



October 9, 2009

Memorandum

To: Members of the Board

From: Melissa Loughan, Assistant Director
Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subj: **Federal Entity-Tab G¹**

MEETING OBJECTIVE

The primary objective for the October Board meeting is to discuss the revised principles and related criteria for defining the boundaries of the federal reporting entity so that staff can continue working towards an Exposure Draft (ED) on the Federal Reporting Entity.

BRIEFING MATERIAL

This transmittal memorandum includes a Staff Discussion and Questions for the Board starting on the next page which will guide the discussion and includes specific questions for the Board members. In addition, the following items are attached:

1. Revised Principles and Related Criteria for Boundaries of the Federal Reporting Entity
2. Flowchart Depicting Boundaries of the Federal Reporting Entity and Display
3. Project History

BACKGROUND

At the August 2009 meeting, staff provided the Board with a summary of the most recent Federal Entity Task Force meeting. The Board also discussed a staff paper related to federal government interventions. The paper presented the federal government with its broad responsibilities may be required to take certain actions or

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.

intervene in certain situations that are deemed necessary and that consolidation of these types of organizations may lead to less meaningful presentation. The Board agreed federal government interventions such as the types detailed in the staff paper should not be consolidated. The Board determined there should be one category for temporary and that temporary can be more than one year, but not permanent. The Board also briefly discussed options for display for organizations that aren't consolidated. The Board directed staff to continue working toward an Exposure Draft and incorporate the issues agreed upon regarding interventions and the temporary exclusion.

NEXT STEPS

Staff will address Board members' concerns and input on the revised principles and work towards developing an ED on the Federal Reporting Entity. Staff will also develop proposals for the alternative display and disclosures, once the principles and criteria have been agreed upon.

Staff is also working with representatives from the Federal Reserve on performing an assessment of how the Federal Reserve would be presented based on the draft principles. A briefing with the Federal Reserve and Federal Entity Task Force has been scheduled for November 18th. Staff plans to provide the Board with a summary of the briefing at the December meeting.

STAFF DISCUSSION AND QUESTIONS FOR THE BOARD

As you may recall, the Board expressed concerns with the potential consolidation of many previously unconsolidated organizations based on the proposed principles and related criteria in the previous draft. Although much outreach had already taken place on the proposed principles via a survey to the financial management community, this work pre-dated many of the recent economic stabilization activities and the Board suggested the task force consider the complexities of ownership and control criteria further.

At the most recent Federal Entity Task Force Meeting, the task force discussed the principles that define an entity as being within the boundaries of the federal reporting entity. The task force agreed the principles should be revised so that financial accountability (inclusion in the budget) would be the first test or conclusive principle for being within the boundaries of the federal reporting entity versus legal status or stating within the three branches as in the previous draft principles. The task force also agreed with making the other principles second tier / indicative principles that would be assessed after determining if the entity meets the conclusive principle. Staff developed revised principles (which have been reviewed by the task force and their comments have been incorporated) for the Board's consideration.

The major revisions in this Draft Principles include:

- Directly Financially Accountable is a Conclusive Principle
- Indicative Principles include other entities not meeting the Conclusive Principle. It may include entities:
 - Existing as a matter of law within or established by the federal government to fulfill a public purpose or federally related mission;
 - Over which the federal government has the ability to exercise control with expected benefits or risk of loss; or
 - In which the federal government has a majority ownership interest.
- Added the principle “Federal reporting entities should also include entities not meeting the conclusive or indicative principles if the nature and significance of their relationships with the federal government are such that the exclusion would cause the federal reporting entity financial statements to be misleading or incomplete.”
- Updated the Temporary Exclusion. Temporary includes conditions that are not likely to remain in existence permanently.
- Added section on Consolidation and Disclosures for determining which organizations should be consolidated versus other presentation and disclosures based on the principles met. Section includes a chart that would depict how indicative principles being met would lead to either consolidation or alternative display and disclosures.
- Briefly introduced Related Parties and how this can be brought into this standard.
- Included a FLOWCHART for Determining the Boundaries of the Federal Reporting Entity and Display

As noted, the principles were revised to include the Conclusive Principle for directly financially accountable “Federal reporting entities include all entities that the federal government is directly financially accountable for. This includes entities in the program and financing schedules of the *Budget of the United States Government* (the President’s budget) as well as those entities the federal government has an ownership interest of 100%.” The task force believes the revised principles results in an approach that will capture the majority of entities within the boundary of the federal reporting entity by first assessing entities against the conclusive principle of Directly Financially Accountable. This is also consistent with concepts in our current Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display*.

The budget is a political document serving many purposes. The 1967 *Report of the President’s Commission on Budget Concepts* indicates that “the budget must serve simultaneously as an aid in decisions about both the efficient allocation of resources among competing claims and economic stabilization and growth.” On the topic of coverage of the budget, the Commission recommended that “the budget should, as a general rule, be **comprehensive of the full range of Federal activities**” and included specific recommendations on matters then considered controversial.

Staff believes that a decision by the Office of Management and Budget or the Congress to include an entity in the budget settles the matter of the entity being “federal.” Inclusion in the budget means that allocation of resources to its activities is determined through federal legislation – making the entity itself financially accountable to Congress and OMB. Financial reporting objectives – budgetary integrity, operating performance, stewardship and systems and controls – could not be met if entities included in the budget were not included in the financial reports.

