



August 14, 2009

Memorandum

To: Members of the Board
From: Eileen W. Parlow, Assistant Director
Through: Wendy M. Payne, Executive Director
Subj: GASB Briefing: Fiscal Sustainability Reporting - Tab K¹

MEETING OBJECTIVES

To brief GASB Members on the FASAB's proposed Statement of Federal Financial Accounting Standards (SFFAS) 36, *Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government*.

FASAB staff will provide a brief overview of major issues encountered and resolved, followed by an open discussion between the FASAB and the GASB in order to assist GASB in moving forward with a proposed GASB project on a similar issue.

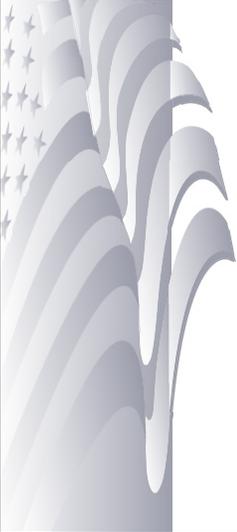
BRIEFING MATERIAL

Attached are:

1. Power Point Presentation: major issues
2. GASB Project Prospectus: Economic Condition Reporting
3. Final proposed SFFAS 36 submitted for 90-day review on June 25, 2009

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.

**The Federal Accounting
Standards Advisory Board**



**Comprehensive Long-Term Fiscal
Projections for the U.S.
Government**

Eileen W. Parlow
Assistant Director

Disclaimer:

Views expressed are the views of the speaker. Official positions of the FASAB are determined only after extensive due process and deliberations.

Background: Federal Financial Statements

- U.S. Government's fiscal year ends September 30
- Individual agencies issue audited financial statements
- Treasury issues an audited financial statement for the federal government as a whole: "Financial Report of the U.S. Government"

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FASAB's Challenge

To communicate to "financial statement readers" (in particular, the general public and public intermediaries) vitally important information about the federal government's fiscal sustainability in a way that is

- Understandable
- Meaningful
- Technically robust

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Successful Communication

- Is Easy to Remember
- Changes behavior

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“Sticky” ideas are easy to remember

Made to Stick by Chip Heath and Dan Heath

- Simplicity
- Unexpectedness- surprise element
- Concreteness
- Credibility
- Emotions
- tells a Story

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Challenges

- **Technical challenges**
 - Data is very complex
 - Data involves uncertainty
 - Projections require assumptions
- **Communication challenges**
 - How to simplify complex information
 - How to hold the reader's attention

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Fiscal Sustainability Task Force

- **Technical experts**
 - Chief Actuaries for Social Security and Medicare
 - Representatives from several “think tanks”
 - Subject-matter experts from GAO,OMB, CBO and Treasury
- **Communications experts**
 - Academics in Communication and Public Policy
 - Executives of public advocacy groups
 - Two members of Congress

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Technical Challenges

- Assumptions
- Time Horizon for Projections
- Per Capita amounts

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Technical Challenges

- Type of data:
 - present-value dollars?
 - % GDP?
- How to address uncertainty
- How to set boundaries (what to include)

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What's the objective?

Objective:

Federal financial reporting should provide information that helps the readers to determine whether future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due. [SFFAC 1. par.139]

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Technical Challenges: Assumptions

- Demographic assumptions
- Economic assumptions
- Policy assumptions

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Technical Challenges: Policy Assumptions

- What is “current policy”?
- Current law = current policy?
- Challenging aspects of current law
 - Statutory limit on Treasury debt
 - Short term of most discretionary legislation
 - Limitations on social insurance programs (earmarked receipts plus trust funds)

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Technical Challenges: Time Horizon for Projections

- Infinite horizon- pros and cons
- Finite horizon- pros and cons

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Technical Challenges

Per Capita Amounts

- Pros and cons
- Board proposal

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Technical Challenges

Dollars versus Ratios

- Dollars- pros and cons
- Ratios- pros and cons

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Technical Challenges: Proposed new financial statement

	PV Dollars (in trillions)	% GDP
Receipts		
Medicare		
Social Security		
All Other Receipts		
Total Receipts		
Spending		
Medicare		
Medicaid		
Social Security		
Rest of Federal government		
Total Spending		
Spending in Excess of Receipts		

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Technical Challenges: Proposed new financial statement

Simplified bottom line:

- Spending in Excess of Receipts

Other alternatives:

- Fiscal imbalance
- Fiscal gap

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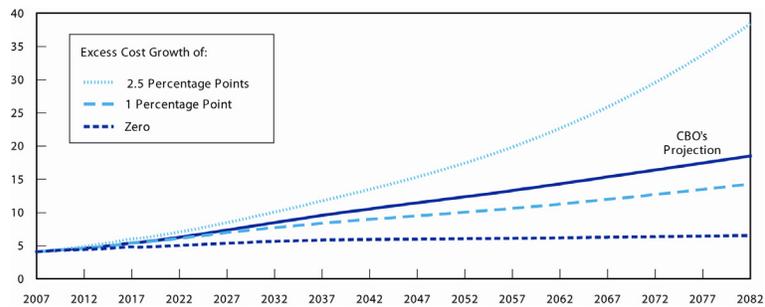
Technical Challenges: Uncertainty

How can we communicate uncertainty
without confusing readers?

