the federal financial reporting environment since FASAB issued SFFAC 1, the Board decided to revisit the four financial reporting objectives and obtain feedback from the financial reporting community. During 2005, FASAB staff conducted roundtable discussions on each of the reporting objectives and the participants agreed that the financial reporting objectives were broad and related to a reform initiative to improve the effectiveness and accountability of government. The Board agreed to maintain the broad objectives and determined that it should articulate FASAB’s strategic directions by clarifying the Board’s near-term role in relation to the broad objectives. Upon considering several factors, such as its mission, current language in concepts statements, comparative advantages as a GAAP standard-setter, and evolution of financial management laws and administrative directives, the Board decided that the Operating Performance objective should be the FASAB’s highest priority in the near-term. The objective offered the greatest opportunity for FASAB to play a direct role in achieving the stated objectives.⁷

⁵ SFFAS 4, par. 55.

⁶ SFFAC 1, par. 200.

⁷ *FASAB’s Strategic Directions: Clarifying FASAB’s Near-Term Role in Achieving the Objectives of Federal Financial Reporting*, November 2006.

Levels of Reporting

The PAR primarily evolved from financial management improvement laws. The Chief Financial Officers (CFO) Act of 1990, the Government Performance and Results Act of 1993 (GPRA), the Government Management Reform Act of 1994 (GMRA), and the Reports Consolidation Act of 2000 contributed to the report's development. The CFO Act created 24 chief financial officers for the major executive departments and agencies. In addition to requiring those agencies to prepare and submit audited financial statements for each revolving and trust fund and for accounts that performed substantial commercial functions, the CFO Act required some agencies to have agency-wide financial statements. The GPRA requires agencies to prepare strategic plans, annual performance plans, and annual performance reports. The GMRA substantially expanded the requirements in the CFO Act by requiring audited financial statements covering all accounts in the 24 CFO agencies and authorized a pilot program that allowed an agency to combine its audited financial statement, as required by GMRA, and its performance report as required by GPRA. The Reports Consolidation Act builds on the GMRA pilot program and requires that a consolidated report:

- Shall be referred to as a *Performance and Accountability Report* if it incorporates the agency's GPRA program performance report;
- Contain a summary of the most significant portions of the agency's program performance report, including the agency's success in achieving key performance goals, if the GPRA program performance report is not incorporated;
- Include a statement by the agency's inspector general that summarizes the agency's most serious management and performance challenges; and
- Include a transmittal letter from the agency head containing an assessment of the completeness and reliability of the performance and financial data used in the report.

The Office of Management and Budget (OMB) provides form and content guidance for the PAR. OMB Circular A-136, *Financial Reporting Requirements*, provides this guidance for all agencies and entities required to submit the report.