The conclusive principle represents a starting point in analysis but does not mean that entities not addressed in the budget should be excluded. Because the budget’s purposes differ from financial reporting objectives in many respects (such as the forward looking focus of the budget and decisions on the allocation of resource flows), it is possible that entities or activities might be excluded from the budget for reasons that do not justify exclusion from financial reports. For example, in addressing the recommendation that transactions with the International Monetary Fund reflecting net changes in the U.S. position with the fund be excluded from the budget, the Commission indicated that these transactions are essentially exchanges of one monetary asset for another. Since federal reporting objectives address management of assets and liabilities, the Board may reach a different conclusion than the Commission. The indicative criteria are necessary to ensure completeness in the context of the federal financial reporting objectives.

1. **Does the Board agree with the Conclusive Principle of Directly Financially Accountable being the first assessment for determining whether an entity is within the boundaries of the federal reporting entity?**
2. **Does the Board have any comments or suggestions about the Conclusive Principle and Criteria -- Directly Financially Accountable? See paragraphs 14 through 25 in the *Revised Principles and Related Criteria for Proposed Standards*.**

The revised approach also now includes Indicative Principles. The Indicative Principles (Existing as a matter of law within or established by the federal government to fulfill a public purpose or federally related mission; Over which the federal government has the ability to exercise control with expected benefits or risk of loss; or In which the federal government has a majority ownership interest) is the second test for determining whether an entity is within the boundaries of the federal reporting entity.

As noted in the proposed Standard, this assessment is done only against entities that were not captured with the conclusive principle. This approach is also consistent with the concepts presented in SFFAC 2. The indicative principles are the most complex and require detailed criteria for assessing if they are met and obviously are much more subjective. However, the task force believes the criteria provided in the proposed Standard complements what is presented in SFFAC 2 and should enable users to make these assessments in a more consistent manner.

3. **Does the Board agree with the Indicative Principles and with them being the second test for determining whether an entity is within the boundaries of the federal reporting entity?**
4. **Does the Board have any comments or suggestions about the “Existing as a matter of law within or established by the federal government” indicative principle and related criteria? See paragraphs 27 through 33 in the *Revised Principles and Related Criteria for Proposed Standards*.**
5. **Does the Board have any comments or suggestions about the “Control” indicative principle and related criteria? See paragraphs 34 through 46 in the *Revised Principles and Related Criteria for Proposed Standards*.**
6. **Does the Board have any comments or suggestions about the “Majority ownership interest” indicative principle and related criteria? See paragraphs 47 through 51 in the *Revised Principles and Related Criteria for Proposed Standards*.**

The task force also believed adding the principle “Federal reporting entities should also include entities not meeting the conclusive or indicative principles if the nature and significance of their relationships with the federal government are such that the exclusion would cause the federal reporting entity financial statements to be misleading or incomplete.” would help to ensure that the proposed Standard could accommodate rare or unique situations that may arise in the future. Staff notes this was in an earlier version that was circulated and agreed upon by the community in a survey last year. However, certain Board members requested that it only be included if there were specific examples that could be included. Staff notes including something along these lines would be consistent with concepts in SFFAC 2. Additionally staff notes in our joint meeting with GASB, we learned it was important for them to have similar language for unique situations the standard may not address.

7. **Does the Board agree with adding the Misleading to Exclude principle in the proposed Standard?**
8. **Does the Board have any comments or suggestions on the language included for this principle? See paragraphs 52 through 55 in the *Revised Principles and Related Criteria for Proposed Standards*.**

Staff updated the Exception for Temporary Conditions to reflect the fact that temporary are situations where the conditions are not likely to remain in existence permanently. Staff also included language specific to long-term interventions and proposed disclosures for entities meeting the temporary exclusion. Staff also included language for Agency Mission-Related Interventions in an Entity as a separate exception to note that certain agencies do interventions as part of their mission and naturally may not require as detailed disclosures as the temporary conditions.

9. **Does the Board agree with the Exception—Temporary Conditions and Disclosures in the proposed Standard?**
10. **Does the Board agree with the Agency Mission-Related Interventions in the proposed standard?**
11. **Does the Board have any comments or suggestions on the language for Exception--Temporary Conditions and Agency Mission-Related Intervention in an Entity? See paragraphs 56 through 67 in the *Revised Principles and Related Criteria for Proposed Standards*.**

The task force suggested a Flowchart *Determining the Boundaries of the Federal Reporting Entity and Display* would be a useful Appendix to the Standard. Staff notes that GASB utilized a similar type format to depict their standard and it appears to have been helpful.

12. **Does the Board agree the Flowchart should be included as an Appendix to the Standard?**
13. **Does the Board have any comments or suggestions on the Flowchart at Tab 2?**