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Technical Challenges: Uncertainty

Federal Spending for Medicare and Medicaid as a Percentage of Gross Domestic Product Under Different Assumptions About Excess Cost Growth

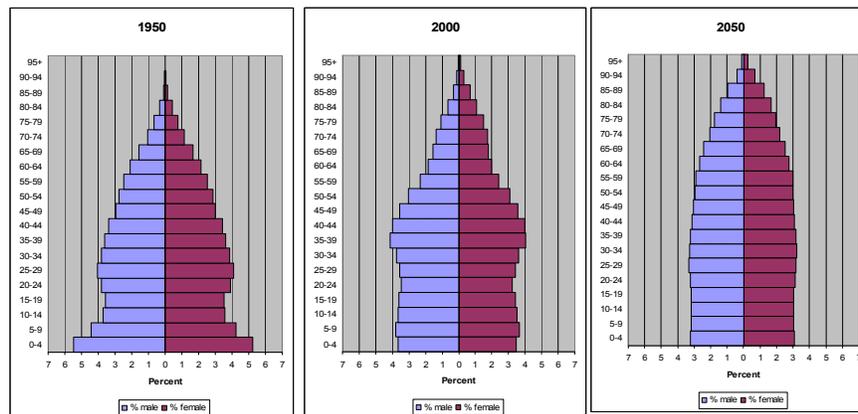


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Technical Challenges: What to include

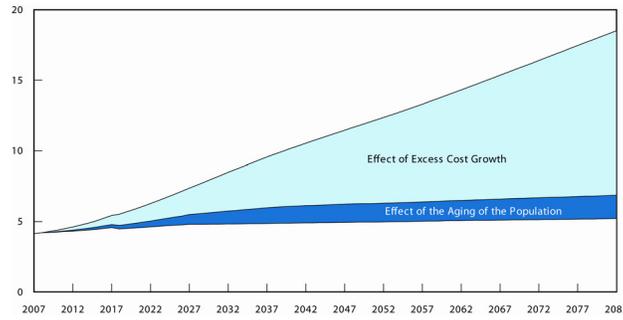
How about something to illustrate changing demographics?

Technical Challenges: What to include

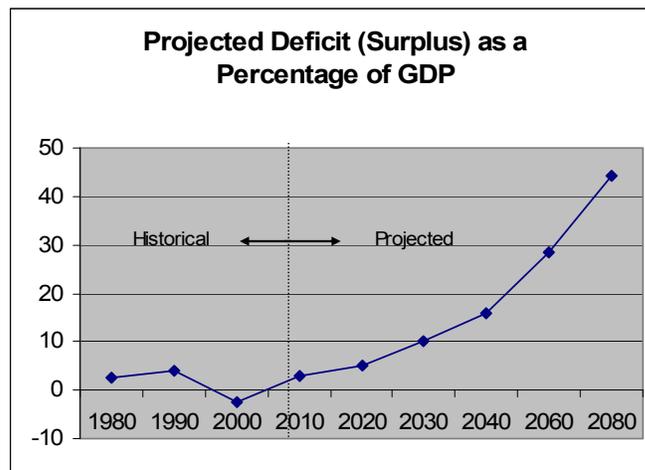


What are the primary cost drivers? Perhaps not what you expect!

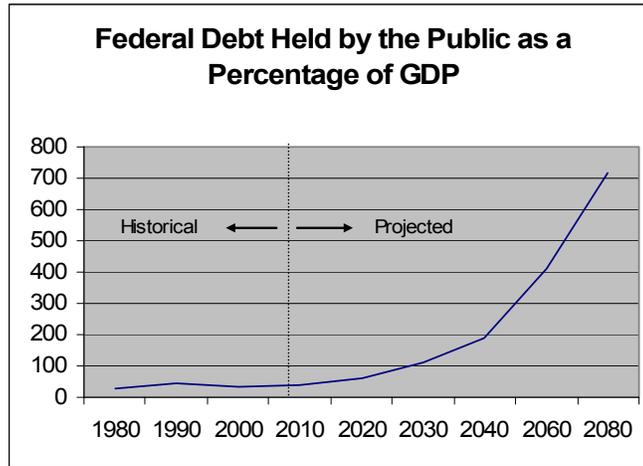
Sources of Growth in Projected Federal Spending on Medicare and Medicaid