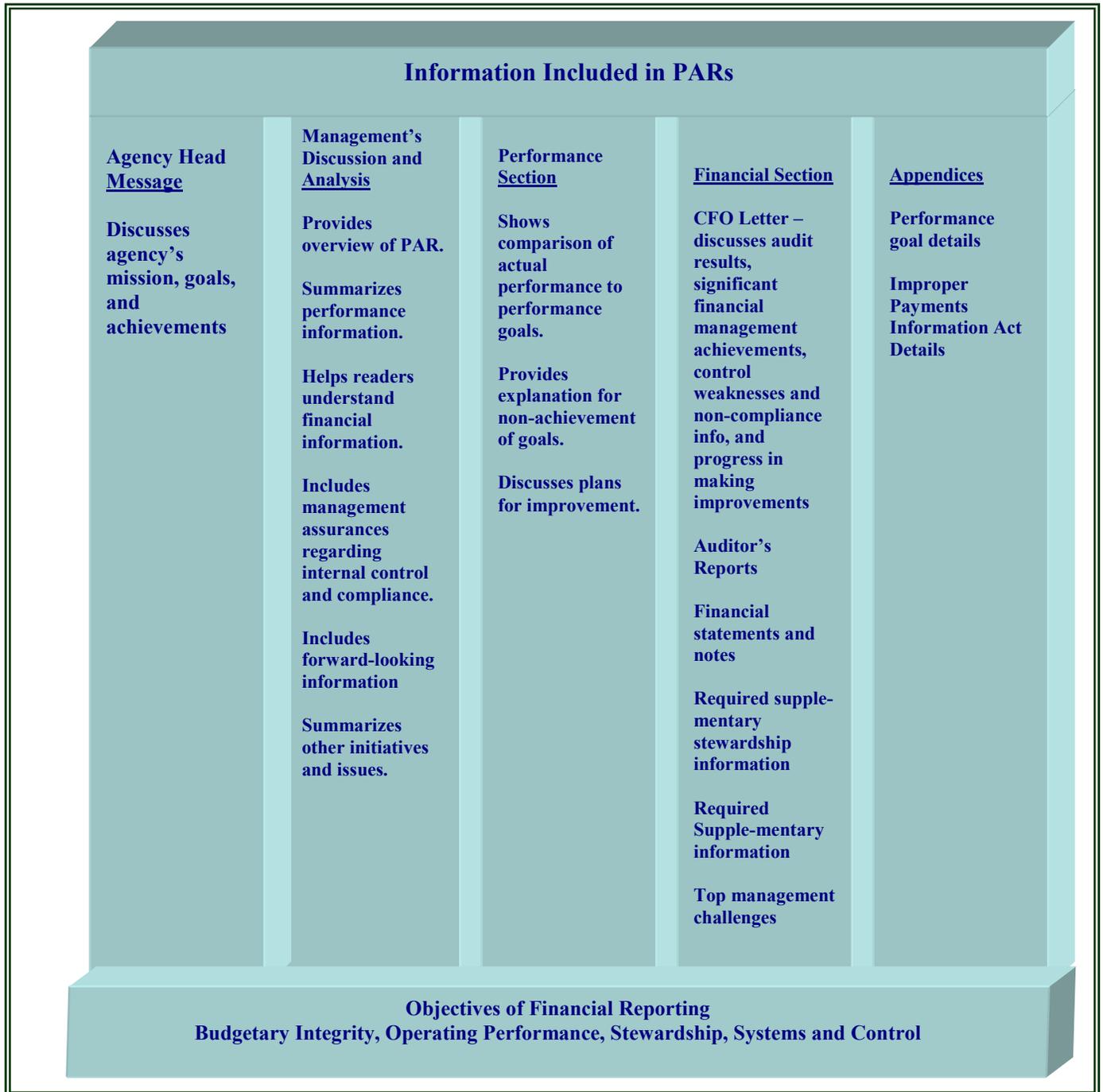
Information Included in PARs

Combining financial and performance information in a single document offers users a wealth of information. Users can gain insights on the cost of federal programs and how they are being managed and have some assurance that the information is reliable. As demonstrated in Figure 2, the PAR includes information such as:

- The agency's mission, goals, and achievements.
- Information on the adequacy of internal control and compliance with laws and regulations.
- Forward-looking information about the possible effects of key existing and anticipated performance and financial demands and trends.

- Comparison of actual performance and performance goals.
- Plans to meet unmet goals.
- Discussion of internal control weaknesses and plans for corrective action.
- Financial statements prepared in accordance with generally accepted accounting principles (GAAP).
- Auditor report on the financial statements, internal control, and compliance with laws and regulations (audits conducted in accordance with generally accepted government auditing standards).
- Auditor's view of the top management and performance challenges.
- Improper payment information.

Figure 2: Information Included in PARs



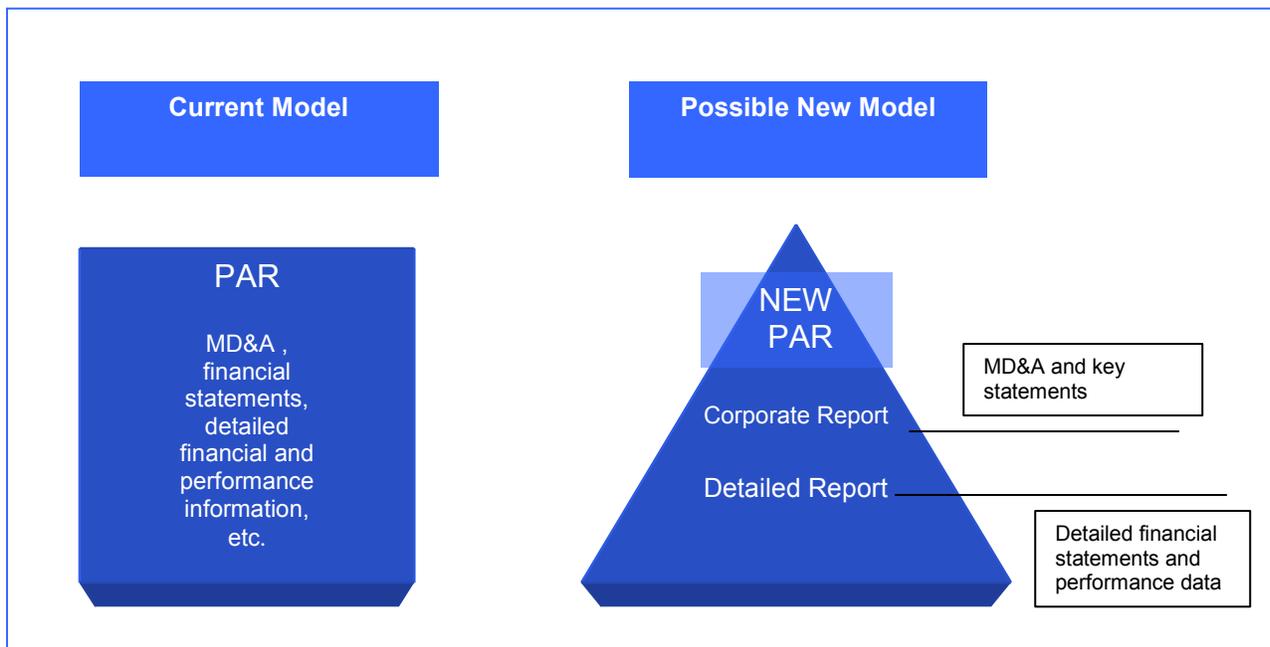
The PAR includes information required by legislation and administrative directives and helps to achieve the objectives of financial reporting. However, when considering the level of information provided in a single document, the PAR has become lengthy and may be difficult for citizens and others to use. In addition, agencies appear to be seeking alternative means of communicating information to users, given the increase

use of ‘summary reports.’ A possible solution to this condition is to provide guidance on different levels of reporting.