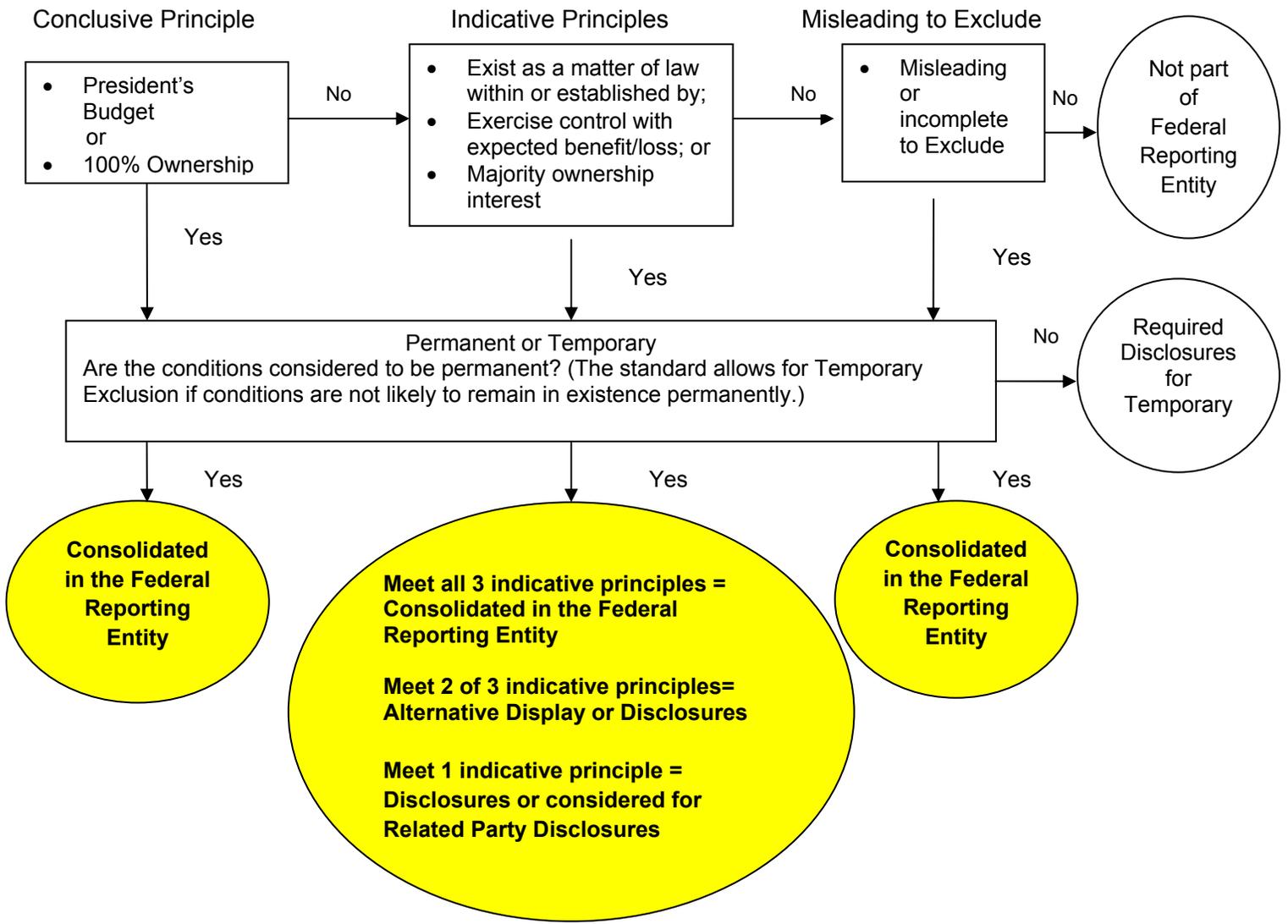
Staff began drafting the Consolidation Criteria and Disclosure Requirements but notes the final alternative display for entities meeting the indicative principles would be discussed at a future Board meeting. Staff thought it would be best to first get agreement on the revised approach and principles. However, staff presented a chart suggested by the task force for the Board's consideration. As a means of keeping in line with a principles-based approach to this Standard, the task force thought it would be appropriate if an approach similar to the Indicative Principles chart was used in determining the presentation and disclosure.

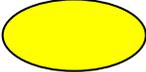
Specifically, the task force notes that entities meeting one of the indicative principles alone would not lead to consolidation in the federal reporting entity. When assessing the entities against the criteria, there may be entities that meet all three of the indicative principles while others may only meet one or two. From this, there are many variations of how an entity may fall within the boundaries of the federal reporting entity, which ultimately would relate to how the entity is presented and disclosed. Entities meeting all three of the indicative principles would be consolidated in the federal reporting entity (unless it meets the temporary exclusion.) Entities meeting one or two of the indicative principles would require alternative presentation or disclosures. One suggestion is for the Related Parties to be brought in to the proposed Standard to represent entities

meeting only one of the indicative principles. The Related Party discussion needs to be explored further but staff is presenting this as an option.

14. Does the Board believe this is a viable approach to addressing presentation and disclosures of the entities meeting the indicative principles? See Indicative Principles Chart on page 15 *Revised Principles and Related Criteria for Proposed Standards*.

If you have any questions or comments prior to the meeting or would like to provide feedback prior to the meeting, please contact me by telephone at 202-512-5976 or by e-mail at loughanm@fasab.gov.



Part of the Federal Reporting Entity 

Definitions

1. Definitions in paragraphs 2 through 4 are presented first in the proposed accounting standards because of their importance in understanding the Statement. Other terms shown in **boldface type** the first time they appear in this document are presented in the Glossary at Appendix C. Users of this document may want to examine all definitions before reviewing the proposed accounting standards and Basis for Conclusions.

2. **Federal Reporting Entity** A federal reporting entity is a federal entity² that issues GPFFR. It issues reports because either there is a statutory or administrative requirement to prepare them or it chooses to prepare them. A federal entity may choose to issue GPFFR to communicate financial and related information because

- 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; or
- c. It would be helpful for managing government operations and there is a management responsibility for controlling and deploying resources.

The term “federal reporting entities” is used throughout this Statement to refer broadly to all federal reporting entities which would include the U.S. Government Reporting Entity and Component Reporting Entities.

3. **U. S. Government Reporting Entity** The U. S. Government reporting entity is the largest federal reporting entity in the federal government and encompasses all entities existing within the federal government, which are the component reporting entities within the executive, legislative, and judicial branches as well as other entities assessed to be included based on the principles and criteria outlined in this statement.

4. **Component Reporting Entity** Component reporting entity is used broadly to refer to a federal reporting entity within a larger federal reporting entity that issues GPFFR. Examples of component reporting entities include entities that are part of the federal government, such as executive departments, independent agencies, and government corporations. Component reporting entities would also include sub-components (entities that are part of a larger component reporting entity³) that prepare GPFFR. 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 are prepared.