Projected Federal Deficits



Federal Debt Held by the Public

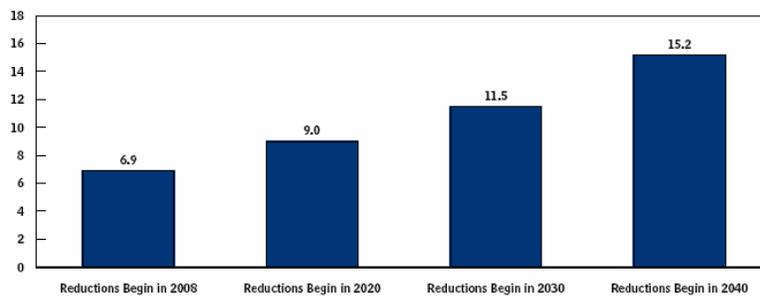


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Impact of Delaying Action

Reductions in Noninterest Spending Needed to Close the Fiscal Gap in Various Years Under CBO's Alternative Fiscal Scenario

(Percentage of gross domestic product)



Source: Congressional Budget Office.

Notes: The fiscal gap is a measure of federal shortfalls over a given period. It represents the extent to which the government would need to immediately and permanently either raise tax revenues or cut spending—or do both, to some degree—to make the government's debt the same size (in relation to the economy) at the end of that period as it was at the beginning.

The alternative fiscal scenario deviates from CBO's baseline projections during the next 10 years, incorporating changes in policy that are widely expected to occur and that policymakers have regularly made in the past.

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Technical Challenges: What to include

Foreign Holdings of U.S. Treasury Debt

Original staff proposal had two displays:

- List of top foreign government holders of Treasury debt, plus
- Chart showing the change

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Technical Challenges: What to include

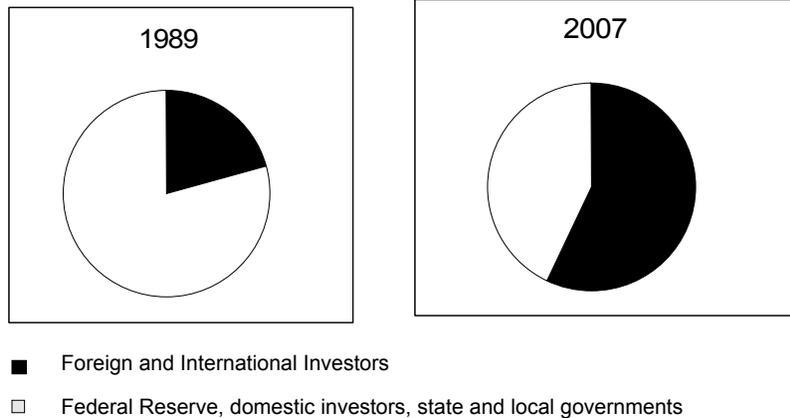
Foreign Holdings of U.S. Government Debt
by Major Investing Country
As of June 30, 2006
Billions of Dollars

Japan	719
China, mainland	619
Luxembourg	90
Middle East Oil-Exporters**	78
United Kingdom	75
Cayman Islands	57
Belgium	56
Switzerland	43
Netherlands	35
Canada	<u>22</u>
Total	1,794

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Technical Challenges: What to include

Foreign Ownership of U.S. Treasury Debt Has Increased



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Technical Challenges: What to include

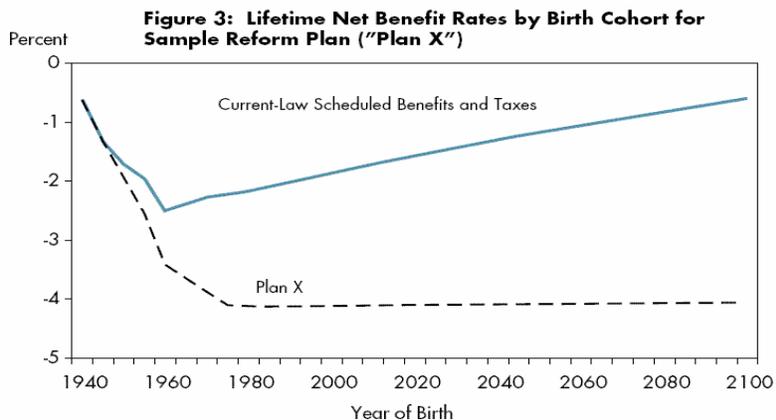
The proposed requirements do not include:

- Policy proposals
- “Inter-generational equity”

(See Treasury’s “**Issue Brief No. 3: Social Security Reform: Benchmarks for Assessing Fairness and Benefit Adequacy**”)

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Inter-generational Equity



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Outreach

FASAB outreach for this ED:

- FASAB mailing list
- Press contact list
- IPA contacts
- Over 300 think tanks
- Public advocacy /government watchdog groups
- Presentation at various professional events
- Public hearing held on February 25, 2009