During each of our roundtable meetings on the objectives of financial reporting, participants discussed the need for improvement in reporting PAR information and using different levels of reporting was one recommendation that received wide support. The participants discussed that many agencies are moving towards a ‘condensed’ report and they believed that such reports are easier to understand and the general public may find them more useful and interesting. Details of this discussion during the September 19, 2005, Budgetary Integrity Objective Roundtable meeting and the staff analysis are provided in Appendix II.

In addition, others involved in financial reporting have indicated the need for other reporting levels. The Government Accountability Office recently issued a special report entitled, *Understanding Similarities and Differences between Accrual and Cash Deficits*. The report notes that a summary annual report that summarizes important financial and performance information embodied in the CFR could be useful to both Congress and the American people.⁸ Additionally, the OMB encourages agencies to prepare a ‘PAR highlights’ document that highlights important aspects of the PAR and provides interested parties with a more user friendly document. Figure 3 shows a comparison of the current reporting model and a possible new model with multiple levels.

Figure 3: Comparison of Current and Possible New Reporting Models



⁸ *Understanding Similarities and Differences between Accrual and Cash Deficits*, Government Accountability Office, December 2006, GAO-07-1175P, p. 33.

Staff Analysis

Although agencies appear to be moving toward preparing summary reports, the spectrum of information that could be included is broad. As noted in Figure 2, the PAR has an abundance of information from which agencies may choose to present in a summary document. Agencies may choose to focus on performance information and exclude the financial statements and auditor's report. The array of choices could affect comparability among the reports.

Currently, the federal model has vehicles for reporting summarized information. The Consolidated Financial Report (CFR) helps to address citizens' need for highly summarized information. Statement of Federal Financial Accounting Concepts (SFFAC) 4, *Intended Audience and Qualitative Characteristics for the Consolidated Financial Report of the United States Government*, states that "the CFR is a general purpose report that is aggregated from agency reports and tells users where to find information in other formats, both aggregated and disaggregated, such as individual agency reports, agency websites, and the President's Budget." Thus, the CFR works in conjunction with detailed PARs to provide users with information about the federal government as a whole and individual programs.

In addition to the CFR, the management's discussion and analysis (MD&A) provides a vehicle for communicating concise information about an agency. The MD&A could include links to guide readers to more detailed information. The existing requirements for the MD&A are discussed in the staff analysis section of Appendix II.

A model exists for further study on the topic of levels of reporting. The states and local governments (SLG) environment provides examples that could be used in developing guidance for levels of reporting in the federal government. SLGs use 'popular' reports to help citizens understand financial information and the Governmental Accounting Standards Board (GASB) provides guidance on preparing these reports. GASB Concepts Statement No. 1, *Objectives of Financial Reporting*, describes popular reports and the intended audience. The statement notes that popular reports are less detailed than Comprehensive Annual Financial Reports (CAFR) and the reports are intended for users whose financial reporting needs can be satisfied with condensed information. In addition, the National Council on Governmental Accounting Statement 1, *Governmental Accounting and Financial Reporting Principles*, provides criteria regarding popular reports. The statement notes that popular reports should supplement the CAFR and be reconcilable with statements.

Staff Recommendation

During the January 2006 Board meeting, the Board discussed results of the Budgetary Integrity Roundtable and staff noted that there may be value in providing guidance on levels of reporting. In addition, the Board could review this topic further during a strategic planning session. However, at that time, the Board decided to develop and issue a strategic directions document rather than engage in a strategic planning exercise. The resulting document clarified the Board's near-term role relative to each reporting objective.

Given the present level of interest in this topic and the demand for performance information, the Board could revisit the issue. Staff believes that timely guidance on levels of reporting would help facilitate consistency in reporting and help users advance their understanding of the cost of federal programs and the results they achieve. To research the topic, staff plans to conduct roundtable meetings with financial reporting experts and users. Agencies have recently completed the PARs preparation process and their concerns and suggestions for improvement may be "fresh" on their minds. In addition, the roundtable meetings provide an outreach opportunity to educate constituents on Board activities and obtain feedback on possible solutions to issues. Should the Board decide to pursue guidance, Appendix I provides a draft plan for the roundtable meetings.

Cost Accounting and Performance Reporting

Another topic that has received much attention recently is the matter of improving the use of cost accounting for performance reporting. During our September 28, 2005, roundtable meeting, participants discussed that although Statement of Federal Financial Accounting Standard (SFFAS) 4, *Managerial Cost Accounting Concepts and Standards*, requires the notion of costs of specific programs, it was not being accomplished in the financial reports. They noted that some agencies show the total cost of specific goals, but the idea of specific program costs is not specifically included in the financial statements. Appendix III provides an excerpt from the Summary of the Operating Performance Roundtable Meeting that presents additional matters discussed and the staff analysis of the discussion. In addition, as noted earlier, groups have conducted studies that noted the need for improvement in developing cost data in the federal government. For instance, the NAPA report, *Moving From Scorekeeper to Strategic Partner: Improving Financial Management in the Federal Government*, noted that most agencies have not yet implemented cost accounting systems.⁹

⁹ *Moving From Scorekeeper to Strategic Partner: Improving Financial Management in the Federal Government*, National Academy of Public Administration, October 2006, p. 19.