² The term “entity” is a general term used to refer to any legal, administrative or organizational structure or unit. See paragraphs 29-38 of SFFAC 2.

³ 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.

Proposed Standards

Principles Defining the Boundaries of Federal Reporting Entities

5. Clearly defining the boundaries of federal reporting entities⁴ ensures that the financial statements contain all the information essential for fair presentation of the financial position and results of operations. Defining the boundaries of federal reporting entities ensures consistency and completeness in what entities or involvements the reporting entities encompass.
6. Determining whether an entity is within the boundary of a federal reporting entity involves assessing organizations against the principles in this Standard. An entity must first be assessed against the conclusive principle to determine if it is within the boundaries of the federal reporting entity. Entities not meeting the conclusive principle are assessed against the indicative principles to determine if they are within the boundaries of the federal reporting entity. Lastly, entities not meeting the indicative principles should be assessed against the misleading to exclude principle. See the Flowchart at Appendix X.
7. **Temporary** existence of conditions that meet the principles and related criteria are situations where such conditions are not likely to remain in existence permanently. These entities would be excluded from the boundaries of the federal reporting entity unless they meet the misleading to exclude principle but require certain disclosures regarding the temporary nature and relationship as discussed in paragraphs 56 through 64.
8. After defining the entities within the boundaries of the federal reporting entity, additional analysis is required to determine which entities should be consolidated with the federal reporting entity and which require alternative display presentations or disclosures (**TBD but options include discrete presentation, detailed disclosures or RSI**) as discussed under Consolidation Criteria and Disclosure Requirements.

Conclusive Principle

9. Federal reporting entities include all entities that the federal government is directly financially accountable for. This includes entities in the program and financing schedules of the *Budget of the United States Government* (the President's budget) as well as those entities the federal government has an ownership interest of 100%. See par. 14 through 25 for discussion of this principle and related criteria for assessing. An entity meeting this

⁴ Federal reporting entities as used throughout this standard refers broadly to all federal reporting entities which would include the U.S. Government Reporting Entity and Component Reporting Entities.

conclusive principle is within the boundary of the federal reporting entity and no further assessment against the indicative principles is required.

Indicative Principles

10. Other entities not meeting the conclusive principle above may still fall within the boundaries of the reporting entity; however, additional assessment is required to ascertain if it is in fact within the boundaries of the federal reporting entity and what the appropriate financial presentation and display would be.
11. Federal reporting entities may also include entities:
 - a. Existing as a matter of law within or established by the federal government to fulfill a public purpose or federally related mission (See par. 27 through 33 for discussion of this principle and related criteria for assessing.)
 - b. Over which the federal government has the ability to exercise control with expected benefits or risk of loss (See par. 34 through 46 for discussion of this principle and related criteria for assessing.)
 - c. In which the federal government has a majority ownership interest (See par. 47 through 51 for discussion of this principle and related criteria for assessing.)

Misleading to Exclude Principle

12. Federal reporting entities should also include entities not meeting the conclusive or indicative principles if the nature and significance of their relationships with the federal government are such that the exclusion would cause the federal reporting entity financial statements to be misleading or incomplete. See par. 52 through 55 for discussion.

Criteria for Assessing the Boundaries of the Federal Reporting Entity

13. Each principle identified above requires criteria or indicators and guidance to assist in application. This Statement provides criteria or indicators that may assist in assessing whether an entity meets the principles and is within the boundaries of the federal reporting entity. Further, certain determinations will require the use of professional judgment.

Conclusive Principle and Criteria--Directly Financially Accountable

14. The federal government is directly financially accountable for entities included in the program and financing schedules of the *Budget of the United States Government* (the President's budget) as well those entities the

federal government has an ownership interest of 100%. These entities are within the boundaries of the U.S. Government Reporting Entity. Each component reporting entity should include all entities appearing in the component entity's portion of the President's budget.

15. If an entity meets this principle, no further assessment against the indicative principles is required; it is considered within the boundaries of the federal reporting entity (U.S. Government Reporting Entity and the component reporting entity with which it appears in the budget), unless it meets the conditions for Temporary Exclusion discussed in par. 56 or in the extreme circumstance inclusion of the entity would not result in fair presentation.⁵
16. SFFAC 1, *Objectives of Federal Financial Reporting*, includes the Budgetary Integrity Objective that states "Federal financial reporting should assist in fulfilling the government's duty to be publicly accountable for monies raised..."
17. As reflected in the *Report of the President's Commission on Budget Concepts*⁶, the budget should be "comprehensive of the full range of Federal activities" and "borderline agencies and transactions should be included in the budget unless there are exceptionally persuasive reasons for exclusion."
18. Federal reporting entities and officials responsible for executing the budget are accountable for their stewardship of public funds as well as to manage fiscal policy. This would include all entities that are included in the program and financing schedules of the President's budget.
19. Specifically, an entity that is included in the *Budget of the United States Government Analytical Perspectives* volume, supplemental materials currently entitled *Federal Programs by Agency and Account* should be considered part of the federal reporting entity (U.S. Government Reporting Entity)⁷, as well as part of the component reporting entity in which it appears, if applicable.
20. However, an appropriation to a federal reporting entity that finances a subsidy to a separate entity would not alone necessitate inclusion of the

⁵ For example, the Office of Management and Budget (OMB) has granted the U.S. Department of Labor (DOL) a waiver from consolidating the Pension Benefit Guaranty Corporation (PBGC) because **NEED TO DISCUSS WITH OMB TO ENSURE STANDARD COVERS PRINCIPALLY BASED REASON FOR EXCLUDING or alternatively discuss if this waiver should continue?**

⁶ The purpose of this 1967 report was to make the Budget a useful instrument of public policy and financial planning. The Commission established principles that would be of continuing value. Noteworthy recommendations included the following: a unified budget is used, the budget should be thought of as part of a broad financial plan, and the budget should include all programs of the Federal Government and its agencies. Chapter 3 of the report, *Coverage of the Budget*, discusses the recommendation for a comprehensive budget with very few exclusions.