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Public Comments Received

- 22 Comment Letters
- 7 speakers addressed the Board at the February 25th Public Hearing

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Public Comments on the Draft

- Innovative items- graphics and FAQs- were helpful for readers
- Most supported finite-horizon, not infinite-horizon data (the Board agreed)
- Most support reporting foreign holdings (the Board disagreed and did not include this requirement)

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SFFAS 36

- The Board voted to approve proposed SFFAS 36, “Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government”
- On June 25, 2009 the Board forwarded the proposed SFFAS to the Secretary of the Treasury, the Director of OMB, the Acting Comptroller General and the Director of the Congressional Budget Office for a required 90-day review period.
- Absent objections from the Acting Comptroller General (OMB has indicated approval) SFFAS 36 will be issued on September 28, 2009.



Memorandum

Issue 1 Paper 1

August 2009 Board Meeting

To: GASB and FASAB Members, David Bean and Wendy Payne
From: Lisa Parker, Andrew Brownfield, and Jay Fountain
c: GASB and FASAB Staff, Meeting observers
Date: August 21, 2009
Re: Project Prospectus: Economic Condition Reporting: Fiscal Sustainability

The following is a draft of a project prospectus related to the GASB's research on Economic Condition Reporting: Fiscal Sustainability, for your review and comment. The GASB will be discussing the project prospectus further at their September 15, 2009 teleconference meeting.

OBJECTIVES OF THE PROPOSED PROJECT

The objective of this project would be to consider whether guidance or guidelines should be considered for additional information as part of general purpose external financial reporting (GPEFR) to enhance a user's ability to assess a government's economic condition. . The consideration of additional information would include risks associated with a government's intergovernmental financial dependencies, which previously was a separate project in the technical plan but was deferred for consideration as part of this project.

I. DESCRIPTION OF THE PROJECT TOPIC

This project represents phase three of a multiphased research program. Phase one involved the background research, including a literature review. The second phase (which resulted in the issuance of GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section* in May 2004) focused on the existing reporting of economic condition information as presented in the statistical section.

The third and current phase of this project examines the usefulness of indicators of economic condition and its related components, including *fiscal sustainability* that might be a part of general purpose external financial reporting. The Board has not yet deliberated a working

definition of fiscal sustainability or the information users need to assess fiscal sustainability in the state and local government environment. This phase of the project will incorporate the recent research on fiscal sustainability, determine and clarify its relationship to economic condition, including fiscal capacity, and service capacity, and financial position.

The project also would:

- A. Develop a definition for fiscal sustainability
- B. Consider whether additional guidance or guidelines should be provided based on the recently completed research
- C. Determine the preferable methods of communicating any additional information, if applicable.

II. REASONS FOR CONSIDERING THE ADDITION OF THIS PROJECT TO THE CURRENT AGENDA

Relevant literature; the research of other standards setters; and the views of various types of users of governmental financial information; all highlight the fact that economic condition and similar concepts of financial health are not limited to where a governmental entity *currently* stands. GASB research also indicates that users are interested in understanding a governmental entity's *past* economic condition—and thus how the governmental entity arrived at its current status—with an eye toward assessing a governmental entity's *future* viability or fiscal sustainability. In other words, based on existing information, users seek to assess a governmental entity's *ongoing* ability to raise revenue, to deliver services, to issue debt, to meet obligations and commitments—the capacity to *sustain* or improve its financial status. A considerable amount of research has been conducted by the GASB staff and others to identify users' information needs with regard to the assessment of a government's economic condition.

A literature review conducted in the first phase of this project produced several major findings. First, it confirmed the notion that users employ a wide range of terms when describing the financial health of a government, including financial position, financial

condition, fiscal condition, and fiscal capacity. These terms are often used interchangeably, and individual terms have diverse meanings to different people. Regardless of the terminology used, however, the review of the literature suggests that there is substantial agreement on the key areas of concern that should be addressed when one is assessing the financial health of a government.

Despite variation in the way information from financial reports is used, there was substantial consensus that assessing the financial health of a government requires trend information regarding: (1) fund balances, equity, or net assets, (2) revenues and expense/expenditures, as well as surpluses and deficits, (3) changes in revenue bases, (4) spending pressures and needs, (5) outstanding debts, debt service, and postemployment benefits, and (6) liquidity. There was less widespread, though still notable, agreement on several other types of information, including: (1) short-term debt, (2) credit ratings, (3) number of employees, (4) condition of the physical plant, (5) output and outcome measures, and (6) management issues such as the quality of financial reporting, planning and budget processes, and accounting practices.

