



November 30, 2018

Memorandum

MEMBER ACTIONS REQUESTED:

By December 10, 2018, please review the materials and provide answers to the questions on page 7.

To: Members of the Board

From: *Ross Simms*
Ross Simms, Assistant Director

Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subj: Management's Discussion and Analysis—**TAB D**¹

OBJECTIVE

The objective is to determine the FASAB actions that might improve management's discussion and analysis (MD&A).

BRIEFING MATERIAL

The briefing material includes this memorandum and the following attachments:

- Attachment I: Illustrations of Alternative Formats provides examples of how the MD&A of two component reporting entities could be structured to distinguish program level information for users.
- Attachment II: Social Security Administration MD&A provides the Social Security Administration's MD&A
- Attachment III: Department of Veterans Affairs MD&A provides the Department of Veterans Affairs' MD&A

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.

BACKGROUND

During the October 2018 meeting, staff suggested eliminating the requirement for sections to permit more flexibility in presenting information in MD&A and facilitate an integrated discussion of the required topics. The Board determined that the requirement for sections should be retained but supported the notion of flexibility within a general framework of topical sections. The Board emphasized that sections and section headings assist users in locating the information they need, and the sections help ensure that management addresses all the required topics.

The Board also discussed stewardship investments and concluded that reporting entity MD&A should discuss the information. Users need the information to assess how the government has contributed to the nation's current and future well-being. The Board, however, decided to propose rescinding the requirement for required supplementary stewardship information (RSSI). Users rely on cash-based investment information rather than the accrual-based stewardship information and investment trend amounts expressed in constant dollars rather than current dollars. Once exposed, the proposal would provide feedback regarding the need for stewardship investment information.

NEXT STEPS

The next steps will be determined during the meeting.

MEMBER FEEDBACK

If you have any questions or comments, please contact Mr. Simms by email at simmsr@fasab.gov with a cc to paynew@fasab.gov by December 10, 2018.

MD&A FORMAT

Overview

Staff is proposing that the Board develop an interpretation to SFFAS 15. Users expect information regarding major programs and, in some instances, a discussion of program level information may be needed to help users understand the reporting entity's operations.² SFFAS 15, however, requires specific sections and it may not be clear how preparers should structure MD&A. The interpretation would clarify the purpose of the requirement, explain options that preparers have in discussing program level information, and discuss when program level discussions would be appropriate.

Discussing Programs in MD&A

MD&A should communicate managers' insights about the reporting entity; increase the understandability and usefulness of the general purpose federal financial report (GPFFR); and provide accessible information about the entity and its operations, service levels, successes, challenges, and future.³ While reporting entities primarily structure MD&A to provide information from an entity-wide perspective, users may look to MD&A for information on major programs⁴ or the services the entity provides. For instance, a reporting entity may administer a critical program that has a high level of public interest and management may discuss the program in MD&A to inform users of successes and challenges. Also, a reporting entity's GPFFR may consolidate dissimilar programs or a particular program may contribute significantly more toward the net cost of operations than other programs. A discussion regarding the nature of such programs could help users understand the reporting entity's operations.

Format of MD&A

Reporting entity management could structure MD&A in various ways to address the needs of their financial report users. The Board has noted that reporting entities need a flexible framework for discussing topics in MD&A and the reasoning for this view is that some topics, such as information on risks, could affect different levels (organization, sub-organization, program, or activity) of the reporting entity.

A concern is that current MD&A standards require sections that address the following topics: entity's mission and organizational structure; performance goals, objectives, and results; financial statements; and systems, controls, and legal compliance. MD&A should also address the future effects on the entity of existing, currently-known demands, risks,

² Office of Management and Budget Circular A-136, *Financial Reporting Requirements*, notes that the MD&A may discuss each major program identified on the statement of net cost and could include for each major program a summary of key risks, mitigation strategies, and any significant changes in financial and non-financial performance.

³ SFFAS 15.

⁴ Staff memo, Risk Assumed – TAB E, April 12, 2018.

uncertainties, events, conditions and trends.⁵ If management chooses to better inform users about major programs, it is not clear how best to structure MD&A to address all the required topics. For instance, should management address each topic for each major program or each major program within a specific topic? Figure 1: Example of MD&A Structures to Feature Program Information illustrates some of the possible structures intended to provide program level information.

⁵ SFFAS 15, pars. 2-3.