⁷ Even in cases where Congress defines an entity as "not an agency or instrumentality" of the federal government, an entity included in the *Federal Programs by Agency and Account* Schedule is part of the federal reporting entity for financial reporting purposes.

subsidized entity because the subsidized entity may not be directly responsible for meeting budgetary reporting requirements.

21. Certain entities may be partially on budget and receive funding from other sources, such as fees, premiums, or donations that are not included in the budget.⁸ However, it is the authorities provided by Congress that allow these financing activities to be undertaken and thus accountability is for the entity in totality. In these cases, the whole federal entity is considered within the boundaries of the federal reporting entity based on this conclusive principle (Directly Financially Accountable).
22. An ownership interest of 100% of an entity also meets the directly financially accountable conclusive principle. An **ownership interest** is a claim on the net residual assets of an entity, such as a legal claim on the net residual assets or holding shares or other formal equity structure. A formal equity structure includes share capital or an equivalent form of unitized capital, or other equity structures in which the interest can be measured reliably.
23. 100% ownership should be determined based on the definition of ownership interest while noting the federal government may often use similar terms in defining corporate entities.⁹
24. Ownership interests less than 100% should be reviewed against the indicative principle related to a majority ownership.¹⁰
25. Entities not meeting this criterion would be assessed against the indicative principles and related criteria detailed below to assess if they are within the boundaries of the federal reporting entity.

Indicative Principles and Criteria

26. Entities not meeting the conclusive principle above may still fall within the boundaries of the reporting entity; however, additional assessment against the indicative principles is required to ascertain if they are in fact within the boundaries of the federal reporting entity. Federal reporting entities may also include entities:

⁸ For example, the Smithsonian Institution receives additional funding from non-federal sources (trust fund receipts) that are not included in the budget as trust funds are not subjected to the budgetary constraints inherent in being included in the budget. Clearly, the Smithsonian Institution is still accountable for their handling of general revenue appropriations, offsetting collections (e.g. donations) that are appropriated for their uses as well as the non-budgetary trust funds.

⁹ For example, Tennessee Valley Authority (TVA) is owned by the federal government, as evidenced by the Tennessee Valley Authority Act of 1933, as amended (P.L. 73-17, 16 U.S.C. § 831). The Act declared that TVA shall be a “body corporate.” TVA is listed as a “wholly owned government corporation” in 31 U.S.C. § 9101 and is subject to the provisions of the Government Corporation Control Act. 5 U.S.C. § 103 defines a “Government corporation” as “a corporation owned or controlled by the Government of the United States.”

¹⁰ See discussion of Majority Ownership paragraphs 47 through 50.

- a. Existing as a matter of law within or established by the federal government to fulfill a public purpose or federally related mission;
- b. Over which the federal government has the ability to exercise control with expected benefits or risk of loss; or
- c. In which the federal government has a majority ownership interest.

Existing as a Matter of Law within or Established by the Federal Government

27. Federal reporting entities may also include entities existing as a matter of law within or established by the federal government to fulfill a public purpose or federally-related mission.
28. The U.S. Government Reporting Entity encompasses all the entities existing as a matter of law within the federal government, which comprises three branches: the legislative (Congress); the executive (the President); and the judicial (Supreme Court and inferior courts established by law).¹¹ The fundamental organization of the U.S. government is established by the U.S. Constitution.¹²
29. Statutes or regulations¹³ that establish an entity within a branch of the federal government often clearly state so.¹⁴ However, in other cases, the statutes or regulations establishing the entity may not be as clear, requiring additional analysis.
30. Statutes or regulations may state that an entity is established within the federal government without locating it in a particular branch. In such cases, the nature of the federal government's powers exercised by the entity generally determines the branch of government to which it belongs, so long as the relevant branch retains the authority to direct and remove the head of

¹¹ U.S. Constitution, Art. I, § 1; Art. II, § 1; and Art. III, §, respectively.

¹² "[The] Constitution sought to divide the delegated powers of the new Federal Government into three defined categories, Legislative, Executive, and Judicial." [INS v. Chadha, 462 U.S. 919, 951 \(1983\)](#). "The declared purpose of separating and dividing the powers of government, of course, was to '[diffuse] power the better to secure liberty.'" *Bowsher v. Synar*, 478 U.S. 714, 721 (1986), quoting *Youngstown Sheet & Tube Co. v. Sawyer*, [343 U.S. 579, 635 \(1952\)](#) (Jackson, J., concurring).

¹³ Certain government officials may have the authority under law to establish an entity by regulation. Under this standard, the term "by regulation" includes the act of incorporation or other official filing or notice that an entity is established.