Panel discussions conducted during the second phase of the research project with users experienced with, and knowledgeable about, the assessment of a government's financial health provided additional insights regarding users' economic condition information needs. In general, the user panelists agreed that a comprehensive annual financial report (CAFR) containing the financial reporting model established in Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, provided a considerable amount of the information needed to assess economic condition. The panelists generally agreed that the CAFR contains most, if not all, of the information needed to assess financial position, not enough information about fiscal capacity, and little information about service capacity. The panelists considered information in the statistical section to be particularly useful for assessing fiscal capacity. However, these users identified other necessary information not currently found in the CAFR, such as more detailed revenue and expense trends, comparative and benchmarking information, financial ratios, explanations, and a variety of demographic and economic indicators as necessary for assessing fiscal and service capacity.

The enhancement of the statistical section by Statement No. 44, *Economic Condition Reporting: The Statistical Section*, appears to have improved the usefulness of the CAFR in providing information that GASB research has shown is valuable for assessing economic condition, particularly fiscal capacity. For instance, the inclusion of government-wide information has given the users more comprehensive trends in revenues, expenses, financial position, and outstanding debt. Furthermore, the addition of trend information presented in schedules such as principal revenue payers and debt limitations should make them more meaningful to users. The improved statistical section is expected to be an enhanced resource for the purposes it currently serves. However, with the important exception of providing trend data for information contained in the government-wide statements and narrative explanations, it does not address the additional information needs that user participants in the GASB research identified. This is primarily because the scope of the revisions to the statistical section was limited to existing reporting.

A. Why This Project Should Be Added to the Current Agenda

In light of growing national concern with fiscal sustainability and calls for greater transparency, a third phase of this project included research to consider how these concerns may relate to economic condition. Twenty-seven telephone interviews and four user roundtables with a total of twenty-nine users confirmed that the ability to make an assessment of a government's fiscal sustainability was important to them. This phase of the research also confirmed that some of the information necessary to make an assessment of fiscal sustainability is consistent with the information necessary to make an assessment of fiscal capacity and service capacity. Although the assessment of fiscal sustainability is different than the consideration of either fiscal or service capacity, users indicated that it is a part of economic condition. Through these discussions with users, several common themes arose in their attempts to define fiscal sustainability, as well as common components of information they would need to assess fiscal sustainability.

Based upon the working definitions of other standard setters, national governments, and other organizations, and the GASB research from the user roundtables and telephone interviews, the following common themes were identified by the participants in describing fiscal

sustainability:

- The ability to continue to provide public services and/or existing programs considering the economy a government is operating within, during economic cycles, and given the challenges a government faces.
- The ability to meet financial commitments both now and in the future.
- The ability to rely on a government's future revenue sources which influence long-term decision making.
- The ability to assess intergenerational equity.
- The ability and willingness to make decisions that will keep a government fiscally sound for years into the future and having measures in place to determine if they have been successful at doing so ("political will and ability").

Five common components of information users need to make an assessment of fiscal sustainability identified by the GASB staff during its previous research efforts and later validated by the current research participants include:

- Ability to generate sufficient future resources
- Ability to maintain or improve the delivery of public services
- Ability to meet financial obligations and commitments
- Achievement of intergenerational equity
- Effects of fiscal interdependencies between various governments

The following three additional common components of information users need to assess fiscal sustainability that were identified by current research participants include:

- Potential effects of the underlying economy
- Potential effects of changing demographics
- Implications of political ability and willingness to make decisions that will keep a government fiscally sound

Research participants provided a diversity of responses within each of the eight components identified. There were a wide range of views on what specific information should be

included within each component. However, there were common concepts that characterized each component of fiscal sustainability.

The research on fiscal sustainability also confirmed that information about the interdependency of revenue sources, including intergovernmental revenues, is needed by users for assessing the economic condition of a government. Fiscal capacity, service capacity, and fiscal sustainability appear to depend on a consistent and reliable revenue stream. If these revenue sources are reduced or eliminated, and additional revenues cannot be obtained, then service levels, fiscal capacity, and the fiscal sustainability of a government will be negatively impacted.

Input from GASAC

A research status report was presented to the Governmental Accounting Standards Advisory Council (GASAC) at its March 2009 meeting and positive feedback was provided by the members. The GASAC members rated the project as a high priority at that time.

A draft project prospectus was presented to the GASAC at its August 2009 meeting and both positive and negative feedback was provided by the members. The GASAC members who responded that the project should be added to the GASB's current technical agenda were of the opinion that projecting the fiscal sustainability of state and local governments and disclosing the challenges they are facing is critical information necessary for users in making assessments and decisions. Some of the GASAC members who responded that they did not believe the project should be added to the GASB's current technical agenda were of the opinion that the project was a low priority and that there were other practice issues that the GASB should be addressing first. Others stated that they believed that the project was outside the GASB's mission.

