



June 6, 2019

Memorandum

To: Members of the Board

*Robin M. Gilliam*

From: Robin M. Gilliam, Assistant Director

**MEMBER ACTIONS REQUESTED:**

Please review the materials and provide answers to the questions by **June 17, 2019**

*Monica R. Valentine*

Through: Monica R. Valentine, Executive Director

Subj: Management's Discussion and Analysis Amendments – **TAB G<sup>1</sup>**

**MEETING OBJECTIVE**

The objective is to discuss the Draft Proposal Statement to amend Statement of Federal Financial Accounting Standards (SFFAS) 15, *Management's Discussion and Analysis*.

**BRIEFING MATERIALS**

The briefing material includes this memorandum and the following:

**Attachment 1:** Draft Proposal Statement, *Improving Management's Discussion and Analysis, Amending SFFAS 15, Management's Discussion and Analysis*

**Attachment 2:** Analysis of SFFAC 3, *Management's Discussion and Analysis*, for standards-based language

**Appendix A:** Risk Reporting: Project History and Milestones

**Appendix B:** SFFAS 15, *Management's Discussion and Analysis*

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<sup>1</sup> 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

At the April 2019 Board meeting, the risk reporting project and reporting model phase I: MD&A and stewardship investments improvements project staff recommended amendments to Statement of Federal Financial Accounting Standard (SFFAS) 15.

Risk reporting project staff recommended a number of amendments to SFFAS 15 instead of developing an Interpretation—which was previously approved—because “financial effects” of risk events were not clearly stated in the standards, and therefore could not be interpreted. Staff also emphasized that Statement of Federal Financial Accounting Concepts (SFFAC) 3 was written as standards which should be included in SFFAS 15.

To understand the history and development of SFFAC 3 and SFFAS 15, Ms. Payne shared the following:

*The Board originally worked on MD&A during the window seeking GAAP recognition from the AICPA. Concept 3 was written more like a standard to holistically describe MD&A; but exposed as a concept statement.*

*During the response period, the audit and preparer community said that if FASAB wanted to achieve a GAAP based statement that always included MD&A, the Board must create a standard that required it. The Board, therefore, quickly used the MD&A outline from Concept 3 and proposed standard 15 as required supplementary information (RSI).*

*In Ms. Payne’s opinion, the concepts in SFFAC 3 are not concepts at all but standards, and a must read by preparers to really understand what should be included in MD&A.*

The reporting model phase I: MD&A and stewardship investments improvements project staff also proposed an amendment to SFFAS 15 to rescind Paragraph 2 and references in paragraphs 3 and 4 to the format requirements for sections. This amendment would permit reporting entities to structure MD&A in a manner most appropriate for communicating with general purpose federal financial report users.

The Board agreed to the following for both the risk reporting and MD&A Improvement projects:

- To expand the project to amend SFFAS 15 with the standard-type language currently included in SFFAC 3; noting the following
  - merely moving certain paragraphs from SFFAC 3 to SFFAS 15 will not address the issue that SFFAC 3 holds the actual standards language;

- amendments should occur simultaneously on SFFAC 3 and SFFAS 15;
- SFFAS 15 should become a standalone document that helps to change behavior; and
- amendments to SFFAS 15 should be principle based and not overly prescriptive.
- To remove guidance in SFFAS 15 requiring sections and allow for more flexible reporting;
- To amend paragraphs 3 and 4 in SFFAS 15 to
  - include SFFAC 3 standard-type language;
  - include a discussion on how to include “financial effects” in MD&A; and
  - include a distinction between risks versus problems, and financial versus non-financial.
- To improve financial analysis for material balance differences.
- To ensure amendments to SFFAS 15 encourage agencies to improve risk reporting as ERM processes evolve and improve.

#### **A. STAFF PROPOSAL:**

Staff developed a Draft Proposal Statement (Attachment 1) based on the Board’s discussions on Risk Reporting and MD&A Improvements projects at the April 2019 meeting.

In preparation, staff analyzed SFFAC 3 for standards-based language to determine what content could be incorporated into SFFAS 15 as amendments. Attachment 2, *Analysis of SFFAC 3, Management’s Discussion and Analysis*, for standards-based language, is available as a reference for members to review staff’s notes on recommendations and future considerations.

## **B. STAFF ANALYSIS AND RECOMMENDATIONS:**

### **1. ADDING THE MATERIALITY BOILERPLATE PARAGRAPH**

Staff recommends adding the materiality boilerplate paragraph to conform to current SFFAS formats.

In addition, staff recommends that management provides discussion and analysis on material changes to amounts in financial statements from factors that could affect achieving operational missions, such as strategic and performance goals, management systems and internal controls, legal compliance, budget integrity, currently known demands, events, conditions, and trends, and risks. As a result, staff recommends that materiality be the same throughout the entire agency financial statement.

Staff recommendations support members' agreement to create a financial centric focus in MD&A [April 2019 Board meeting—Risk Reporting] by removing any confusion about what to include in relation to: “discuss important problems;”<sup>2</sup> “most important matters to discuss;”<sup>3</sup> and “MD&A should deal with ‘vital few’” matters; i.e.”<sup>4</sup>

Please see **Attachment 1, #1** to review recommended amendments.

**QUESTION 1: Does the Board approve adding the MATERIALITY boilerplate paragraph to SFFAS 15?**

### **2. CHANGING “STANDARDS” HEADER TITLE**

Staff recommends changing the SFFAS 15 title from “STATEMENT of STANDARDS” to “STANDARDS” to conform to current SFFAS formats.

Please see **Attachment 1, #2** to review recommended amendments.

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<sup>2</sup> SFFAS 15, paragraph 4

<sup>3</sup> SFFAS 15, paragraph 5

<sup>4</sup> SFFAS 15, paragraph 6

**QUESTION 2: Does the Board approve updating the SFFAS 15 header title from “STATEMENT of STANDARDS” to “STANDARDS” to conform to current SFFAS formats?**

### **3. ADDING A SCOPE SECTION AND CONTENT**

Staff recommends adding a scope section to SFFAS 15 to conform to current SFFAS formats with four recommended paragraphs including a boilerplate paragraph of explanation.

Please see **Attachment 1, #3** to review recommended amendments.

#### **QUESTIONS:**

**3a – Does the Board approve adding a SCOPE section to conform to current SFFAS formats?**

**3b – Does the Board have any comments about the recommended scope content?**

### **4. ADDING A DEFINITIONS SECTION**

Staff recommends adding a definitions section to SFFAS 15 to define risk and other new relevant terms.

Please see **Attachment 1, #4** to review recommended amendments.

**QUESTION 4: Does the Board approve adding a DEFINITIONS section to SFFAS 15?**

## 5. REPLACING SFFAS 15 PARAGRAPH 2

At the February 2019 Board meeting—MD&A project discussion—the Board noted *that reporting entity mission-related programs, functions, and activities are complex; therefore, preparers need a flexible framework to discuss the topics SFFAS 15 requires. SFFAS 15, however, is explicit regarding the structure of MD&A and requires preparers to organize their discussion of specific topics into specific sections.*

The Board agreed that the requirement should be changed to provide the flexibility preparers need to communicate the required information to users. As a result, staff reviewed paragraphs 9-17 of SFFAC 3 to understand the foundation and intent of the information required and incorporated it into the recommended content to replace paragraph 2.

At the April 2019 Board meeting—Risk Reporting project discussion—members agreed that MD&A should be updated to focus on the financial effects of operating performance information. Therefore, staff added content in paragraph 2 to begin focusing the MD&A on a more financial centric discussion.

In addition, there was a lot of extraneous information in SFFAC 3, paragraphs 9-17 that staff did not include, such as questions to drive management’s analysis. Staff will consider incorporating this information into a future implementation guide.

Please see **Attachment 1, #5**, to review recommended amendments to replace SFFAS 15, paragraph 2.

**QUESTION 5: Does the Board have any comments about the recommended content to replace SFFAS 15 paragraph 2?**

## 6. REPLACING FASAB 15 PARAGRAPHS 3-7

At the April 2019 Board meeting—Risk Reporting project discussion—the Board agreed that SFFAC 3 included standards-based language that should be incorporated into SFFAS 15 to clarify the intent of forwardlooking discussions and create a stand-alone document that had a financial centric focus.