¹⁴ For example, for the executive branch, the U.S. Department of Defense is created by statute as "an executive department of the United States," 10 U.S.C. § 111, the United States Postal Service is "an independent establishment of the executive branch of the Government of the United States," 39 U.S.C. § 201, and the Pension Benefit Guaranty Corporation is "established within the Department of Labor [as] a body corporate," 29 U.S.C. § 1302(a). (The Department of Labor is "an executive department in the Government." 29 U.S.C. § 551.) For the legislative branch, an example is the Congressional Budget Office, which "is established [as] an office of the Congress." 2 U.S.C. § 601(a)(1). For the judicial branch, an example is the Administrative Office of the United States Courts, which "shall be maintained at the seat of government," and be supervised by a director, 28 U.S.C. § 601, who is "the administrative officer of the courts." 28 U.S.C. § 604. "The courts" are the U.S. federal courts of appeals, district courts, and other courts established within the judicial branch as inferior to the U.S. Supreme Court. 28 U.S.C. § 610.

the entity.¹⁵ For example, the U.S. Supreme Court has held that because the Comptroller General of the United States is removable solely upon the initiative of Congress, he and the Government Accountability Office, which is “an instrumentality of the United States Government independent of the executive departments,” are in the legislative branch.¹⁶ Because the determination of whether an entity carries out a legislative, executive, or judicial power is one of a legal nature, not one of accounting, the most convenient method of determining the branch to which an entity belongs is to identify the branch of the federal government that possesses the power to direct and remove the head of the entity.

31. Statutes or regulations may omit any express statement about the location of the entity as either within or outside the federal government.¹⁷ For example, in 1846, Congress created “an establishment by the name of the Smithsonian Institution,”¹⁸ and in 1923, Congress provided that “a commission is hereby created and established, to be known as the American Battle Monuments Commission.”¹⁹
32. Such entities may take many forms, including administrations, agencies, banks, boards, commissions, corporations, foundations, and institutions and may be given any combination of powers and privileges of the federal government as incidental to exercising the federal government’s constitutional powers.²⁰
33. These entities that were established by the federal government often exercise a power of the federal government (whether or not other entities could exercise such powers) and should be considered within the boundaries of the federal government.

¹⁵ *Mistretta v. United States*, 488 U.S. 361 (1989); *Buckley v. Valeo*, 424 U.S. 1 (1976).

¹⁶ *Bowsher v. Synar*, 478 U.S. 714 (1986).

¹⁷ Statutes or regulations may establish an entity and clearly indicate its status as outside of the federal government by stating that the entity is “private” or that it is “not an agency or instrumentality of the United States Government.” Congress defines what constitutes an agency or instrumentality of the federal government for purposes of a particular statute or set of statutes that assigns duties, liabilities, and administrative requirements and grants privileges of the federal government to individual entities or types of entities. Even in cases where Congress defines an entity as “not an agency or instrumentality” of the federal government, the entity may be found to be part of the federal government for certain purposes. *Lebron v. Nat’l R.R. Passenger Corp.* 513 U.S. 374 (1995) (Amtrak is part of the federal government for purposes of the 1st Amendment to the U.S. Constitution).

¹⁸ Act of Aug. 10, 1846, § 1, 9 Stat. 102, *codified, as amended at* 20 U.S.C. § 41.

¹⁹ Act of Mar. 4, 1923, 42 Stat. 1509, *codified, as amended, at* 36 U.S.C. ch. 21.

²⁰ See *McCulloch v. Maryland*, 17 U.S. (4 Wheat) 316 (1819); *Reconstruction Finance Corp. v. J.G. Menihan Corp.*, 312 U.S. 81 (1941); see also *Lebron v. Nat’l R.R. Passenger Corp.* 513 U.S. 374 (1995) (discussion of the evolution of government corporations and their legal status) and Kevin R. Kosar, *The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics*, RL30533, Congressional Research Service (Washington, D.C.: Feb. 17, 2009).

Control

34. The federal reporting entity may also include entities over which the federal government exercises control with expected benefits or risk of loss.
35. For purposes of defining the boundaries of the federal reporting entity for financial reporting, control is defined as follows: **Control** is the power to govern the financial and/or operating policies of another entity with expected benefits (or the risk of loss)²¹ to the federal reporting entity.
36. Control for these purposes refers to the ability to control and should be assessed at the reporting date regardless of the federal 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 federal reporting entity and the entity as it may not be completely reflected by their legal form.
37. Control does not necessarily mean the federal reporting entity has responsibility for the management of the day-to-day operations of an entity. It is the federal reporting entity's authority to determine the policies governing those activities that indicates control.
38. Determining whether control exists requires the application of professional judgment. The federal government achieves its objectives through a wide range of entities which individually will fall somewhere along a continuum. At one end of the continuum, it will be clear that an entity does not have the power to act independently and is controlled by the federal reporting entity. At the other end, the entity will have the power to act independently and, while the federal government may have a level of influence on the entity, 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 entity in order to determine whether control exists.

Indicators of Control

39. There are certain indicators of control that should be considered in determining whether the federal government controls an entity. 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.
40. The assessment of whether control exists requires the application of professional judgment and should include consideration of all the facts and circumstances of a particular relationship.

²¹ The expected benefit or risk of loss may be financial or non-financial. For example, a non-financial benefit would be the federal government benefits from a service being provided on its behalf.

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41. There are certain indicators²² that provide more persuasive evidence of control. Control generally exists when the federal government:
- a. Has the authority to unilaterally appoint or remove a majority of the governing board members of another entity;
 - b. Has the authority to govern or direct the governing body on the financial and operating policies of the entity or holds a voting majority that would permit it to govern the financial and operating policies of the entity;
 - c. Has ongoing access to another entity's assets or has the ability to direct the ongoing use of those assets, or has ongoing responsibility for losses; or
 - d. Has the authority to unilaterally dissolve the entity thereby having access to the assets and responsibility for the obligations.
42. There are other indicators that, when considered in the aggregate, would provide evidence control exists. Control may exist when the federal government has the power to:
- a. Provide significant input into the appointment of members of the governing body of the entity or being involved in the appointment or removal of a significant number of members;
 - b. Establish or amend the entity's fundamental purpose and mission;
 - c. Require the entity to carry out federal missions and objectives which results in the entity being an integral part of the federal government's exercise of its sovereign power to carry out federal functions such as powers to collect compulsory payments and conduct negotiations involving the interest of the United States with other nations;
 - d. Appoint or remove key executives or personnel;
 - e. Approve the budgets or business plans for the entity;
 - f. Veto, overrule, or modify governing board decisions or otherwise significantly influence normal operations;
 - g. Establish, rescind, or amend management policies;
 - h. Establish limits or restrictions on borrowing and investments of the entity; or
 - i. Restrict the capacity to generate revenue of the entity, especially the sources of revenue.