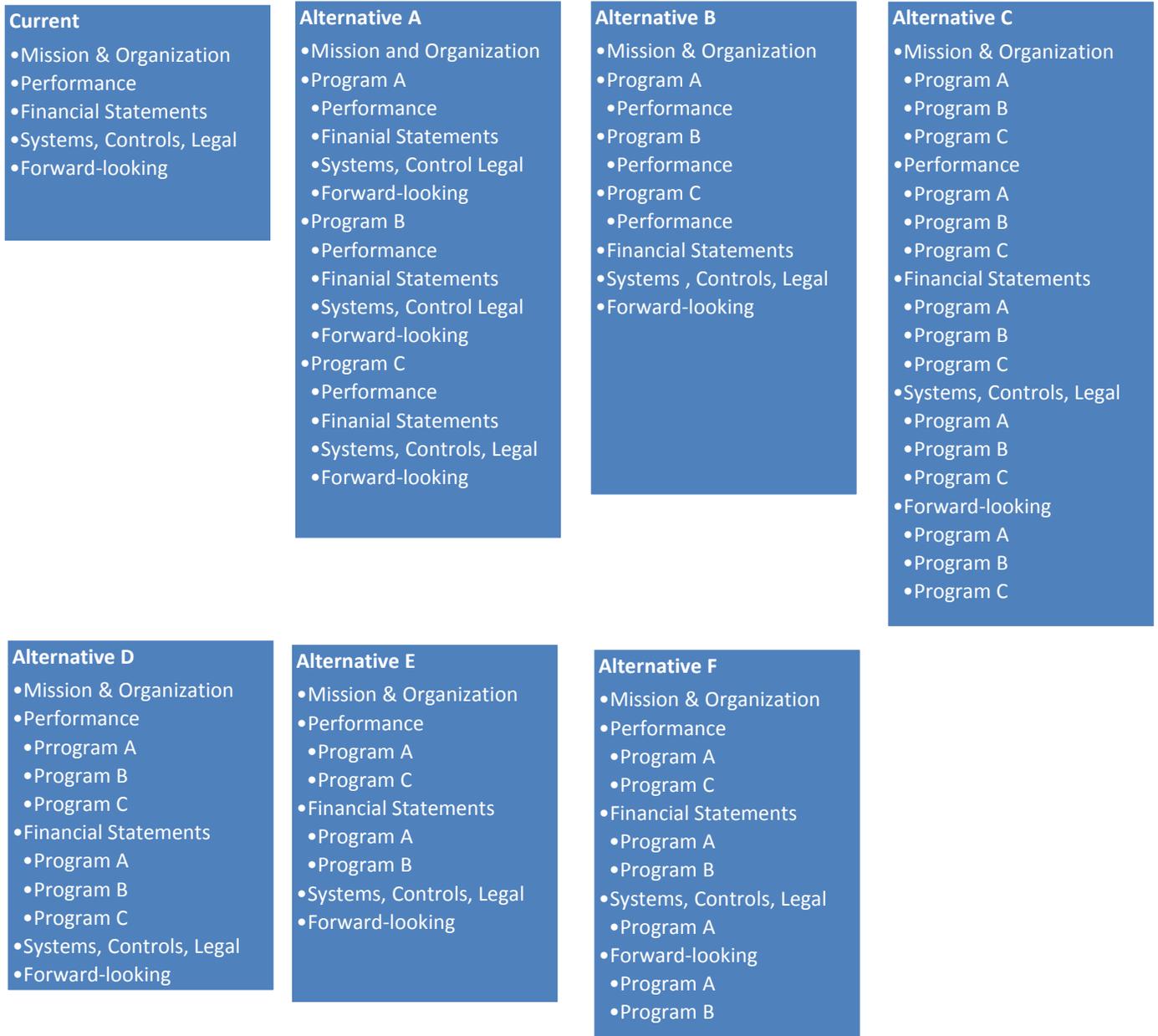


Figure 1: Example of MD&A Structures to Feature Program Information

The Purpose of Sections in MD&A

Separating MD&A into sections facilitates accessibility to information and helps users understand the information presented. The Board noted that sections and section headings

assist users in locating the information they need, and the sections help ensure that management addresses all the required topics. In addition, section headings may assist users in following the flow of the presentation.

Staff Recommendation

To clarify MD&A standards and encourage information about programs in MD&A, staff suggests developing an interpretation to SFFAS 15. The interpretation could explain the intent of the requirement for sections and the flexibility permitted in formatting MD&A. The interpretation could also inform preparers that management may use sections as necessary to help users understand the MD&A and key matters regarding the reporting entity. For example, management may provide an “overview” or “introduction” section that discusses the most important matters that management considered in its analyses of the entity and provide context for understanding the information presented. In addition, management may develop sections to discuss program or other sub-component information to assist users in understanding the operations of the reporting entity. For example, management may develop sections to discuss program level information when:

- a program contributes disproportionately to the net cost of operations
- simply an entity-wide discussion would present an incomplete or misleading perspective of the reporting entity, such as when existing, currently-known demands, risks, uncertainties, events, conditions and trends relate to a particular program or particular programs

Management may also combine interrelated topics in MD&A. For example, information on currently known risks or uncertainties may also help explain the financial statements and performance results.

Questions for the Board

1. Does the Board agree with the recommendation to develop an interpretation to SFFAS 15? The interpretation would clarify the flexibility permitted in formatting MD&A and how sections may be used to help users understand the information presented in MD&A and the operations of the reporting entity.
2. If the Board agrees with the recommendation to develop an interpretation, are there particular issues staff should ensure to consider or address?

Questions for the Board

1. Does the Board agree with the recommendation to develop an interpretation to SFFAS 15? The interpretation would clarify the flexibility permitted in formatting MD&A and how sections may be used to help users understand the information presented in MD&A and the operations of the reporting entity.
2. If the Board agrees with the recommendation to develop an interpretation, are there particular issues staff should ensure to consider or address?