During the review of SFFAC 3 for standards-based language, staff found that paragraphs 14 and 26-39—*Discussion and Analysis of Financial Statements*—mapped closely to the intent of SFFAS 15 paragraphs 3-7. Therefore, staff incorporated standards-based information from SFFAC 3, paragraphs 14 and 26-39, into the SFFAS 15 amendments for paragraphs 3-7. This standards-based content will help preparers to focus on providing a discussion and analysis of material changes to amounts in financial statements from factors that could affect

achieving operational missions such as, strategic and performance goals, management systems and internal controls, legal compliance, budget integrity, currently known demands, events, conditions, and trends, and risks.

Staff recommends the following major changes to paragraphs 3-7:

- a. Staff separated risk from currently known demands, events, conditions, and trends, to address the Board's decision to provide a distinction between risks and problems, and to remove the gap—create a bridge—between an agencies risk management processes (enterprise risk management) and financial risk reporting.
- b. Staff removed information about “anticipated” because members agreed at the April 2019 Board meeting *that the amendment can address the word “anticipated” through updated wording for a risk discussion because risk is anticipated.* The risk definition will be developed at a future date and address “anticipated.”
- c. Staff removed information about estimates to focus on qualitative discussions versus quantitative content, per the Board's discussion at the April 2019 meeting.<sup>5</sup>
- d. Staff emphasized that preparers only include brief yet concise summaries throughout the recommended amendments to help reduce the current page volume of MD&A.
- e. Staff emphasized discussions that focus on reporting entities as a whole and any mission related programs, functions, and/or activities throughout the recommended amendments to help management develop a holistic MD&A.

Please see **Attachment 1, #6**, to review recommended amendments to replace SFFAS 15, paragraphs 3-7.

<p><b>QUESTION 6: Does the Board have any comments about the recommended content to replace SFFAS 15 paragraphs 3-7?</b></p>
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<sup>5</sup>Estimates required in MD&A from other standards, such as those in SFFAS 37, *Social Insurance: Additional Requirements for Management's Discussion and Analysis and Basic Financial Statements*, are not affected by this amendment.

## **BOARD QUESTIONS:**

**QUESTION 1:** Does the Board approve adding the MATERIALITY boilerplate paragraph to SFFAS 15?

**QUESTION 2:** Does the Board approve updating the SFFAS 15 header title from “STATEMENT of STANDARDS” to “STANDARDS” to conform to current SFFAS formats?

**QUESTION 3a:** Does the Board approve adding a SCOPE section to conform to current SFFAS formats?

**QUESTION 3b:** Does the Board have any comments about the recommended scope content?

**QUESTION 4:** Does the Board approve adding a DEFINITIONS section to SFFAS 15?

**QUESTION 5:** Does the Board have any comments about the recommended content to replace SFFAS 15 paragraph 2?

**QUESTION 6:** Does the Board have any comments about the recommended content to replace SFFAS 15 paragraphs 3-7?

## **NEXT STEPS**

The next steps for the project will be determined during the meeting.

## **MEMBER FEEDBACK**

If you have any questions or comments, please contact me by telephone at (202) 512-7356 or by email at [gilliamr@fasab.gov](mailto:gilliamr@fasab.gov) with a cc to Ms. Valentine at [valentinem@fasab.gov](mailto:valentinem@fasab.gov), by June 17, 2019.



TAB G

MD&A AMENDMENTS

ATTACHMENT 1

DRAFT PROPOSAL STATEMENT

*IMPROVING MANAGEMENT 'S DISCUSSION AND ANALYSIS*

*Amending SFFAS 15, Management's Discussion and Analysis*

JUNE 2019

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Federal Accounting Standards Advisory Board

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# IMPROVING MANAGEMENT'S DISCUSSION AND ANALYSIS

AMENDING SFFAS 15, MANAGEMENT'S DISCUSSION AND ANALYSIS

**Statement of Federal Financial Accounting Standards**

**Exposure Draft**

Written comments are requested by [date 90 days after issuance]

Month day, year

Working Draft – Comments Are Not Requested on This Draft

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## THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD

The Secretary of the Treasury, the Director of the Office of Management and Budget (OMB), and the Comptroller General of the United States established the Federal Accounting Standards Advisory Board (FASAB or “the Board”) in October 1990. FASAB is responsible for promulgating accounting standards for the United States government. These standards are recognized as generally accepted accounting principles (GAAP) for the federal government.

Accounting standards are typically formulated initially as a proposal after considering the financial and budgetary information needs of citizens (including the news media, state and local legislators, analysts from private firms, academe, and elsewhere), Congress, federal executives, federal program managers, and other users of federal financial information. FASAB publishes the proposed standards in an exposure draft for public comment. In some cases, FASAB publishes a discussion memorandum, invitation for comment, or preliminary views document on a specific topic before an exposure draft. A public hearing is sometimes held to receive oral comments in addition to written comments. The Board considers comments and decides whether to adopt the proposed standards with or without modification. After review by the three officials who sponsor FASAB, the Board publishes adopted standards in a Statement of Federal Financial Accounting Standards. The Board follows a similar process for Statements of Federal Financial Accounting Concepts, which guide the Board in developing accounting standards and formulating the framework for federal accounting and reporting.

Additional background information and other items of interest are available at [www.fasab.gov](http://www.fasab.gov):

- [Memorandum of Understanding](#) among the Government Accountability Office, the Department of the Treasury, and the Office of Management and Budget, on Federal Government Accounting Standards and a Federal Accounting Standards Advisory Board
- [Mission statement](#)
- [Documents for comment](#)
- [Statements of Federal Financial Accounting Standards and Concepts](#)
- [FASAB newsletters](#)

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## Federal Accounting Standards Advisory Board

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### ISSUE DATE

TO: ALL WHO USE, PREPARE, AND AUDIT FEDERAL FINANCIAL INFORMATION

The Federal Accounting Standards Advisory Board (FASAB or “the Board”) requests your comments on the exposure draft of a proposed Statement of Federal Financial Accounting Standards, entitled *Improving Management’s Discussion and Analysis: Amending SFFAS 15, Management’s Discussion and Analysis*. Specific questions for your consideration appear on page 4, but you are welcome to comment on any aspect of this proposal. If you do not agree with specific matters or proposals, your responses will be most helpful to the Board if you explain the reasons for your positions and any alternatives you propose. Responses are requested by **DUE DATE**.

All comments received by FASAB are considered public information. Those comments may be posted to [FASAB's website](#) and will be included in the project's public record.

Mail delivery is delayed by screening procedures. Please provide your comments by email to [fasab@fasab.gov](mailto:fasab@fasab.gov). If you are unable to email your responses, we encourage you to fax comments to 202-512-7366. Alternatively, you may mail your comments to:

Monica Valentine, Executive Director  
Federal Accounting Standards Advisory Board  
441 G Street, NW, Suite 1155  
Mailstop 1155  
Washington, D.C. 20548

We will confirm receipt of your comments. If you do not get a confirmation, please contact our office at 202-512-7350 to determine if your comments were received.

FASAB's rules of procedure provide that the Board may hold one or more public hearings on any exposure draft. No hearing has yet been scheduled for this exposure draft.

FASAB will publish notice of the date and location of any public hearing on this document in the Federal Register and in its newsletter.

Sincerely,

**D. Scott Showalter/George A. Scott**  
Chair

## EXECUTIVE SUMMARY

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### WHAT IS THE BOARD PROPOSING?

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FASAB is proposing this Statement to

- incorporate standards-based language from Statement of Federal Financial Accounting Concepts (SFFAC) 3, *Management's Discussion and Analysis*, into Statement of Federal Financial Accounting Standards (SFFAS) SFFAS 15, *Management's Discussion and Analysis*
- provide a stand-alone SFFAS for preparing Management's Discussion and Analysis (MD&A);
- update MD&A standards to include risk reporting as it pertains to using resources efficiently and effectively to achieve operating results and performance goals; and
- reduce preparer burden by streamlining MD&A to focus on material changes to amounts in financial statements and supplemental information resulting from management of operating performance for the reporting entity as a whole and any mission-related programs, functions, and/or activities.<sup>1</sup>

### HOW WOULD THIS PROPOSAL IMPROVE FEDERAL FINANCIAL REPORTING AND CONTRIBUTE TO MEETING THE FEDERAL FINANCIAL REPORTING OBJECTIVES?