Staff Analysis

As discussed in SFFAS 4, the Board intended that agencies perform managerial cost accounting on a regular basis. In addition, the statement requires that management define responsibility segments and that cost accounting be performed to measure and report the costs of each segment's output. The results of segment performance measurement could support external reporting on performance measures for the agency's programs. The statement also notes that "the topics of cost and performance measurement are related because it is by associating cost with activities or 'cost objectives' that accounting can make much of its contribution to reporting on performance."¹⁰ Thus, SFFAS 4 helps facilitate the linkage to performance reporting.

Other initiatives also help facilitate the use of cost information. For instance, the President's Management Agenda (PMA) includes the Budget and Performance Integration initiative. This initiative directs departments to improve program results and to ensure that performance is routinely considered in funding and management decisions. In addition, the Board has been monitoring cost and performance issues and in 2001 considered a project to assess the effectiveness of SFFAS 4. However, the Board decided that other financial reporting projects warranted higher priority. Appendix III provides additional staff analysis of the roundtable discussion on SFFAS 4 and cost and performance reporting.

Staff Recommendation

During the January 2006 Board meeting, the Board discussed the results of the Operating Performance roundtable meeting and the roundtable participants' concerns regarding the implementation of cost accounting in the federal government. In addition, staff provided the following recommendation.

While there has been significant progress in improving federal financial management, challenges such as establishing financial management systems that provide reliable, timely, and useful information to support day-to-day decision-making and oversight and for the systematic measurement of performance remain.¹¹ Given the time that has elapsed since SFFAS 4 was issued, and the flexibility afforded in its implementation, more progress in achieving the standard may have been expected. The Board may want to reconsider a project devoted to assessing the effectiveness of SFFAS 4 during the next agenda setting process. In addition, as part of the strategic planning process, the Board should consider whether additional vehicles and the types of vehicles that may be needed to enhance the progress in implementation. The Board would need to remain aware that others such as OMB have initiatives on-going and are able to provide more prescriptive guidance. However, staff does not believe there is a need to enhance the reporting objective or to immediately address standards regarding the issues identified above.

At that time, the Board decided to develop and issue a strategic directions document rather than engage in a strategic planning exercise. As discussed earlier, the strategic

¹⁰ SFFAS 4, *Managerial Cost Accounting Concepts and Standards*, par. 58.

¹¹ See GAO-06-242T, CFO ACT OF 1990: Driving the Transformation of Federal Financial Management, November 17, 2005.

planning document would clarify the Board's near-term role relative to each reporting objective.

With the matter of cost and performance reporting presently being deliberated in the financial reporting community, staff believes that this may be an opportune time to consider an educational session on SFFAS 4 and cost accounting. The session could serve dual purposes – to inform constituents and obtain feedback on how FASAB can assist in improving progress. The session could emphasize the value of developing cost information and have presentations of best practices in implementing managerial cost accounting and linking that information to performance reporting. Participants may also discuss how cost information has been used to improve decision-making and enhance operations. Presenters from federal and SLG may be invited to share their experiences.

Moreover, the session could be beneficial for FASAB. The educational session provides a venue for the Board to obtain ideas on whether constituents need additional guidance and an opportunity to gain insights on whether improvements are needed regarding the Statement of Net Cost. Staff plans to review the Statement of Net Cost as part of the Financial Report project and staff information gained from the education session could be used in conducting the review. Enhancements may be needed to facilitate the reporting of program costs.

Should the Board decide to pursue this option, staff will prepare a plan for the session and present it to the Board at the March 2006 Board meeting.

APPENDIX I – Draft Plan for Roundtable Meetings on Levels of Reporting**Objective**

To determine what guidance, if any, is needed to improve the reporting of financial and performance information, presently presented in Performance and Accountability Reports (PAR). The roundtable meeting results may lead to report users having reports useful for 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. In addition, the roundtable results may lead to improved comparability of reports from different agencies.

Proposed Meeting Dates

February 22, 2007

March 28, 2007

Proposed Venue

Government Accountability Office (GAO)
441 G St NW - Room 7C13
Washington DC 20548

Proposed Roundtable Composition

Plan to include individuals from the following:

OMB

GAO

Treasury

CBO

IG audit community

CFO financial statement preparation community

IPA firms

Public Interest Groups

Subject matter experts

Proposed Topics

- I. Current Model
 - a. Overview of the current PAR
 - i. Evolution of legislation
 - ii. Information reported
 - b. Purpose and Benefits of the PAR
 - i. What internal benefits have been noted?
 - ii. What are some benefits to external users?
 - c. Current Practices
 - i. Summary or Highlight reports
 1. Reasons for their use
 2. Benefits achieved
 3. Issues noted

- II. Possible Changes
 - a. Discuss views on areas for improvement
 - i. Some recent reference materials
 1. Moving From Scorekeeper to Strategic Partner: Improving Financial Management in the Federal Government, National Academy of Public Administration, October 2006, p. 21. (<http://www.napawash.org/index.html>).
 2. PAR: The Report We Love to Hate, Association of Government Accountants, June 2006, p. 16. (<http://www.agacgfm.org/research/publications>).
 - ii. How can the management's discussion and analysis (MD&A) be better utilized?
 - iii. Consider state and local government use of popular reports
 1. See *A Report to the Citizens of the Commonwealth of Virginia: Virginia Financial Perspective for the Fiscal Year Ended June 30, 2005*, (http://www.doa.virginia.gov/Financial_Reporting/PAFR/PAFR_Main.cfm) for an example of a popular report.
 - b. Different levels of reports
 - i. What information should be included in each level?
 - ii. What criteria should be used?
 - c. FASAB's role
 - i. What should be the FASAB's role?