III. RELEVANT LITERATURE

The National Council on Governmental Accounting (NCGA) in Concepts Statement No. 1, *Objectives of Accounting and Financial Reporting for Governmental Units*, highlights in paragraph 9 that one of the basic objectives of accounting and financial reporting for

governmental units is, “To provide financial information useful for determining and forecasting the financial condition of the governmental unit and changes therein:

- For determining the value and forecasting the service potential of resources held by the governmental unit.
- For determining whether the value and service potential of physical resources have been maintained during a period and forecasting the financial impact of maintaining or replacing service capacity.
- For forecasting the amounts and timing of future outflows resulting from existing commitments and the ability of the governmental unit to meet these when they come due.
- For determining and forecasting the cost of programs or services provided by the governmental unit.”

The Financial Accounting Standards Board (FASB) highlights the need for economic condition reporting in Statement of Financial Accounting Concepts No. 4 *Objectives of Financial Reporting by Nonbusiness Organizations* (SFAC 4). Paragraph 30 of SFAC 4 states: “Present and potential users of the information provided by financial reporting by a particular nonbusiness organization share a common interest in information about the services provided by the nonbusiness organization, its efficiency and effectiveness in providing those services, and its *ability to continue to provide those services*. Resource providers, such as members and contributors, may be interested in that information as a basis for assessing how well the organization has met its objectives *and whether to continue support*. Taxpayers may need similar information to *help them assess whether governmental units and government-sponsored entities have achieved their operating objectives*. In addition, they may want to know how the services provided by the governmental unit or government-sponsored entities are likely to *affect the amount of taxes and fees they will be required to pay* (emphasis added).” These concepts set forth FASB’s recognition of the potential need for financial reporting of economic condition information by nonbusiness entities.

In Concepts Statement No. 1, *Objectives of Financial Reporting*, the GASB identified the provision of information for the assessment of financial position and financial condition as necessary for state and local governments preparing external financial reports. The Concepts

Statement indicates that, “Financial reporting should assist in fulfilling a government’s duty to be publicly accountable and should enable users to assess that accountability by providing information to determine whether current-year revenues were sufficient to pay for current-year services. This also implies that financial reporting should show whether current-year citizens received services but shifted part of the payment burden to future-year citizens; whether previously accumulated resources were used up in providing services to current-year citizens, or, conversely, whether current-year revenues were not only sufficient to pay for current-year services, but also increased accumulated resources.” (paragraph 77a)

The Concepts Statement also indicates that, “Financial reporting should assist users in assessing the level of services that can be provided by the governmental entity and its ability to meet its obligations as they become due by (a) providing information about the financial position and condition of a governmental entity, (b) providing information about a governmental entity’s physical and other nonfinancial resources having useful lives that extend beyond the current year, including information that can be used to assess the service potential of those resources, and (c) disclosing legal or contractual restrictions on resources and risks of potential loss of resources.” (paragraph 79a,b, and c) [Note: As discussion later, the GASB now uses the term economic condition in place of financial condition to avoid confusion with financial position.]

In 1988, the GASB commissioned a study by Dr. Robert Berne to examine the degree to which GPEFR met the objectives outlined in Concepts Statement 1. Published as a GASB Research Report in October 1992, *The Relationships between Financial Reporting and the Measurement of Financial Condition* identified ten specific weaknesses in financial reporting relative to the information needs of financial condition analysis. Many of these shortcomings have been addressed by the standards issued by the GASB since 1992, most notably Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*. However, Berne (p. xv) also identified four “key aspects of financial condition” that remained largely unaddressed:

1. Economic and demographic information is reported only sporadically.
2. Most financial reporting does not even attempt to make interjurisdictional comparisons, and even the reporting of time series information is limited.
3. The political dimensions of financial condition are difficult to capture in financial reports.
4. A complete assessment of financial condition requires knowledge of how effectively and efficiently the resources raised are being used to deliver services. Within the current financial reporting framework, there is no requirement to report on “service efforts and accomplishments,” which would assist in assessing the government’s operations.

Berne also noted a consensus among users participating in the study regarding four characteristics of financial condition that are informative about the information needs of users. According to Berne (p. xii), users generally agree that financial condition (a) includes a time dimension, (b) is rooted in the government’s economic environment, (c) is a multidimensional or multiconstituency concept with complex interdependencies among the different parts, and (d) involves implicit as well as explicit obligations. The Berne report concludes by offering several alternatives for improving the ability of financial reporting to meet the information needs of financial condition assessment. The alternatives include enhancing the statistical section or creating a new, separate section of the comprehensive annual financial report (CAFR), issuing separate reports devoted to information about financial condition, and adding financial condition information to the transmittal letter, the notes to the financial statements, or separate official statements.