Overview

Staff developed an illustration⁶ of Alternative A and Alternative C presented in Figure 1: Example of MD&A Structures to Feature Program Information. A reporting entity may consist of multiple programs with diverse objectives and operating characteristics. Providing entity-wide and program level discussions would assist users in understanding the reporting entity's performance.

Illustration of Alternative A: Social Security Administration⁷

- 1) Mission and Organization
 - a) Deliver quality social security services to the public
 - b) Administer three programs
 - i) Old-Age and Survivors Insurance (OASI)
 - ii) Disability Insurance (DI)
 - iii) Supplemental Security Income (SSI)
- 2) Reporting entity-wide matters – performance information including financial and non-financial measures, systems, controls, legal
 - a) Increase online service availability (target/actual, cost, savings estimates, and relationship to program areas (that is, mostly DI and SSI related)
 - b) Increase number of successful online transactions (target/actual, cost and savings estimates)
 - c) Provide real-time assistance to online users (target/actual, cost and impact on stakeholders)
 - d) Cybersecurity
- 3) Program A – OASI
 - a) Performance including financial and non-financial measures
 - i) Coverage rates and impact on poverty
 - ii) Cost of benefits & administrative services
 - b) Financial and Forward-looking
 - i) Financed by payroll taxes, interest on investments, and income taxes on benefits
 - ii) Liabilities grew by \$1.7 billion primarily due to the increase in the number of OASI beneficiaries and the 2 percent cost of living adjustment provided to beneficiaries
 - iii) Other information on OASI benefits (trends, trust balance and solvency, open & closed group analysis, other forward-looking measures such as ratio of beneficiaries to workers)
- 4) Program B – DI
 - a) Performance including financial and non-financial measures
 - i) Increase labor force participation (target/actual, cost and benefit reduction estimates)
 - ii) Reduce the number of actions pending at processing centers (target/actual, cost and impact on stakeholders)

⁶ Staff selected the reporting entities for illustrative purposes. The reporting entities received an unmodified opinion on their financial statements and prepared the MD&A in conformity with FASAB standards.

⁷ See Attachment II for SSA's actual MD&A.

- b) Financial and Forward-looking
 - i) Financed by payroll taxes, interest on investments, and income taxes on benefits
 - ii) Other information on DI benefits (trends, long-term effect of return to work efforts, trust balance and solvency, other forward-looking measures)
- 5) Program C – SSI
 - a) Performance including financial and non-financial measures
 - i) Improve the integrity of the SSI program
 - (1) Accuracy rate percentage of dollars paid (actual vs. target)
 - b) Financial and Forward-looking
 - i) Financed by general revenues from the Treasury
 - ii) Other information on SSI benefits

Illustration of Alternative C: Department of Veterans Affairs⁸

- 1) Mission and Organization
 - a) Program A – Veterans Health Administration (VHA)
 - i) Provides a broad range of primary care, specialized care, and related medical and social support services
 - b) Program B- Veterans Benefits Administration (VBA)
 - i) Provides a variety of benefits (compensation, pension, fiduciary services, educational opportunities, vocational rehabilitation and employment (VR&E) services, home ownership promotion, and life insurance) to Veterans and their families.
 - c) Program C – National Cemetery Administration (NCA)
 - i) Provides burial and memorial benefits to Veterans and their eligible family members
- 2) Performance goals
 - a) Entity-wide performance goals
 - i) Greater choice for veterans
 - ii) Improve timeliness of service
 - iii) Suicide prevention
 - iv) Others
 - b) Program A – VHA
 - i) identify and provide interventions for at-risk Veterans
 - c) Program B – VBA
 - i) Improve appeals process
- 3) Financial and forward-looking
 - a) Entity-wide information
 - i) Capital investment
 - (1) Expand facilities
 - b) Program A - VHA
 - i) Program costs increased due to increase personnel and wage and benefit costs
 - ii) Streamlining community care
 - c) Program B - VBA

⁸ See Attachment III for the Department of Veterans Affairs MD&A

- i) Compensation and pension benefit payments increased due to efficiency gains from transformational process changes and IT advances, resulting in a higher number of beneficiaries accessing and receiving benefits
- ii) Compensation and Burial increase is a result of the new legislation and administrative changes for initiatives which represent prior service costs
- iii) Others
- d) Program C – NCA
 - i) Financial data
- 4) Systems, Controls, Legal
 - a) Entity-wide
 - i) Modernizing systems
 - ii) Improper payments
 - iii) Control weaknesses and corrective actions
 - iv) Noncompliance with laws and corrective actions
 - b) Program A - VHA
 - i) Weaknesses in controls over Community Care Program and corrective actions have been taken
 - ii) Reducing improper payments
 - iii) Noncompliance and corrective actions
 - c) Program B – VBA
 - i) Control deficiencies related to compensation, pension, burial and education actuarial estimates
 - ii) Updating financial model
 - iii) Reducing improper payments
 - d) Program C – NCA
 - i) Systems, controls, and legal compliance information