Situations Where Control Does Not Exist

43. Because of the uniqueness of the federal government, it is important to distinguish what does not constitute control. Specifically, control would not be inferred from:

²² The indicators noted in par. 41 and 42 provide support for both the power and/or benefit part of the control definition. When assessing control for financial reporting purposes, a federal reporting entity should meet both the power and benefit element for determining whether control exists.

- a. The authority to exercise regulatory powers over an entity;
 - b. Constitutional responsibility for a particular matter related to the entity's mission or operations; or
 - c. Purchasing power of or economic dependency on the federal government in relation to the entity.
44. The federal government has the power to regulate many entities by use of its sovereign and legislative powers. For example, the federal government has the power to regulate the behavior of entities by imposing conditions or sanctions on their operations. However, the governing bodies of the regulated entities 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 entities extends only to the regulatory aspects of the operations.
45. 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 entities performing such activities. The nature of the relationship between the federal government and the entity performing the activity is the determining factor.
46. Purchasing power does not constitute control for purposes of defining the boundaries of the reporting entity. Certain entities 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 entity which is dependent on its funding or business through purchase power, the federal government does not govern the entity's financial and operating policies.

Majority Ownership Interest

47. The federal reporting entity may also include entities in which the federal government has a majority ownership interest.
48. The federal government may acquire an ownership interest in an entity. An **ownership interest** is a claim on the net residual assets of an entity, such as a legal claim on the net residual assets or holding shares or other formal equity structure. A formal equity structure includes share capital or an equivalent form of unitized capital, or other equity structures in which the interest can be measured reliably.
49. The holding of an ownership interest often entitles the holder to an equivalent percentage interest in voting rights, but not always. In the federal government there may be instances of:

- a. Ownership interest with voting (controlling) interest;
 - b. Ownership interest without voting (controlling) interest; and
 - c. Control without ownership interest, which is addressed in the Control section.
50. An ownership interest with over 50% of the voting shares or 50% of the net residual assets²³ of an entity is considered a majority and within the boundaries of the federal reporting entity.
 51. As noted above, although the federal government may not hold a majority ownership interest, it is possible to control an entity and therefore the control principle detailed above would be considered.

Misleading to Exclude Principle

52. The boundaries of federal reporting entities should include entities for which the nature and significance of their relationships with the federal government are such that the exclusion would cause the federal reporting to be misleading or incomplete.
53. There are instances where entities may not meet conclusive or indicative principles, yet the nature and significance of the relationship is such that excluding them from the federal reporting entity boundaries would make the GPFFR misleading or incomplete.
54. For example, there may be instances when an entity is not listed in the *Federal Programs by Agency and Account* and it may be difficult to provide sufficient evidence it meets the indicative principles yet the GPFFR would be misleading or incomplete if the entity were excluded.²⁴
55. Examples may include where in those rare instances an entity does not meet the conclusive principle or indicative principles for being within the boundary of the federal reporting entity, yet the material entity is an integral part of the federal government's exercise of its sovereign power to carry out federal functions and missions (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).

²³ For example, the federal government may hold more equity in preferred stock than all other stockholders but the preferred stock may be non-voting.

²⁴ Although situations such as this would be considered unique or rare, the Standard should make provisions for those situations that could potentially arise.

Exception—Temporary Conditions

56. Temporary existence of conditions that meet the principles and criteria are situations where such conditions are not likely to remain in existence permanently. This includes situations where the explicit intent of the federal government's activities is not to make the conditions permanent.
57. In these types of situations, if the temporary conditions resolve / end within one fiscal year, then there are no questions related to whether the entity falls within the boundary of the federal reporting entity as the conditions would not exist as of year-end.
58. Temporary situations that exist at fiscal year-end must be assessed to determine whether they are in fact temporary conditions and not expected to be permanent. If deemed temporary or not permanent, the entity should be excluded from the boundaries of the federal reporting entity. However, certain disclosures would be appropriate as described below.
59. Example of situations where existence may be temporary are:
 - a. Temporary control-- the federal government has no plan to continue control permanently and instead plans to relinquish or cede control; and
 - b. Temporary ownership--the federal government acquires ownership of an entity but it is held exclusively with the view of being disposed.
60. Temporary situations may last several reporting periods. In such situations, the federal reporting entity should confirm such conditions are not likely to remain in existence permanently as of each reporting period.
61. For example, the federal government's intervention in exceptional circumstances--such as an economic crisis situation or military occupation—may last for more than several years, but it is not intended to be permanent. Circumstances may arise that necessitate the federal government intervention to be longer than would normally be anticipated, but considering the conditions are not expected to be permanent, it meets the temporary exclusion.
62. Typically the federal government intervention actions in these instances are not routine activities. For example, strategic planning documents are unlikely to include objectives to routinely initiate such interventions and the actions are not necessarily taken to further established government policies.
63. Although these types of interventions may last several years, there is typically an end date in the future, such as a date certain in legislation when the activity will end or when authority expires that supports such interventions. In addition, the federal government is likely to have a plan that demonstrates the intervention is not to be considered permanent. The plan may detail milestone dates for certain actions, the expectations of the

interventions and results, necessary factors to end the intervention, as well as a commitment to the plan.