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This proposal will improve federal financial reporting by providing a stand-alone Statement of Federal Financial Accounting Standards (SFFAS) for preparing MD&A. Currently, most of the standards-based language for developing Management's Discussion and Analysis resides in SFFAC 3 than in SFFAC 15.

The following history explains how SFFAC 3 has most of the standards-based language.

The Board originally worked on MD&A during the window in which it was seeking GAAP recognition from the American Institute of Certified Public Accountants (AICPA). SFFAC 3 was written more like an SFFAS to holistically describe MD&A even though it was exposed as a concepts statement.

During the response period, the audit and preparer community said to achieve a GAAP-based statement that always included MD&A, the Board must create standards that required it. The Board, therefore, quickly used the MD&A outline from SFFAC 3 and proposed SFFAS 15 as required supplementary information.

As a result, the guidance in SFFAC 3 is not concepts-based but standards-based and should be read with SFFAS 15 by preparers to understand what to include in MD&A. However, most preparers only rely on SFFAS 15—which is very limited.

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<sup>1</sup> FASAB is developing this proposal in response to a number of round tables and surveys that found MD&A to be too long, too dense, embellished with beautiful, but non-related pictures, and full of boilerplate language.

This proposal will incorporate the standards-based language from SFFAC 3 into SFFAC 15 to create a stand-alone document for preparing the GPFFR MD&A section.

This proposal will inform management about what required information to analyze and discuss about the reporting objectives to achieve a financial focus. The updated financial focus will help GPFFR users understand if resources were used efficiently and effectively in achieving performance goals for the reporting entity as a whole and any mission-related programs, functions, and/or activities.

In addition, this proposal should help to reduce preparer burden by streamlining MD&A to only focus on material changes to amounts in financial statements and supplemental information resulting from management of operating performance for the reporting entity as a whole and any mission-related programs, functions, and/or activities.

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## QUESTIONS FOR RESPONDENTS

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The Federal Accounting Standards Advisory Board (FASAB or “the Board”) encourages you to become familiar with all proposals in the Statement before responding to the questions below. In addition to the questions below, the Board also welcomes your comments on other aspects of the proposed Statement. Because FASAB may modify the proposals before a final Statement is issued, it is important that you comment on proposals that you favor as well as any that you do not favor. Comments that include the reasons for your views are especially appreciated.

The Board believes that this proposal would improve federal financial reporting and contribute to federal financial reporting objectives. The Board has considered the perceived costs associated with this proposal. In responding, please consider the expected benefits and perceived costs and communicate any concerns that you may have regarding implementing this proposal.

The questions in this section are available in a Microsoft Word file for your use at <http://www.fasab.gov/documents-for-comment/>. Your responses should be sent to [fasab@fasab.gov](mailto:fasab@fasab.gov). If you are unable to respond by email, please fax your responses to 202-512-7366. Alternatively, you may mail your responses to:

Monica Valentine, Executive Director  
Federal Accounting Standards Advisory Board  
Mailstop 1155  
441 G Street, NW, Suite 1155  
Washington, D.C. 20548

All responses are requested by **[insert date]**.

Q1. TBD

## PROPOSED STANDARDS

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### AMENDMENTS TO SFFAS 15, MANAGEMENT'S DISCUSSION AND ANALYSIS

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#### 1. Add **Materiality** boilerplate paragraph

*The provisions of this Statement need not be applied to immaterial items. The determination of whether an item is material depends on the degree to which omitting or misstating item about the information makes it probable that the judgement of a reasonable person relying on the information would have been charged or influenced by the omission of the statement.*

#### 2. Update header title from “**STATEMENT of STANDARDS**” to “**STANDARDS**” to conform to current standards structure.

#### 3. Add “**SCOPE**” Section to conform to current standard structure and the following content:

- a. This Statement applies when a reporting entity is presenting general purpose federal financial reports (GPFFRs), including the consolidated financial report of the U.S. Government (CFR), in conformance with generally accepted accounting principles (GAAP) as defined by paragraphs 5 through 8 of Statement of Federal Financial Accounting Standards (SFFAS) 34, The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board.
- b. This Statement provides general principles to guide reporting entities in developing the Management's Discussion and Analysis (MD&A) section of GPFFR with a financial centric focus in regards to the reporting entity as a whole and its mission-related programs, functions, and activities.
- c. To reduce burden of reporting, reporting entities should reference separate documents that provide detailed information to support brief yet concise summaries provided in the MD&A.
- d. MD&A is required supplementary information (RSI).

#### 4. Add “**DEFINITIONS**” Section to define “risk” and other new relevant terms (TBD).

## 5. Paragraph 2 is replaced with:

- a. MD&A should contain a brief but concise summary of the reporting entity's mission as a whole and for mission-related programs, functions, and/or activities.
- b. MD&A should present a complete analysis of the financial position and financial condition that will inform GPFFR users about the efficient and effective use of resources for the reporting entity as a whole and for mission-related programs, functions, and/or activities, to include discussions about strategic and performance achievements, management systems and internal controls, and legal compliance
  - i. MD&A should present a brief but concise summary of how any statistics presented for achieving/not achieving strategic and performance goals may affect the amounts reported in the financial statements and supplementary information.
  - ii. MD&A should present a brief but concise summary of how the status of management systems and internal controls may affect the amounts reported in the financial statements and supplementary information.
  - iii. MD&A should present a brief but concise summary of how legal compliance or lack thereof may affect the amounts reported in the financial statements and supplementary information.

## 6. Paragraphs 3-7 are replaced with:

- a. MD&A should discuss in a brief but concise summary the reporting entity's **financial position**.
  - i. MD&A should discuss any material changes in assets, liabilities, costs, revenues, and/or net position, and supplemental information, for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
- b. MD&A should explain factors, such as any strategic and performance goals, management systems and internal controls, and legal compliance issues, that contributed to material changes to the amounts reported in the financial statements and supplemental information, for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
- c. MD&A should discuss currently-known demands, events, conditions and trends that contributed to material changes in the amounts reported in the financial statements and supplemental information for the reporting entity as a whole and any mission-related programs, functions, and/or activities.

- i. MD&A should discuss actions needed, taken and planned to prevent currently-known demands, events, conditions and trends from causing negative material changes to amounts reported in the financial statements and supplemental information for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
- d. MD&A should describe risks existing as of the balance sheet date that could impact achieving operating performance for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
  - i. MD&A should explain mitigation strategy(s) for risks existing as of the balance sheet date that should help to achieve performance goals for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
- e. MD&A should describe risks existing as of the balance sheet date that could potentially have a material impact on financial statement amounts for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
  - i. MD&A should explain how risks existing as of the balance sheet date could materially affect the future financial position—financial statement amounts—for the reporting entity as a whole and any mission-related programs, functions, and/or activities if they are mitigated and if they are not mitigated.
  - ii. MD&A should explain mitigation strategy(s) for risks existing as of the balance sheet date that may help to prevent negative material changes to financial statement amounts reported for the reporting entity as a whole and any mission-related programs, functions, and/or activities.
- f. MD&A should explain in a brief but concise summary what budgetary and financing resources have been obtained and how they were used for the efficient and effective achievement of the mission-related programs, functions, and/or activities.
- g. MD&A should explain in a brief but concise summary the possible material impact of any currently-known demands, events, conditions, trends and/or risks on the **financial condition** on the national economy and society.<sup>2</sup>

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## EFFECTIVE DATE

### 7. Effective date TBD.

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<sup>2</sup> See SFFAC 1, *Objectives of Federal Financial Reporting*, paragraph 144, for more information about financial condition.

## APPENDIX A: BASIS FOR CONCLUSIONS

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This appendix discusses some factors considered significant by Board members in reaching the conclusions in this Statement. It includes the reasons for accepting certain approaches and rejecting others. Individual members gave greater weight to some factors than to others. The standards enunciated in this Statement—not the material in this appendix—should govern the accounting for specific transactions, events, or conditions.

This Statement may be affected by later Statements. The FASAB Handbook is updated annually and includes a status section directing the reader to any subsequent Statements that amend this Statement. The authoritative sections of the Statements are updated for changes. However, this appendix will not be updated to reflect future changes. The reader can review the basis for conclusions of the amending Statement for the rationale for each amendment.