In 1993, a project on Financial Condition Reporting was added to the Board’s long-term research agenda to address the issues raised in the Berne report and to consider whether changes in standards could improve the effectiveness of state and local government financial reports in meeting the objectives to provide users with the information they need to assess financial condition. At that time, the perception of the meaning of financial condition and, consequently, the scope of the project was broader than the more commonly used financial position, but existing standards and Concepts Statements did not clearly distinguish between the two terms. As part of Concepts Statement No. 3, *Communication Methods in General Purpose External Financial Reports That Contain Basic Financial Statements*, issued in April 2005, the Board discussed the fact that the two terms have been used interchangeably in the governmental accounting literature (including Concepts Statement 1 and many GASB

standards), as well as in the business accounting literature. The Board tentatively decided that it would be useful to define the terminology more precisely.

The Board tentatively preferred a narrow definition of *financial position* similar to established dictionary definitions, which refer to the status of an entity's accounts as reported in a balance sheet. However, the Board viewed *financial condition* as a broader concept that incorporates but extends beyond financial position, similar to paragraph 34 of Concepts Statement 1. In that paragraph, financial condition is referred to as a government's "financial position and its ability to continue to provide services and meet its obligations as they come due." To avoid confusion with current usage of that term as equivalent to financial position, the Board tentatively adopted the term *economic condition*. That term was used in the NCGA's 1981 Research Report, *Objectives of Accounting and Financial Reporting for Governmental Units: A Research Study*, with a meaning similar to the definition in paragraph 34 of Concepts Statement 1. The NCGA research report stated as an objective that a financial report should provide information "useful for determining and predicting the economic condition of the governmental unit and changes therein." The research report further states that economic condition refers to how "well off" an entity is in economic value terms at a given point in time. Well off is described as the "ability of the governmental unit to sustain its operations, meet long-term obligations as they come due, and minimize the future burden on taxpayers and service recipients for financial contributions."

Based on its review of the NCGA Research Report, Concepts Statement 1, the Berne study, and other relevant literature, in January 2006, the Board developed a tentative definition of a government's economic condition. A government's financial position, along with fiscal capacity and service capacity, were identified as components of economic condition and were tentatively defined by the Board. These definitions were utilized as the working definitions for purposes of the fiscal sustainability research:

- Economic Condition is a composite of a government's financial position and its ability and willingness to meet its financial obligations and service commitments on an ongoing basis. Economic condition includes three components: financial position, fiscal capacity, and service capacity.

- Financial Position is the status of a government's assets, liabilities, and net assets, as displayed in the basic financial statements.
- Fiscal Capacity is the government's ability and willingness to meet its financial obligations as they come due on an ongoing basis.
- Service Capacity is the government's ability and willingness to meet its commitments to provide services on an ongoing basis.

Other Standards Setters, National Governments, and Other Organizations

Several other standards setters, national governments, and other organizations have established reporting standards focusing on fiscal sustainability or are currently deliberating the issues. These standards setters, national governments, and other organizations have focused on: (a) establishing a definition of fiscal sustainability, (b) determining the components of fiscal sustainability that should be reported, (c) establishing time periods for projecting fiscal sustainability information and (d) determining how to make fiscal sustainability assessments.

Defining Fiscal Sustainability

As noted above, currently there is no common accepted definition of fiscal sustainability. However, a number of formal or implied definitions of this term or related terms have been developed by other standards setters, national governments, and other organizations in their endeavors to establish standards or provide guidelines in the area of fiscal sustainability. The Federal Accounting Standards Advisory Board (FASAB), International Public Sector Accounting Standards Board (IPSASB), The United Kingdom's *Long-term public finance report: an analysis of fiscal sustainability*, The Chartered Accountants of Canada (CICA), and Australia's *Intergenerational Report* all establish unique definitions of fiscal sustainability. Some of the common themes running through all of these definitions developed by other standard setters, national governments, and other organizations include:

- The ability to continue public services and/or existing programs (FASAB, IPSASB, and CICA)

- The ability to meet financial commitments both now and in the future (IPSASB, Australia, United Kingdom, and CICA)
- The ability to maintain stability and predictability of future tax burdens which supports informed long-term decision making (FASAB)
- The ability to rely on a government's future revenue sources (United Kingdom)
- The ability to maintain reasonable levels of debt (FASAB, United Kingdom, and CICA).

Components of Fiscal Sustainability

The FASAB, IPSASB, the United Kingdom's *Long-term public finance report: an analysis of fiscal sustainability*, and Australia's *Intergenerational Report* also established individual components of fiscal sustainability which indicate the types of information needed by users of financial information to assess the fiscal sustainability of a governmental entity. Several common components (also referred to as indicators, requirements, and framework) were developed by other standard setters and national governments that also might be applicable to state and local governments. These components include:

- The present value of projected receipts and spending (FASAB and United Kingdom)
- Changes in projected future revenues and spending as compared to the prior year (FASAB and United Kingdom)
- Present and projected net debt and gross debt (IPSASB)
- Present and projected fiscal gap (deficits) or surpluses (FASAB and IPSASB)
- Present and projected financing/tax gap (IPSASB)
- Projected trends using specific alternative scenarios (FASAB)
- Present and projected net worth which is a broader measure of sustainability than net debt as it includes non-financial, as well as financial assets (United Kingdom).