III. Implication of Changes

- a. Discuss impact of possible changes
 - i. Contribution to reporting objectives and benefit to users
 - ii. Practical problems, including additional accounting costs
 - iii. Others
- b. Among the alternatives discussed, what changes would be most useful?

**Draft Plan for Roundtable Discussions on
Levels of Reporting**

Example Agenda

9:00 – 9:10	Introductions and Overview of Project
9:10 – 10:30	Group Discussion
10:30 – 10:45	Break
10:45 – 11:55	Group Discussion
11:55 – 12:00	Wrap-up

APPENDIX II - Excerpt from *Summary of the Budgetary Integrity Roundtable Meeting, September 19, 2005***Other Report Formats and Other Guidance Vehicles**

Several participants commented that some of the PARs are over 500 pages in length and are overwhelming to read. The participants agreed that it is a struggle to clearly communicate the information effectively in the PARS. The participants noted that many agencies are moving towards a 'popular report' or a 'condensed report' and believed that the general public may find those much more useful and interesting. One participant commented that condensed reports are easier for the public to understand. Participants agreed that summary reports with a link to the detailed report would be an improvement. The participants discussed that FASAB may want to consider the requirements for the popular or condensed reports.

The participants discussed the use of multiple reports to convey different information. The participants believed that the current financial statement reports are blended and contain what some might consider special reports along with general-purpose financial statements. Certain participants commented that if the Board took the approach of multiple reports, the Board could consider what it wants a particular report to communicate. The participants expressed interest in the Board using multiple reports, some for external users and other reports that focus on internal users. Additionally, the participants discussed that FASAB could in theory have a whole series of types of pronouncements that address issues such as budgetary reporting or performance reporting. The participants discussed that these pronouncements could be for special reports and not for producing GAAP financial statements.

The participants discussed the use of multiple reports by reporting entities and special report guidance from GASB in the state/local government arena as a possibility. For example, GASB developed a special report regarding suggested criteria for effective performance reporting. This report did not have authoritative status but provided criteria for performance reporting. The participants discussed that FASAB could develop similar reports depending on the objective they would like to achieve. The participants discussed that similar to GASB, FASAB could setup a tool that is prescriptive for a special report on accounts and that the auditors could use as a benchmark to test this separate report.

The participants acknowledged that standards-setters typically use tools such as concept statements, standards, and implementation guidance. The ones with force are the standards and implementation guidance. These come into play when an entity is producing a GAAP set of financial statements and seeking an audit opinion. FASAB could in theory have a whole series of pronouncements that address detailed budgetary

account reporting and place these pronouncements under a category such as standards of budgetary reporting. These standards would be used to judge the report and, as a special report, the report would not be a part of the financial statements.

The participants also discussed that the special reports could alternatively be accomplished through guidance produced by OMB instead of FASAB. Specifically, the participants discussed that one could envision an attestation engagement that would not necessarily need a FASAB pronouncement. Specifically, OMB could prescribe how information should be prepared or give a common set of guidelines to all agencies and require that an auditor attest against it.

Staff Analysis:

Reporting vehicles that are shorter in length and containing condensed or summarized information may offer some benefits to users. For instance, readability may be enhanced and information may be more readily obtained. For the general public in particular, condensed reports can be designed to enhance the citizen's understanding of financial information. State and local governments have been using condensed reports called "popular reports" to communicate financial information to citizens and some federal agencies are starting to use summary reports or "highlights" to communicate information to citizens about their organizations. While there may be benefits to these reporting vehicles, some users require detailed information to assist them in managing and monitoring government programs. Also, the Management's Discussion and Analysis (MD&A) section of financial reports is intended to communicate financial and performance results in a concise, readable manner for a broad audience.

State and local governments have been utilizing popular reports to help make financial information easier for citizens to understand. For example, the popular report for the Commonwealth of Virginia notes that information in the financial statements are technical and complex and, as a result, the full financial statements may not be particularly useful to the citizens who wish to better understand state government finances. The popular report is intended to better inform the public about their government's financial condition, without excessive detail or the use of technical accounting terms.

GASB notes that external reports include popular reports and Comprehensive Annual Financial Reports (CAFRs). The popular reports are less detailed and are often intended for users whose financial reporting needs are better satisfied through more condensed information. CAFRs are more detailed and are intended for users who need a broad range of information. Both popular reports and CAFRs may include such nonfinancial information as statistical data, analytical data, demographic information, forecasts, economic and service delivery statistics, legally required data, narrative explanations, and graphic displays.¹²

¹² GASB Concepts Statement No. 1, Objectives of Financial Reporting, paragraph 6.

In addition, similar to FASAB, the GASB considered that some financial reporting objectives can be met by means of reporting beyond the general purpose financial statements (GPFS) and outside the CAFR, such as in the popular report. In its Concepts Statement No. 1, Objectives of Financial Reporting, paragraph 91, the GASB stated,

...developing and implementing standards to achieve these objectives will be an ongoing and evolutionary process. The Board has no preconception of precisely how an individual objective will be met. It is likely that some objectives will be accomplished in the GPFS without significant extension of the GPFS's scope. It is also likely that other objectives will be better accomplished by some means of reporting beyond the GPFS—in the CAFR, for example. In addition, some objectives may be met by standards developed for means of reporting outside the CAFR—in condensed "popular" reports, for example. The Board will determine—on a standard-by-standard basis—the best means of financial reporting, and only after full due process. The Board believes that it is unlikely that all of the objectives will be, or can be, met through a single means of reporting, such as the GPFS.