### PROJECT HISTORY

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TBD

A1.

## APPENDIX B: ABBREVIATIONS

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AICPA	American Institute of Certified Public Accountants
CFR	Consolidated Financial Report of the U.S. Government
ED	Exposure Draft
FASAB	Federal Accounting Standards Advisory Board
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GASB	Governmental Accounting Standards Board
GPFFR	General Purpose Federal Financial Report
MD&A	Management's Discussion and Analysis
OMB	Office of Management and Budget
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards

### **FASAB Members**

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R. Scott Bell

Gila J. Bronner

Robert F. Dacey

**George A. Scott**

**Michael H. Granof**

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TAB G

MD&A AMENDMENTS

ATTACHMENT 2

Analysis of SFFAC 3,  
*Management's Discussion and Analysis*  
for standards-based language

JUNE 2019

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## Statement of Federal Financial Accounting Concepts 3: Management's Discussion and Analysis

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### Status

<b>Issued</b>	June 8, 1999
<b>Interpretations and Technical Releases</b>	
<b>Affects</b>	SFFAC 1, paragraph 181, by providing guidance on MD&A
<b>Affected by</b>	SFFAS 27, paragraph 39, amends paragraph 26

See pages 6-7 for the preamble to Statements of Federal Financial Accounting Concepts ([www.fasab.gov/pdffiles/handbook\\_preamble.pdf](http://www.fasab.gov/pdffiles/handbook_preamble.pdf)).

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### Summary

This document describes the concepts on which the Board relied in recommending standards for Management's Discussion and Analysis (MD&A) to be included in general purpose federal financial reports (GPFFR).<sup>1</sup> Concepts Statements are not authoritative in the sense that they do not establish standards or principles. Preparers may find them useful, but these concepts are not "prescribed guidelines" for required supplementary information as discussed in section 558 of the *Codification of Statements on Auditing Standards* published by the American Institute of Certified Public Accountants. No standards or prescribed guidelines for MD&A are presented in this statement of concepts.

MD&A is an important vehicle for (1) communicating managers' insights about the reporting entity, (2) increasing the understandability and usefulness of the GPFFR, and (3) providing accessible information about the entity and its operations, service levels, successes, challenges, and future. Some federal agencies also refer to MD&A as the "overview."

The basic concept that underlies the standards for MD&A is:

Each general purpose federal financial report (GPFFR) should include a section devoted to management's discussion and analysis (MD&A). It should address the reporting entity's performance measures, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address problems. The discussion and analysis of these subjects may be based partly on information contained in reports other than the GPFFR. MD&A also should address significant events, conditions, trends and contingencies that may affect future operations.

<sup>1</sup>The term general purpose financial report, abbreviated "GPFFR," is used as a generic term to refer to the report that contains the entity's financial statements that are prepared pursuant to federal accounting principles.

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### Concepts 3

~~A separate document titled *Standards for Management's Discussion and Analysis* presents the standards for MD&A. The standards for MD&A say that MD&A should address:~~

- ~~• the entity's mission and organizational structure;~~
- ~~• the entity's performance goals and results;~~
- ~~• the entity's financial statements;~~
- ~~• the entity's systems, controls, and legal compliance; and~~
- ~~• the possible future effects on the entity of existing, currently known demands, risks, uncertainties, events, conditions and trends.~~

~~The discussion and analysis of these subjects may be based on information in other discrete sections of the GPFFR or it may be based on reports separate from the GPFFR. The standards require MD&A should to be included in each GPFFR as required supplementary information (RSI).~~

**Comment [RG1]:** Recommend rescinding because this references a standard instead of discussing a concept.

**Comment [RG2]:** Incorporate into SFFAS 15 as an amendment

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## Statement Of Concepts

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### Basic Concept

1. Each general purpose federal financial report (GPFFR), ~~see figure 1 on 7~~ should include ~~a section devoted to~~ management's discussion and analysis (MD&A).<sup>1</sup> MD&A should address the reporting entity's program and financial performance measures, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address problems. The discussion and analysis of these subjects may be based partly on information contained in reports other than the GPFFR. MD&A also should address significant events, conditions, trends and contingencies that may affect future operations.

**Comment [RG3]:** Recommend rescinding this figure from SFFAC 3 – more suitable to SFFAC 2

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### Discussion and Rationale

2. A typical GPFFR is a highly summarized profile of a complex entity. It is based on conditions that exist at the reporting date and events that occurred in the preceding period. It shows what has happened, but it does not explain why it happened or what may reasonably be expected to happen in the future.
3. Financial reports have two key roles. One is a feedback role to provide information used for evaluating past decisions, expectations, and trends. Another is a predictive role to provide information used for formulating expectations and making decisions about the future. Both roles can be enhanced by insights and interpretations from an entity's management.
4. The managers of an entity have detailed knowledge of the transactions, events, and conditions reflected in the entity's financial report and of the policies that govern the entity's operations. The managers also have informed expectations regarding the future based on that knowledge. As a part of their stewardship responsibility, managers should explain the significance of key financial and nonfinancial information shown in the report, the strategies

**Comment [RG4]:** Pars 2 – 5 = concepts – move to SFFAC 2 or rescind if duplicated

<sup>1</sup>The term general purpose federal financial report, abbreviated "GPFFR," is used as a generic term to refer to the report that contains the entity's financial statements that are prepared and audited pursuant to the CFO Act of 1990, as amended. entities may refer to these reports using different terms, such as "Annual Report," "Accountability Report," "Financial Management report," etc. Paragraphs 54-112 and Appendix 1 of Statement of Federal Financial Accounting Concepts 2, *Entity and Display*, describe and illustrate the contents of the GPFFR. For more information on the "Accountability Report" see paragraph 59 and the glossary. (Other words defined in the glossary are marked with an asterisk.) See also *Toward a Report to Citizens on the State of their Nation and the Performance of Their Government: proceedings of the AGA Task Force on a Report to Citizens on the State of the Nation*, Association of Government Accountants, 1994.

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that led to the results reported, and the implications for future operations of events that have occurred or are likely to occur. The distinction between “financial” and “nonfinancial” information is arbitrary and often tenuous, but in this context “nonfinancial information” can include information on systems, controls, compliance with laws and regulations, and performance.

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

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## Background

6. The Securities and Exchange Commission (SEC) has for many years recognized the importance of such a narrative discussion of the financial statements. To serve the interests of investors and creditors, the SEC requires such a narrative discussion and analysis from management of companies under its purview. The SEC wants MD&A to help readers understand the entity’s financial position and results of operations with the benefit of management’s understanding and perspective. The SEC also wants MD&A to go beyond the basic financial statements, to include relevant forward-looking information. Research on MD&A for companies registered with the SEC shows that MD&A adds value to the financial statements. Forward-looking information, for example, can be an important contribution.<sup>2</sup>
7. Several factors suggest that MD&A may be even **more** important for Federal reporting entities than for those in the private sector and may need to be more extensive in scope. These factors include the complexity of Federal operations, the myriad objectives they pursue, and the diverse nature of the groups affected by and interested in the Government’s activities. Fundamentally, the Government’s objective is to provide for the common defense and to promote the general welfare, not to earn a profit. Therefore, reporting on performance and other matters in a way that is understandable to diverse audiences is

**Comment [RG5]:** Update discussion to replace with FASAB 30 years of experience

<sup>2</sup>Research on MD&A in private sector financial reporting suggests that forward-looking information in MD&A, in particular, is a significant source of added value for financial analysts. See Stephen H. Bryan, “Incremental Information Content of Required Disclosures Contained in Management Discussion and Analysis,” *The Accounting Review* Vol. 72 No. 2, (April 1997), pp. 285-301.

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important. For these reasons, both SFFAC 1, *Objectives of Federal Financial Reporting*, and SFFAC 2, *Entity and Display*, refer to MD&A in concept as part of the general purpose federal financial report.