64. Entities where the conditions are deemed temporary are not considered within the boundaries of the federal reporting entity. Disclosures for temporary situations should include the following for each entity:
- a. Name and description of the entity;
 - b. Nature of the federal government's relationship with the entity and if applicable, the percentage of ownership interest and voting;
 - c. Primary reasons for the temporary situation or intervention and intended timeframes;
 - d. Brief description of the formal plan that describes the federal government's intervention is not expected to be permanent and plans for ending the intervention, including any information regarding the length of such arrangement or plans to change terms of such arrangement; and
 - e. Other information that would provide an understanding of the possibility of potential financial reporting impact, including financial-related exposures to potential gain and risk of loss to the federal reporting entity resulting from the temporary situation.

Agency Mission-Related Intervention in an Entity

65. There are certain federal entities whose mission may include taking control or ownership of an entity with no goal to maintain control or ownership. For example, certain federally-created entities may act as a receiver to liquidate failing financial institutions or as a conservator to guide such institutions back to safe and sound conditions.²⁵
66. The entities related to these types of mission-related activities would be excluded from the boundaries of the federal reporting entity. However, this exemption is due to the activities being part of the normal activities and mission of the federal reporting entity (not because of the temporary exclusion) and separate disclosures would be appropriate that are consistent with existing practices.
67. Disclosures should include the following:
- a. Nature and description of the federal reporting entity's relationship with the entities.

²⁵ For example, the Federal Deposit Insurance Corporation (FDIC) is an independent agency created by the Congress with the mission "to maintain stability and public confidence in the nation's financial system by: insuring deposits; examining and supervising financial institutions for safety and soundness and consumer protection; and, **managing receiverships.**"

- b. Other information that would provide an understanding of the possibility of potential financial reporting impact, including financial-related exposures to potential gain and risk of loss to the federal reporting entity resulting from the relationship.
- c. Other information about the entities may be voluntarily disclosed if deemed necessary or included as RSI or Other Accompanying Information (OAI).

Consolidation Criteria and Disclosure Requirements

- 68. Consolidation aggregates the individual financial statements of entities comprising a reporting entity. Consolidation is a method of accounting that combines the accounts of those entities line by line on a uniform basis of accounting and eliminates balances and transactions among the entities. For selected financial statements such as the statement of budgetary resources, a combined financial statement which does not eliminate balances and transactions among the entities is acceptable.
- 69. The principles and related criteria described above provide guidance on determining the boundaries of the federal reporting entity. However, not all of those entities should be consolidated.
- 70. An entity meeting the conclusive principle and related criteria (federal government is directly financially accountable through 100% ownership or the entity is encompassed in its budgetary reporting requirements) is consolidated unless it meets the temporary exclusion discussed in the standard.
- 71. The indicative principles and related criteria for determining other entities to be included within the boundaries of the federal reporting entity, include entities:
 - a. Existing as a matter of law within or established by the federal government to fulfill a public purpose or federally related mission;
 - b. Over which the federal government has the ability to exercise control with expected benefits or risk of loss; or
 - c. In which the federal government has a majority ownership interest.
- 72. However, meeting one of the indicative principles alone would not necessarily lead to consolidation in the federal reporting entity. When assessing the entities against the criteria, there may be entities that meet all three of the indicative principles while others may only meet one or two. From this, there are many variations of how an entity may fall within the boundaries of the federal reporting entity, which ultimately would relate to how the entity is presented and disclosed.
- 73. Entities meeting all three of the indicative principles would be consolidated in the federal reporting entity (unless it meets the temporary exclusion). Entities that do not meet any of the criteria would not be considered within

the boundaries of the federal reporting entity and they would not be subject to alternative presentation or disclosure requirements.

- 74. Entities meeting two of the principles would require Alternative Presentations or Disclosures. **NOTE: This will be presented at the next meeting once the principles and criteria are agreed upon, but options include the possibility of Discrete Presentation, Detailed Note Disclosures, or RSI Information.**
- 75. Entities meeting only one of the principles would be considered a Related Party and subject to the Related Party Disclosures below.
- 76. The chart listed below summarizes where entities may fall along this continuum and the required presentation and disclosures.

Indicative Principles

Entity (Potential Example ²⁶)	Within Fed Gov't or Established	Control	Ownership Interest	Alternative Presentation or Disclosures
Entity A	X	X	X	Consolidation
Entity B	X	X		Options for Disclosures
Entity C	X		X	Options for Disclosures
Entity D	X			Related Party? Disclosures
Entity E		X	X	Options for Disclosures
Entity F		X		Related Party? Disclosures
Entity G			X	Related Party? Disclosures
Entity H				Not within boundaries

(NOTE-Alternative Presentations or Disclosures will be presented at the next meeting but include the possibility of Discrete Presentation, Detailed Note Disclosures, or as RSI Information)

- 77. Lastly, the federal reporting entity should consolidate entities if the nature and significance of their relationships with the federal government are such

²⁶ Once the Board agrees upon the revised principles and criteria, staff and the task force will perform test cases and provide an appendix for examples of the various scenarios. The examples in the appendix will be based on a preliminary assessment and not be taken as authoritative.

that the exclusion would cause the federal reporting entity financial statements to be misleading or incomplete

Related Parties

78. Related parties are entities with whom the federal government has a relationship, but is not [within the boundaries of the federal reporting entity] or [consolidated in the federal reporting entity.]

79. To Be Completed

Effect on Existing Concepts

80. This Statement affects existing Concepts is amended as follows:
COMPARE FINAL TO SFFAC 2 to determine any necessary amendments

Effective Date

81. These standards are effective for periods beginning after September 30, 2011. Earlier implementation is encouraged.