When summarizing information, decisions need to be made to determine what information should be included and how it should be presented to ensure consistency with the more detailed report. Regarding criteria for reporting information in the state and local government popular reports, the National Council on Governmental Accounting Statement 1, Governmental Accounting and Financial Reporting Principles notes that

...such statements should supplement, rather than supplant, the CAFR and the separately issued GPFS. Further, the Council believes that the data in such highly condensed summary statements should be reconcilable with the combined, combining, and individual fund and account group statements, and that the reader of such statements should be referred to the CAFR and/or the separately issued GPFS of the governmental unit. (paragraph175)

In the federal environment, agencies are starting to use summary or highlight reports in addition to the PARs. The number of agencies using summary reports increased from five for FY 2002 to seven for FY 2003. This increase probably resulted from the view that PARS were lengthy. Agencies needed to include all the prescribed materials in a single document that was primarily of interest to persons in oversight roles, such as OMB. Agencies perhaps used the summary report because they sought ways to demonstrate accountability to constituents, stakeholders, new employees, members of Congress and others with less extensive information.¹³ The length of the summary

¹³ Accountability Reporting Trends & Techniques: A survey of Federal Agencies' Accountability Reporting Practices, KPMG, Summer 2004, pp. 91,

reports for FY 2003 ranged from 24 to 84 pages,¹⁴ while the length of PARs ranged from 123 to 564 pages.¹⁵

Also, OMB is encouraging the use of highlight reports. OMB Circular A-136, Financial Reporting Requirements, provides federal financial reporting guidance for Executive branch departments, agencies, and entities required to submit audited financial statements and PARs. The circular encourages a brief highlight version of the PAR. Section 2.2 – Format of the PAR, footnote 2, states,

Agencies are also encouraged to develop a brief highlights version of the annual PAR. The PAR Highlights should exist as a standalone document, presenting key findings and relevant financial and performance data. Agencies should prepare the highlights document in a manner and writing style appropriate for the general public. Agencies may find it useful to prepare a PAR highlights with a CD of the entire PAR document included as an alternative to distributing numerous printed copies of the entire PAR document.

Although the number of agencies using summary reports appears to be increasing, some of the information contained in the reports varied. All seven summary reports prepared for FY 2003 were drawn from the PARs. However, only four agencies specifically mentioned the PAR and directed the reader to the PAR for more detailed information. In addition, although all of the seven reports included performance results, only four included financial statements and the auditor's report.¹⁶

It should be noted that a vehicle for communicating information in a concise manner already exists. The MD&A section of each financial report is intended to provide concise information on an agency's financial and performance results and to describe these results in a manner that is readable to a broad audience. SFFAC 3, Management's Discussion and Analysis, issued April 1999, states,

MD&A is an important vehicle for (1) communicating managers' insights about the reporting entity, (2) increasing the understandability and usefulness of the GPFRR (general purpose federal financial report) and (3) providing accessible information about the entity and its operations, service levels, successes, challenges, and future.(Summary)

MD&A should address the reporting entity's program and financial performance measures, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address problems. The discussion and analysis of these subjects may be

¹⁴ Ibid, p. 91,

¹⁵ Ibid p. 5

¹⁶ Ibid pp. 92-93,

based partly on information contained in reports other than the GPFFR. MD&A also should address significant events, conditions, trends and contingencies that may affect future operations. (paragraph 1)

A Federal reporting entity's GPFFR should be understandable and useful to a wide audience, not just members of the entity's management and specialized analysts working for special interest groups, corporations, and other entities affected by the Government's actions. Therefore, the report should be accompanied by a concise narrative discussion and analysis. Even insiders and specialized analysts often need such a discussion and analysis to understand the report. Communication with a wide audience may require effective use of colors, graphs, photographs, and charts. Reporting understandable, accessible information on the Government's actions and the effects of its actions helps assure accountability and provides a more "level playing field" on which the public interest can best be served. (paragraph 5)

Also, like a summary report, the MD&A could include links to direct the reader to more detailed information.

Summary/highlight reports is an area that is newly evolving in the federal environment which may require further study. SFFAC1 notes,

35. The FASAB recognizes that developing and implementing standards that will contribute to achieving certain objectives may take considerable time. Time will be needed to establish information-gathering systems and to gain experience by experimenting with alternative approaches.

36. The FASAB expects that some of these objectives may best be accomplished through means of reporting outside general purpose financial reports. Indeed, the FASAB recognizes that information sources other than financial reporting, sources over which the FASAB may have little or no influence, also are important to achieving the goals implied by these objectives.

37. In developing specific standards, the FASAB will consider the needs of financial information users, the usefulness of the information in relation to the cost of developing and providing it, and the ability of accounting standards to address those needs compared with other information sources.

Based on the government-wide efforts to streamline reporting requirements and to consolidate reporting (Reports Consolidation Act), it appears that exploring multiple reports would not be consistent with these efforts. However, encouraging the use of a summary report with links to detailed reports and information does seem to be a

plausible way to clearly communicate what agencies are reporting. This could be particularly beneficial at the CFR level. At the CFR level, users can gain insights into the financial operations and condition of the federal government as a whole. Also, effectively utilizing the MD&A section of financial reports may achieve similar results.