8. Page 7 presents a schematic diagram of a sample GPFFR. It is schematic because the information called for by the statements of federal financial accounting standards should be located in the report in a logical sequence, not necessarily in the order shown. MD&A for the reporting entity as a whole normally will be located immediately after the agency head's letter. Reporting entities that organize their GPFFR by responsibility segment may combine MD&A regarding each segment; alternatively, they may have MD&A for each responsibility segment located separately in each of the respective subsections of the report. Preparers have flexibility to structure their report in the manner most appropriate under the circumstances. This diagram, the entire statement of concepts, and the accompanying standards for MD&A are intentionally written in general terms, in light of the evolving practice of performance reporting and accountability reporting in the federal government. The standards for MD&A define in general terms required supplementary information that should accompany financial statements prepared in conformance with federal accounting principles.

**Comment [RG6]:** Recommend Rescinding from SFFAC 3 – and moving to SFFAC 2 with diagram 1.

**FIGURE 1: Schematic Diagram of a Sample General Purpose Federal Financial Report**

Agency Head's Letter					
Management's Discussion and Analysis (RSI)					
<----- Other Elements of the General Purpose Federal Financial Report ----->					
1. Basic financial statements and notes, with auditor's report if audited	2. Required Supplementary Stewardship Information (RSSI)	3. Required Supplementary Information (RSI)	4. Performance Information	5. Other Accompanying Information (OAI)	6. Management's assertions and reports on controls, compliance, and corrective actions under FMFIA and FFMA (or portions of these assertions and reports)

The GPFFR is represented by MD&A plus columns 1-6 of the diagram. (The agency head's letter is part of the GPFFR by general practice, though it is not required by federal accounting principles.) This is not a literal depiction of the organization of a report. Information should be presented in a logical arrangement. MD&A will address major issues that are typically reported in more detail in the discrete sections of the GPFFR or in other publicly available reports that the GPFFR incorporates by reference. Incorporating another report by reference does not, by itself, mean that the separate report is subject to audit.

Unless law or managerial action requires more extensive audit review or examination of the material incorporated by reference, the FASAB expects that the auditor of the financial statements will treat the material incorporated by reference as other accompanying information, although it does not physically accompany the GPFFR. OMB has authority to provide specific guidance on the auditor's minimum responsibility regarding this material. OMB may, for example, direct auditors to treat the material incorporated by reference as if it were other accompanying information in an auditor-submitted document.

SFFAC 2 (paragraphs 106-111 and Appendix 1-F) calls for a "Statement of Performance Measures" as part of the GPFFR, but FASAB has not yet recommended standards for it. Other titles may be used for this section of the GPFFR. Performance indicators included in the GPFFR will either be those in the entity's annual performance report under the Government Performance and Results Act of 1993 (GPRA or the Results Act) or a subset of them.

Alternatively, that report may be incorporated by reference. Until further guidance is available, the agency should select the indicators to report in consultation with OMB.

The assertions and report on control called for by the Federal Managers Financial Integrity Act (FMFIA or Integrity Act) would not be stated in full in MD&A. They would be reported in a discrete section of the GPFFR or incorporated in the GPFFR by reference. They are within the scope of MD&A because highly important aspects of systems, compliance, and internal controls should be discussed in MD&A. "Highly important" in this context may imply a higher threshold than "materiality" for the financial statements.

If the report also includes financial statements for component entities (bureaus, responsibility segments, etc.), management should use its judgment in organizing the report. The component entities' financial statements may be discussed in separate sections of the report or as subsections of MD&A of the consolidated entity.

**Comment [RG7]:** Recommend Rescinding from SFFAC 3 – move to another SFFAC #?. Except concepts specific to MD&A

**Comment [RG8]:** Referenced in Materiality ED – GW

5/22/19 – recommended keeping Materiality same throughout AFR, including MD&A – should not be different.

Recommend creating a new concept just for Materiality and rescind Materiality discussion in all other Handbook chapters – too confusing how it is now and proposal on table.



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9. MD&A should address:

- the entity's structure, mission, goals, and objectives, with indicators<sup>3</sup> of its performance;
- actions taken or planned to improve performance, when appropriate;
- the financial statements;
- systems, internal controls<sup>4</sup> and legal compliance, including corrective action taken or planned; and
- (par 3) the future effects of existing, currently- known demands, risks, uncertainties, events, conditions and trends. MD&A may also address the possible future effects of anticipated\* future demands, events, conditions, trends, etc. that management believes would be important to the reader of the report.

10. MD&A should address these subjects even if, as will be true for many Federal reporting entities, separate documents report much of the information in more detail. Information about these subjects is essential to address the objectives of federal financial reporting regarding performance, stewardship, budgetary integrity, and systems and controls.

The following paragraphs explain the implications of this.

11. Regarding the entity's mission and performance, MD&A should inform the reader how well the reporting entity is doing. This means that it should tell the reader what the reporting entity and its programs have accomplished, and how well the entity is managing its programs. To do this, MD&A should answer such questions as:
- What do we need to know to gauge operating success?
  - How do we measure what we accomplished?
  - What do the measurements show?
12. To understand the information on performance, systems, controls, and legal compliance, it typically is necessary to understand something about the reporting entity's organizational structure, mission, and strategic plan. Accordingly, MD&A should concisely inform the reader about these topics.
13. Reporting information that helps people assess the performance of the Government's programs and organizations is an important objective of Federal financial reporting. For

<sup>3</sup>This document uses the terms "performance measure" and "performance indicator" synonymously. Some people use the term "performance indicator" instead of "performance measure" because the performance of government programs typically involves several factors or dimensions, and many of these dimensions of performance cannot be measured precisely.

<sup>4</sup>Words marked with \* are defined in the glossary.

**Comment [RG9]:** Incorporating pars. 9-17 to amend SFFAS 15 - paragraph 2

**Comment [RG10]:** Parking Lot – possibly implementation guidance

governmental entities, in contrast to profit-seeking entities, the financial result of governmental-type activities is rarely an adequate indicator of performance. (For a few governmental entities, mainly those that conduct primarily business-type instead of governmental-type activities, the financial results of operations may be an important, albeit rarely sufficient, performance indicator.) To assess performance, people need additional information on the consequences of the Government's activities. For a competitive, profit-seeking entity, the value of its products or services is measured by the amount of money customers are willing voluntarily to pay for them. In such a situation, the traditional income statement reports on both the efforts (measured by expenses incurred) and the accomplishments (measured by revenue earned) of the entity. For government, expense reflects efforts, as it does in the private sector, but indicators other than revenue must be used to report on accomplishments. A discrete section of the GPFFR therefore presents indicators of accomplishments (such as indicators of outputs and outcomes) and other indicators of performance. Alternatively, the GPFFR incorporates performance indicators by reference to a separate report such as the Annual Performance Report required by the Results Act. Either way, performance information is an integral part of the GPFFR and should be discussed in MD&A. Management's discussion and analysis should therefore address the most important facets of performance as well as the financial statements and supplementary information.

14. Regarding the financial statements, MD&A should answer questions such as the following, to the extent that they are relevant and important for the entity:

- What is the entity's financial position? What is its financial condition?<sup>5</sup> How did this come about?
- What were the significant variations:
  - from prior years?
  - from the budget?<sup>6</sup>
  - from performance plans, long-term plans, or other relevant plans in addition to the budget?
- What is the potential effect of these factors, of changed circumstances, and of expected future trends? In other words, to the extent that it is feasible to project the effects of these factors, will future financial position, condition, and results, as reflected in future financial statements, probably be different from this year's and, if yes, why? (Any such discussion should acknowledge that the future is unpredictable and will be

**Comment [RG11]:** Recommend rescinding beyond a concept discussion.

**Comment [RG12]:** Parking Lot – possibly implementation guidance

<sup>5</sup>The traditional concepts of "financial position" and "financial condition" are typically applicable to revolving funds, Government corporations, and other reporting entities that are intended to be self-financing. The concepts may be less relevant, or may require some qualification or modification, for other kinds of Federal reporting entities.

<sup>6</sup>Management should use its judgment to decide what variances are relevant for MD&A. It will not always be essential or appropriate to discuss all variances.

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influenced by factors outside the reporting entity's control, including actions by Congress.)