Time Period for Projections

Along with no globally accepted definition of fiscal sustainability, there is no globally accepted time period for projections and assumptions provided within guidance already issued, or soon to be issued, by the other standards setters and national governments. There is an indirect relationship between the time period of a projection and the accuracy of the

information projected: generally the longer the time period of the projection, the less accurate the information being projected. This is due to the notion that assumptions become less reliable the longer you have to project them into the future. As a result, the various standards setters identify a diversity of time periods considered to be acceptable for projecting information into the future. The following time periods for projections of national governments that are being utilized by other standards setters and national governments include:

- FASAB’s Statement—75 years
- IPSASB’s Consultation Paper— preliminarily, minimum time period of 20 years
- Australia’s Report—40 years
- United Kingdom’s Report—30 years (certain cases where longer projections are used).

Fiscal Sustainability Assessments

Currently, other standards setters, national governments, and other organizations are not consistent in the basis they believe should be used in making assessments of fiscal sustainability. Some standards setters, like the FASAB in its recently approved standard and the IPSASB in a draft of their consultation paper, believe that the assessments of fiscal sustainability should be made on the basis of current policy without change or prediction of future events. Other national governments, like Australia and the United Kingdom, believe that the assessments of fiscal sustainability information should be made based on reasonable assumptions about future events.

Practitioner Writings

As noted in *Intergovernmental Financial Dependency and Related Risks* prepared by Cherry, Bekaert & Holland, L.L.P., information in state and local government financial reports regarding intergovernmental fiscal dependency is “difficult to identify” and there is “virtually no information about the degree to which these governments rely on support from other governments.” This report recommends information be reported by governments about “the government’s reliance upon direct and indirect intergovernmental flows; the governments exposure to changes in intergovernmental flows; and trends...relevant to the sustainability of

intergovernmental financial flows.” This report also provides specific recommended reporting requirements which include illustrations, guidance for the preparation of recommended reports, and a discussion of the forces driving the need to report intergovernmental financial dependency.

V. MAJOR ISSUES

Establishing a working definitions

Tentative working definitions for economic condition and its related components of financial position, fiscal capacity, and service capacity have already been established in the past by the Board; however, the definitions need to be reconsidered by the current Board members. In addition, the Board will need to consider establishing a working definition of fiscal sustainability. Currently, there is no common accepted definition of fiscal sustainability. As noted earlier, fiscal sustainability has been defined in a variety of ways by various standards setters and policy makers. Because the research has indicated that fiscal sustainability is a part of economic condition, a potential economic condition reporting project should consider the variety of definitions provided during this research to achieve the most appropriate comprehensive definition for state and local governments. It is critical to first establish a definition of fiscal sustainability because the definition will help determine what information needs to be considered for reporting in order to provide users with the ability to assess economic condition, including fiscal sustainability.

Determining what, if any, information is necessary to be reported

A major issue is determining what, if any, fiscal sustainability information a state or local government should report. In meeting the needs of the diverse users of state and local government financial information, it is important to determine the depth and breadth of information considered necessary by users in assessing fiscal sustainability. It will be critical to strike a balance between being comprehensive and practicable with regard to what information a government needs to report. Most notably, it will be necessary to determine whether information that is outside of the direct control of the government (such as economic or demographic information) but that directly effects the fiscal sustainability of the

government should be addressed. In assessing this area, the project also will consider issues associated with special purpose entities and small governments.

If the Board determines that users need additional fiscal sustainability information to assess a governmental entity's economic condition, the next major issue for the project would be to determine if GASB should provide guidance or guidelines. An economic condition reporting project should clearly show that economic condition reporting is a form of GPEFR that assists governments in meeting their responsibility to be publicly accountable. Furthermore, the project should explain why reporting on fiscal sustainability provides essential information on the financial health of a government that is not provided by traditional financial statements or other currently available sources.

Determining where to report necessary information on fiscal sustainability

If the Board determines that it is important for the GASB to provide guidance or guidelines for the reporting of fiscal sustainability information, then a decision will have to be made as to where the information should be reported within GPEFR.

Reporting forward looking information

Another major issue is whether or not governments should project fiscal information into the future and, if so, what assumptions should be used to execute those projections (for example, current policy, reasonable assumptions, or specific alternative scenarios). A related issue is determining the general time periods for reporting forward projected information.

The project should also address how reporting fiscal sustainability information will impact different types of governmental entities, and whether there should be different reporting requirements, recommendations, or guidelines for different types of governmental entities.

Finally, the issue of the reliability of information being reported should be addressed as it relates to information on fiscal sustainability. This issue is especially important as it relates to future projections and the level of assurance placed on such information.