APPENDIX III – Excerpt from *Summary of the Operating Performance Roundtable Meeting, September 28, 2005***Cost Accounting Issues and SFFAS 4, *Managerial Cost Accounting Concepts and Standards***

Certain participants discussed the belief that the least has been completed to achieve sub-objective 1, which states “Federal financial reporting should provide information that helps the reader to determine the costs of providing specific programs and activities and the composition of, and changes in, these costs.” The participants discussed that even though SFFAS 4 requires the notion of costs of specific programs, it is not being accomplished or reported in the published financial reports. The participants discussed that although some agency financial statements show the total costs of strategic goals, the notion of costs of specific programs and activities, is not specifically included in the statements.

Certain participants suggested that FASAB could ascertain and address the conditions that are impeding the implementation of SFFAS 4. Additionally, participants expressed that FASAB could focus on standards to ensure the inclusion of full costs and improve the alignment of budget accounts with the programs for which costs are reported.

The participants discussed the level of understanding regarding what the cost accounting system should produce, and they discussed their views on SFFAS 4’s contribution to cost accounting at agencies. SFFAS 4 was developed in response to one of the requirements in the National Performance Review (NPR). The NPR required that FASAB produce, within 18 months, a cost accounting standard. The Board did proceed and produced the standard, which is our cost accounting standard. Essentially, the goal of the standard is full cost on an accrual basis of the program, and divided by segments. The participants noted that SFFAS 4 drives what is presented on the face of the Statement of Net Cost, as well as the additional note disclosures that agencies prepare to get the information to a finer level. The participants expressed concern that the standard does not require explicitly that the statement of net cost match the goals under GPRA, and align with all of the other efforts.

The participants noted other matters regarding SFFAS 4. The participants discussed that it is possible for agencies to receive a clean opinion on their financial statements but not have adequate systems to adhere to accounting standards such as SFFAS 4. However, the auditor’s work on agency compliance with laws and regulations can provide an indication of whether agencies are actually determining the cost of providing specific programs.

Also, certain participants believed that SFFAS 4 did not go far enough. Specifically, one participant commented that it talked about concepts and not enough about

requirements. A participant also noted that it allowed manual or non-computerized accounting for costs and was not strong enough to get agencies to change their behavior. Because agencies use many different systems, there needs to be an effort to integrate financial systems with the larger performance measurement system. This could help achieve the integration of performance and financial information as discussed above.

It was noted that SFFAS 4 does have strengths. For example, SFFAS 4 does set forth the requirement for entities to accumulate and report the costs of its activities on a regular basis for management purposes. Additionally, it sets forth the requirement for entities to report the full costs of outputs. Also, SFFAS 30, *Inter-entity Cost Implementation*, will require full implementation of the inter-entity cost provision in SFFAS 4. Specifically, SFFAS 30 will require that each entity's full cost incorporate the full cost of goods and services that it receives from other entities in FY 2009. The participants noted that although this will help show the cost of running an agency, agencies have a problem with accounting for costs that they cannot control or influence the quality of the service.

In addition, the participants agreed that some education on cost accounting and SFFAS 4 would be helpful. The participants discussed that program staff members need to understand the utility in this information. The participants discussed that perhaps identifying an "access point" to the persons responsible for results would facilitate education. For example, in private industry, a comptroller could institute a cultural concern with cost and cost drivers. The participants discussed that a comparable position in the federal government could be the CFO or CIO. However, the structure of agencies could be a factor that hinders progress in this area. As noted earlier, program managers often do not have control over all the resources that support their programs.

Staff Analysis and Recommendations:

With the issuance of SFFAS 4, the Board intended that agencies perform managerial cost accounting on a "regular basis." SFFAS 4, paragraph 68, describes regular basis as follows,

To perform managerial cost accounting on a "regular basis" means that entities should establish procedures to accumulate and report costs continuously, routinely, and consistently for management information purposes. Consistent and regular cost accounting is needed to meet the second objective of federal financial reporting which states information should be provided to help the user determine the costs of providing specific programs and activities and the composition of, and changes in those costs. That objective also requires the reporting of performance information of federal programs and the changes over time in that performance in relation to the costs.

SFFAS 4 also requires that management of each reporting entity define and establish responsibility segments and that managerial cost accounting should be performed to measure and report the costs of each segment's outputs. SFFAS 4 explains the purpose for responsibility segments, which includes the following—provide a vehicle for accumulating costs incurred by the segment to match with its outputs, facilitate cost control and management, provide useful information in support of financial reporting by components. In addition, SFFAS 4 provides the linkage to performance reporting as follows:

85. For internal management, segmentation could also facilitate performance measurement. Since each segment is responsible for a mission, or a line of activity to produce a certain type of output, performance goals can be set for each segment based on its specific tasks and operating patterns. Information on costs, outputs, and outcomes related to each segment can be used to measure its performance against the goals. The results of the segment performance measurement could also support external reporting on performance measures for the entire reporting entity or its major programs.

SFFAS 4 provides flexibility to management in establishing segments by providing in par. 86 that “Reporting entity management should define and structure its responsibility segments. The designation of responsibility segments should be based on the following factors: (a) the entity's organization structure, (b) its lines of responsibilities and missions, (c) its outputs (goods or services it delivers), and (d) budget accounts and funding authorities. However, the predominant factor is the reporting entity's organization structure and its existing responsibility components, such as bureaus, administrations, offices, and divisions within a department.” Although SFFAS 4 does not explicitly state that the segments should be the same as programs identified under GPRA, there is sufficient flexibility and language that encourages segmentation to facilitate performance measurement reporting.