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15. Regarding systems and controls, MD&A should tell the reader whether internal accounting and administrative controls (some authorities prefer the term “management controls”) are adequate to ensure that:
- transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purposes authorized, and are recorded in accordance with Federal accounting standards;
  - assets are properly acquired and used, safeguarded to deter theft, accidental loss or unauthorized disposition, and fraud; and
  - performance measurement information is adequately supported.
16. Reporting information that helps people assess the condition of the entity's management systems and of the relevant internal controls is an important objective of Federal financial reporting. The relevant internal controls for this purpose are those that support reporting on financial and operating performance and reporting on compliance with applicable laws.<sup>7</sup> The great diversity of people (often with competing interests) affected by governmental action, and the fact that governments function within and by means of a framework of laws, mean that more attention to these matters is necessary than in financial reports for profit-seeking entities.
17. An entity's ability to prepare auditable financial statements and other reliable reports for management from the entity's books and records is a positive signal about the finance-related systems and controls of that entity. By themselves, however, the financial statements of a governmental entity do not provide adequate information about the status of the entity's management systems and internal controls that support reporting on financial and operating performance and reporting on compliance with applicable laws. For these reasons, the GPFFR of a Federal reporting entity should include information about systems, internal controls, and legal compliance, in addition to the basic financial statements. This information—like the information on performance—is presented in a discrete section of the GPFFR; alternatively it may be incorporated in the GPFFR by reference to separate reports such as those required by the Integrity Act. MD&A should therefore address the most important facets of this information on systems, controls and legal compliance, as well as the financial statements, supplementary information, and performance information.

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<sup>7</sup>Internal controls are also relevant to other objectives. For example, controls help management assure efficient and effective use of resources for the purpose intended. They also support preparation of performance reports pursuant to GPRA. See, for example, paragraph 40.

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## Relationship to Other Reports

18. The information in the GPFFR about systems, internal controls, and legal compliance (column 6 in figure 1) may include the assertions and a summary of the reports on controls, legal compliance, and corrective actions pursuant to the Integrity Act and the Federal Financial Management Improvement Act (FFMIA), or those reports may be incorporated by reference. This information should be presented in conformance with guidelines published by OMB. MD&A, in turn, should discuss the most important aspects of the information on these topics. Referring to separately-issued reports on systems and controls does not eliminate the need to discuss these topics in MD&A.<sup>8</sup>
19. The performance information (column 4 in figure 1) may include the indicators in an entity's performance report pursuant to the Results Act or a selection of the most important performance indicators. Alternatively, a separate performance report may be incorporated by reference. This information should be presented in conformance with guidelines published by OMB. MD&A, in turn, will discuss the most important aspects of the performance information. Reference to a separately-issued performance report does not eliminate the need to discuss performance in MD&A.
20. The performance reports required by the Results Act may be voluminous for some agencies. In such cases, it may not be desirable to include all this information in the GPFFR. It is necessary to include at least some information about performance with the financial statements, however, so that people who use the GPFFR can understand why the costs reported in the financial statements were incurred and the consequences of doing so.
21. In the same way, the GPFFR by itself may not provide a comprehensive report on systems, controls and legal compliance. There may be voluminous reports from management and auditors on these topics. It is necessary to include at least some information about these topics, however, so that users of the GPFFR can understand whether the resources on which it reports were properly safeguarded and used for the purposes intended, whether reliable reports can be prepared, and whether the other objectives of internal controls are being met. This information is important both to provide a basis for understanding the financial statements themselves and to address the objectives of federal financial reporting.
22. Combining information on these topics adds value by putting the information about performance, internal controls, and systems in the context of audited financial statements. For example, the quality of information on the cost of outputs and outcomes of programs is

**Comment [RG13]:** Recommend rescinding this section; amended SFFAS 15, paragraph 2 will capture updated requirements.

<sup>8</sup>Note that the purpose of the pilot Accountability Reports is to eliminate the need for numerous separate reports and to include the information required by those reports in a single report. For example, the Integrity Act requires an assertion on controls by the agency head. Pilot agencies are including this assertion in the Accountability Report.

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enhanced by linking these indicators to the audited Statement of Net Cost. This is true even though the Statement of Net Cost may be too highly aggregated to identify separately all the programs reported on for the Results Act. Similarly, the auditor's tests of transactions and controls in connection with the audit of the financial statements provide information about the condition of the systems and controls used to safeguard resources and to assure that they are used for the intended purposes, in conformance with law. (Paragraphs 15 and 40-49 say more about the discussion and analysis of systems, controls, and performance.)

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### Authoritative Status of Accounting Concepts

23. This Statement of Federal Financial Accounting Concepts describes ideas and goals to guide the Board in its work. Concepts are not authoritative in the sense that they do not constitute accounting standards or principles for federal reporting entities. In particular, they are not "prescribed guidelines" for required supplementary information as discussed in section 558 of the Codification of Statements on Auditing Standards published by the American Institute of Certified Public Accountants.

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### Topics For MD&A

24. This section provides specific suggestions for the content of MD&A. Like the other sections of this document, this material does not constitute accounting standards or principles for federal reporting entities. Except to the extent that OMB may issue supplementary mandatory guidance regarding the content of MD&A, the following items should be read as suggestions to be considered, not as prescriptive rules that must be followed.

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### Mission and Organizational Structure

25. MD&A should contain a brief description of the mission(s) of the entity and describe its related organizational structure.

**Comment [RG14]:** Included as amendment for SFFAS 15, par 2.

Recommend rescinding requirement to discuss organizational structure. This information does not any value; only increases reporting burden.

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## Discussion and Analysis of the Financial Statements

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26. **Financial Results, Position and Condition**<sup>9</sup>—MD&A should help those who read it to understand the entity's financial results and financial position and the entity's effect on the financial position and condition of the Government.<sup>10</sup> It should give readers the benefit of management's understanding of the significance and potential effect from both a short- and a long-term perspective of:
- the variations discussed in paragraph 14 in terms of major changes in types or amounts of assets, liabilities, costs, revenues, obligations and outlays;
  - particular balances and amounts shown in the basic financial statements, including the notes, such as those dealing with funds from dedicated collections, if relevant to important financial management issues and concerns; and
  - the entity's required supplementary stewardship information (because RSSI describes economic conditions that cannot be expressed in the basic financial statements).
27. Only those variations, balances and amounts, and stewardship matters of potential interest to readers who are not part of agency management should be discussed. Not all changes that are material to the GPFFR are sufficiently important to be included in MD&A. A line-by-line analysis of the financial statements is not generally appropriate. Instead, MD&A should summarize the most important items, explain the relevant causes and effects, and place them in context.
28. **Budgetary Integrity**—MD&A should concisely explain how budgetary resources have been obtained and used, instances in which their acquisition and use were not in accordance with legal authorization, the status of budgetary resources, and how information on the use of budgetary resources relates to information on the cost of program operations. MD&A should explain when major support for cost of a program or activity is provided outside the reporting entity's budget and when the entity's budget supports a program primarily reported by another entity. The discussion should describe major financing arrangements, guarantees, and lines of credit, including those not recognized in the basic financial statements.

**Comment [RG15]:** Information integrated from pars 14, 26-39 into SFFAS 15 amendments

<sup>9</sup>For many readers program performance information is more important than the financial statements. The order in which topics are discussed in this document does not imply that performance information is of secondary importance. See paragraphs 43 and following.

<sup>10</sup>Materiality of effects to be discussed should be evaluated in the context of the specific reporting entity, not the Government as a whole.

29. MD&A should explain major changes during the period to the budget originally approved, major failures to comply with finance-related laws, and other matters management believes necessary. These could include:
- unfunded liabilities that may require appropriations;
  - assets that could be sold to augment future budgetary resources;
  - amounts of payments that have not been matched with obligations;
  - anticipated increases in the cost to complete long-term projects in progress that may require additional obligations or appropriations.
30. Use of Estimates—MD&A should concisely explain the use of estimates where that is important to understand issues discussed in MD&A, such as the major risks and uncertainties mentioned in paragraph 31 or the key forward-looking information discussed in paragraph 32. For example, the future expenses and the long term obligations<sup>11</sup> associated with major social insurance programs such as Social Security and Medicare should be discussed in MD&A of the financial report of the relevant reporting entities. These estimates are inherently imprecise and sensitive to several assumptions. Such factors would, therefore, be worthy of discussion in MD&A.
31. Current Demands, Risks, Uncertainties, Events, Conditions, and Trends—MD&A should describe important existing, currently-known demands, risks, uncertainties, events, conditions and trends--both favorable and unfavorable--that affect the amounts reported in the financial statements and supplementary information. The information called for by this paragraph and paragraph 32 is closely related. Preparers should combine the presentation of this information in whatever fashion is appropriate under the circumstances that apply to the reporting entity.
32. Future Effects of Current Demands, Risks, Uncertainties, Events, Conditions and Trends—The discussion of these current factors should go beyond a mere description of existing conditions, such as demographic characteristics, claims, deferred maintenance, commitments<sup>12</sup> undertaken, and major unfunded liabilities, to include a discussion of the possible future effect of those factors. (This discussion of possible future effect of existing, currently-known factors is required pursuant to the standards in *Standards for Management's Discussion and Analysis*.)
33. Future Effects of Anticipated Future Events, Conditions, and Trends—To the extent feasible and appropriate, the discussion should also encompass the possible future effects of

**Comment [RG16]:** Recommend rescinding to reduce duplicity— estimates and assumptions and characteristics of uncertainty are discussed at length in notes that include estimates.