In a recent Government Accountability Office (GAO) report entitled, *Achieving FFMIA Compliance Continues to Challenge Agencies* (GAO 05-881, issued September 2005), it was noted that despite becoming effective in 1998, SFFAS 4 remains particularly difficult for agency financial managers to fully implement. This difficulty appears to exist even with the Board affording agencies a level of flexibility in implementing the standard. SFFAS 4 states,

70. The managerial cost accounting processes consist of collecting data from the common data source, processing that data, and reporting cost and output information in general purpose and special purpose reports. Appropriate procedures and practices should also be established to enable the collection, measurement, accumulation, analysis, interpretation, and communication of cost information. This can be accomplished through the use of a cost accounting system or the use of cost finding techniques and other cost studies and analyses. A cost accounting “system” is an organized grouping of methods and activities designed to consistently produce reliable cost information.

71. *Regardless of whether a reporting entity uses a cost accounting system or cost finding techniques, the methods and procedures followed should be designed to perform at least a certain minimum level of cost accounting and provide a basic amount of cost information necessary to accomplish the many objectives associated with planning, decision making, control, and reporting. The more important of these minimum criteria for cost accounting are associated with the standards in the remainder of this statement. Others are also important.*

Responsibility Segments - Cost information should be collected by responsibility segments which have been identified by management and outputs should be defined for each responsibility segment.

Full Costing - Each reporting entity should measure the full cost of outputs so that total operational costs and total unit costs of outputs can be determined. "Full cost" includes the cost of goods or services provided by other entities when the applicable criteria are met.

Costing Methodology - The costing methodology used (e.g., activity-based costing, job order costing, standard costing, etc.) should be appropriate for management's needs and the operating environment.

Performance Measurement - Cost accounting should provide information needed to determine and report service efforts and accomplishments and information necessary to meet the requirements of the GPRA or interface with a system that provides such information. This includes the quantity of inputs and outputs and other non-financial information needed in the measurement of performance.

Reporting Frequency - Cost information should be reported in a timely manner and on a regular basis consistent with the needs of management and the requirements of both budgetary and financial reporting.

Standard General Ledger - Managerial cost accounting should be integrated with general financial accounting. Both depend on the standard general ledger for basic financial transaction data.

Precision of Information - Cost information supplied to internal and external users should be reliable and useful in making evaluations or decisions. At the same time, unnecessary precision and refinement of data should be avoided.

Special Situations - The managerial cost accounting processes should be designed to accommodate any of management's special cost information needs that may arise due to unusual or special situations or

circumstances. If such cost information is needed on a regular basis, appropriate procedures to provide it should be developed.

Documentation - All managerial cost accounting activities, processes, and procedures should be documented by a manual, handbook, or guidebook of applicable accounting operations. This reference should outline the applicable activities, provide instructions for procedures and practices to be followed, list the cost accounts and subsidiary accounts related to the standard general ledger, and contain examples of forms and other documents used.

72. While each entity's managerial cost accounting should meet the basics discussed above, this standard does not specify the degree of complexity or sophistication of any managerial cost accounting process. Each reporting entity should determine the appropriate detail for its cost accounting processes and procedures based on several factors. These include the:

- nature of the entity's operations;*
- precision desired and needed in cost information;*
- practicality of data collection and processing;*
- availability of electronic data handling facilities; cost of installing, operating, and maintaining the cost accounting processes; and*
- any specific information needs of management.*

Also, agencies could use a gradual approach to the development of cost systems while developing basic cost information through other means in the short run (paragraph 266).

The Board's flexibility permits others to develop more prescriptive guidelines. It should be noted that the President's Management Agenda (PMA) does include the Budget and Performance Integration initiative. This initiative directs departments to improve program results and to ensure that performance is routinely considered in funding and management decisions. The standards for success in this initiative includes the area of reporting the full cost of achieving performance goals accurately in budget and performance documents and accurately estimate the marginal cost of changing performance goals.

In addition, the GAO report discussed some current initiatives in the federal government that can help address financial management system issues. One initiative is OMB's task forces to conduct a government-wide analysis of lines of business that support the PMA goal to expand electronic government. The purpose of the Line of Business (LOB) initiative is to develop business-driven, common solutions for lines of business that extend across the entire federal government. The lines of business are financial management, human resources management, grants, federal health architecture, and case management. These lines of business share similar business requirements and processes. OMB and designated agency LOB task forces plan to use enterprise architecture-based principles and best practices to identify common solutions for

business processes, technology-based shared services, or both to be made available to government agencies. The solutions are expected to address business improvements to enhance government's performance and services.

Also, OMB established agency task forces that focused on developing Centers of Excellence (COE). The purposes of the COE's are to (1) reduce the number of systems that each individual agency must support, (2) promote standardization, and (3) reduce the duplication of efforts.

The Board has been monitoring cost and performance issues in the federal government, and in 2001, considered a project designed to assess concerns similar to those expressed by the participants, including assessing the effectiveness of SFFAS 4, whether the objectives of the standards are being met and, if not, options for the Board in improving the effectiveness of the standard. However, the Board determined that other financial reporting projects warranted higher priority.