**Comment [RG17]:** Recommend rescinding all references to Standards for Management's Discussion and Analysis- SFFAC 3 is only concept statement that does that)

**Comment [RG18]:** Recommend rescinding all discussion of "anticipated" since risk is anticipated and uncertain.

<sup>11</sup>The term "obligations" is used here in the customary sense, not as it is used in budgetary accounting.

<sup>12</sup>The term "commitments" is used here in the customary sense, not as it is used in budgetary accounting.

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anticipated future events, conditions, and trends, although this additional information is not required by the standards for MD&A.<sup>13</sup> For example, MD&A might discuss the possible future effect of anticipated trends in the cost of inputs that may significantly affect future output costs. Other examples include the future effect of anticipated demographic trends, such as declining mortality rates, and the future effects of potential changes in behavior that may be caused by changes in Government programs. Such behavioral changes can greatly affect the future cost of some Governmental programs. For example, such effects can arise if subsidized insurance encourages the people or entities most at risk to participate in insurance programs (“adverse selection”) or encourages risky behavior (“moral hazard”).

34. An anticipated condition such as a prospective demographic trend or potential behavioral change may not, in itself, constitute a contingency or assumed risk that must be recognized, disclosed, or reported pursuant to SFFAS 5. Likewise, it may not be something that must be discussed in MD&A pursuant to the *Standards for Management's Discussion and Analysis*. Even so, if there is a reasonable prospect of a major effect on the reporting entity due to the anticipated condition, then MD&A should include this information to the extent feasible.
35. Where appropriate, the description of possible future effects of both existing and anticipated factors should include quantitative forecasts\* or projections<sup>13</sup>. Such forecasts or projections can show the implications of existing policies and conditions in light of anticipated or reasonably possible future conditions. For example, for MD&A of the Government-wide financial statements, long-term projections of the deficit or surplus may be important indicators of financial condition and sustainability. For insurance programs, this kind of projection—which actuaries sometimes call “dynamic analysis”—would consider possible interactions among current assets, reserves, policies in force, expected future business or populations covered by the insurance, and potential behavioral changes such as adverse selection and moral hazard, if appropriate. Some programs are inter-related among themselves and/or with conditions in the private sector. For example, flood insurance programs and disaster assistance programs may be related to such an extent that analysis of programs individually would not provide a good idea of their potential impact on the Government. To the extent feasible, projections should consider the potential implications of such relationships.
36. The future implications of current or anticipated factors often can better be expressed as a range of possible outcomes and associated probabilities than as a single point estimate. Sometimes the implications may best be discussed in nonfinancial as well as financial

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<sup>13</sup>Some projections that could involve consideration of anticipated factors would be presented as required supplementary stewardship information pursuant to the standards exposed for comment in FASAB's exposure draft Accounting for Social Insurance, February, 1998.



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terms. Forward-looking information can be highly useful, but management should avoid turning this part of MD&A into mere “lobbying” for more budgetary authority.

37. Understanding Financial Reporting—MD&A should make federal financial statements understandable to a wide audience, not just to users who are specialized analysts or members of the entity’s management. There may be many potential sources of misunderstanding. Management should try to identify those sources of misunderstanding that may be important and deal with them in MD&A. Some of these are general and pervasive, such as those that may arise in the minds of new users of federal financial statements. New users may have been budget-oriented rather than accrual-accounting oriented, or may be accustomed to seeing financial statements prepared on the basis of private sector accounting standards. A general discussion and reference to the Statement of Financing and the basis of accounting footnote may be sufficient for such users, although more specific treatment may be appropriate where the resulting differences in the reported amounts may be important to the understanding of users.
38. Emphasis that may be given in the financial statements to the costs of suborganizations and programs may require cautionary discussion of the relevance and utility of cost information. When MD&A itself discusses the cost of program outcomes, the problems of associating costs with outcomes may need to be discussed. In addition, the possible imprecision of cost information should be mentioned when it could be relevant to users’ understanding. Similarly, any account-level discussion in MD&A of variations, balances, and amounts in the basic and stewardship information made in response to paragraphs 26 and 27 may require mention of the imprecision of amounts cited.
39. Exceptions and disclaimers in the auditor’s report should be mentioned in MD&A, and management should respect the auditor’s professional judgment if management expresses disagreement with auditor’s findings. (This does not mean that management must refrain from stating views that differ from the auditor’s; e.g., different views as to whether a weakness in control is material.) There may be other sources of misunderstanding. Management should be sensitive to them and guide the user to a better understanding when the problem could significantly affect the conclusions and judgments of substantial numbers of users.

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### Discussion and Analysis of Systems, Controls and Legal Compliance

40. The schematic diagram of a sample GPFFR on page 7 includes a discrete section that reports on the status of the entity’s management systems and internal controls that support (1) preparation of financial statements and performance information in accordance with Federal Accounting Standards and management’s criteria, respectively, and (2) the entity’s

**Comment [RG19]:** Paragraphs 40-49 integrated into scope & other amendments to SFFAS 15. Therefore, recommend rescinding.

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compliance with applicable laws.<sup>14</sup> That section also describes material problems revealed by audits or otherwise known to management, and the corrective actions taken or planned regarding material problems.

41. Where relevant, management should discuss the results of audits of non-Federal entities such as those pursuant to the Single Audit Act as amended and OMB Circular A-133. MD&A should also discuss actions taken, in progress, or planned to address systemic problems in program design that contributed to the audit findings. Where relevant, management should describe the methods used to limit, detect, and recover improper payments; to assure that grantees and other nonfederal recipients of Federal funds use the funds as intended; and to assure that Federal and nonfederal entities comply with finance-related laws and regulations. MD&A should include a concise description of any major problems in these areas and of the corrective action taken or planned.

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## Discussion and Analysis of Performance

42. Performance Measurement—The objectives and needs of the Federal Government are markedly different from the objectives and needs of non-governmental organizations. This difference extends to the needs of those who use financial statements of governmental organizations. Their needs are different in many ways from the needs of investors, which the SEC's requirements address. In particular, reporting on the performance of governmental programs, organizations, and activities requires information that goes beyond the change in net assets and, indeed, beyond financial information.

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<sup>14</sup>These responsibilities are defined in numerous laws and administrative requirements, including the Federal Financial Management Improvement Act, OMB Circulars A-123 and A-127, and OMB Bulletin 98-08. A law of special importance in this connections is the Federal Managers' Financial Integrity Act of 1982 (FMFIA or the Integrity Act). The Integrity Act requires, in part, that "internal accounting and administrative controls of each executive agency shall be established.. and shall provide reasonable assurance that --

(i) obligations and costs are in compliance with applicable law;  
(ii) funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and  
(iii) revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets.

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43. The actual outcomes, accomplishments, or degree to which predetermined objectives are met provide indicators or measures of some aspects of effectiveness.<sup>15</sup> MD&A should objectively discuss the entity's program results and indicate the extent to which its programs are achieving their intended objectives.<sup>16</sup> Efficiency and effectiveness are important elements of performance measurement, and measuring cost is an integral part of assessing the efficiency and effectiveness of programs. Relating outputs (the quantity of services provided) to inputs (the cost incurred to provide the services) provides an indicator or measure of one aspect of efficiency. Information about effectiveness is often combined with cost information to help assess "cost effectiveness."
44. The entity's financial performance should be summarized to provide significant indicators of its financial operations for the reporting period. Indicators of financial performance are presented in notes and supplementary information as well as on the face of the principal financial statements, e.g., information about management of loans and accounts receivable. Financial performance is only one aspect of performance for governmental entities. Financial performance should be discussed to the extent relevant for the entity, in a way that appropriately balances the discussion of financial and nonfinancial performance relevant to the program or other reporting entity.
45. The discussion of performance should relate to major goals and objectives from the agency's strategic plan and to the indicators reported pursuant to the Results Act. It should explain what key performance indicators say about program performance. The summary discussion of performance in MD&A should:
- discuss the strategies and resources the agency uses to achieve its performance goals;
  - provide a clear picture of actual and planned performance across the agency; and
  - explain the procedures that management has designed and followed to provide reasonable assurance that the reported performance information is relevant and reliable.
46. The discussion of performance should:

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<sup>15</sup>SFFAC 1, paragraph 206 notes that, to the extent feasible and practical, effectiveness evaluation should focus on program results or effects in the sense of "impacts," i.e., the difference between what actually occurred and what would have occurred in the absence of the program. Assessing impacts of Governmental action in this sense typically requires program evaluations or other techniques that transcend annual performance reporting, although these techniques often will avail of information in the annual performance reports. Valid and reliable evaluations of program impacts are not feasible for some programs. When they are conducted, they often require several years of data, are expensive, and typically are not performed on an annual basis for a given program.

<sup>16</sup>Paragraphs 106-111 and Appendix 1-F of Statements of Federal Financial Accounting Concepts 2, *Entity and Display*, discuss and illustrate reporting on performance in the GPFFR.

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- include both positive and negative results;
  - present historical and future trends, if relevant (see paragraphs 31-36 regarding projections of the financial effects of known and anticipated demands, commitments, events, risks, uncertainties or trends for which a material financial effect is reasonably possible);
  - be illustrated with charts and graphs, whenever helpful, for easy identification of trends;
  - explain the significance of the trends;
  - provide comparison of actual results to goals or benchmarks;
  - explain variations from goals and plans; and
  - provide other explanatory information that management believes readers will need to understand the significance of the indicators, the results, and any variations from goals or plans.
47. To further enhance the usefulness of the information, agencies should include an explanation of what needs to be done and what they plan to do to improve program performance.
48. Understanding Performance Reporting—Important limitations and difficulties associated with performance measurement and reporting should be noted to the extent relevant to the vital performance indicators discussed in MD&A. The relevant limitations will vary from program to program, but some common factors that may need to be discussed include the following:
- performance usually cannot be fully described by a single indicator;
  - indicators of performance do not, by themselves, say why performance is at the level reported; and
  - focusing exclusively on quantifiable indicators can sometimes have unintended consequences.
49. For these and other reasons, performance indicators generally need to be accompanied by suitable explanatory information. Explanatory information helps report users understand reported indicators, assess the reporting entity's performance, and evaluate the significance of underlying factors that may have affected the reported performance. Explanatory information may include, for example, information about factors substantially outside the entity's control, as well as information about factors over which the entity has significant control.

***This Statement of Recommended Concepts was adopted unanimously by the eight members of the Federal Accounting Standards Advisory Board serving on the Board in April 1999.***

## Appendix A: Basis For Conclusions

This Statement may be affected by later Statements. The FASAB Handbook is updated annually and includes a status section directing the reader to any subsequent Statements that amend this Statement. Within the text of the Statements, the authoritative sections are updated for changes. However, this appendix will not be updated to reflect future changes. The reader can review the basis for conclusions of the amending Statement for the rationale for each amendment.

### Background and Project History

50. The Board identified MD&A as a topic for its agenda shortly after the Board's inception. The Board deferred work on this topic, however, until it completed recommendations for an initial set of basic accounting standards. FASAB published an initial exposure draft on MD&A in January, 1997. The Board received comment letters on the initial exposure draft from the following sources:

	Federal (internal)	Nonfederal (external)	Total
Users, Academics and Others <sup>17</sup>		4	4
Auditors	7	3	10
Preparers and Financial Managers	16		16
<b>Total</b>	<b>23</b>	<b>7</b>	<b>30</b>

51. The basic rationale for MD&A has not changed since the initial exposure draft. As a result of its deliberations after receiving comments on the 1997 exposure draft, however, the Board made certain changes. The more significant changes are discussed below.

### Concepts and Standards

52. The initial exposure draft was presented as a statement of recommended concepts. The Board proposed that it would deal with MD&A conceptually, with the understanding that OMB would provide authoritative guidance on MD&A to implement the concepts. This approach would have been similar to the one used to deal with the topics of entity and

<sup>17</sup>This category include representational organizations, retired federal employees, federal employees responding as individuals, and federal contractors, as well as academics and other GPFFR users.

display. The Board dealt with those topics conceptually in SFFAC 2. OMB then provided authoritative guidance in its Bulletin on Form and Content. The 1997 exposure draft asked respondents whether all or part of its provisions should be issued as recommended standards rather than recommended concepts. Responses were mixed; most of those who commented on this question favored concepts, but a significant number expressed the view that standards would be appropriate.

53. The Board concluded that, given the importance of MD&A as an integral part of the GPFFR, it would be appropriate to recommend standards for MD&A. At the same time, however, the Board concluded that for now this information should be treated as required supplementary information. The Board also agreed that no detailed requirements or guidelines for MD&A should be incorporated in federal accounting standards at this time beyond those proposed in the subsequent exposure draft (discussed below) titled *Standards for Management's Discussion and Analysis*. In other words, the Board agreed, a discussion and analysis that addresses the topics listed in the proposed standards should be an essential part of a complete GPFFR. At the same time, management should have great discretion about what to say regarding those topics, subject only to the criteria proposed in the exposure draft *Standards for Management's Discussion and Analysis* and the pervasive requirement that MD&A not be misleading. Because of this change, the Board decided to expose separately for further comment the proposed new standards and concepts. The exposure drafts were issued in October 1998; responses were requested by January 1999.

## Responses to Second Exposure Draft

54. The Board received comment letters on the second exposure draft from the following sources:

	Federal (internal)	Nonfederal (external)	Total
Citizens, Users, Academics and Others		3	3
Auditors <sup>18</sup>	3	3	6
Preparers and Financial Managers	11		11
<b>Total</b>	<b>14</b>	<b>6</b>	<b>20</b>

<sup>18</sup>Includes the AICPA's Federal Accounting and Auditing Subcommittee and the Comptroller General's Advisory Council on Government Audit Standards.

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55. Most comments were generally favorable, but comments were mixed regarding some points. A few auditors and preparers expressed some concern about requiring forward-looking information as RSI. Others expressed support for doing so. After considering these responses, the Board agreed to defer the recommended implementation date of the standard by one year and to make minor editorial changes to the standards and concepts that were exposed for comment.

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### Incorporation of Guidance in OMB Bulletin 97-01

56. This document, like both exposure drafts, integrates some of the guidance in OMB Bulletin 97-01 for preparing the “Overview” of the financial report with some of the guidance proposed in FASAB’s initial exposure draft for MD&A. Some portions of the guidance regarding performance measurement in 97-01’s discussion of the “Overview” have been omitted. As an interim step prior to implementation of the Results Act, OMB and many agencies used the Overview as a major vehicle for reporting on performance, not just as a summary and analysis. With the full implementation of the Results Act in FY 1999, however, it will be appropriate to implement the financial reporting model contemplated in SFFAC 2. This contemplates a discrete section of the GPFFR focused on performance. Alternatively, performance information may be incorporated in the GPFFR by reference to another report or reports.

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### Management’s Assertions

57. Senior management of the reporting unit is responsible for the content of the GPFFR, including MD&A. Consistent with that, the initial exposure draft included the following paragraph:
- MD&A should include a discrete section with management’s explicit assertions that it is responsible for maintaining internal accounting and administrative controls that are adequate to ensure that
- transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purposes authorized, and are recorded in accordance with Federal accounting standards;
  - assets are properly safeguarded to deter fraud, waste, and abuse; and
  - performance measurement information is adequately supported. [footnote omitted]
58. This paragraph, which was based on the language of objective four in SFFAC 1, was modified after the first exposure. The Board concluded that such assertions should be

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presented in a separate section of the GPFFR, not in MD&A. Alternatively, management's assertions about internal control and related information about systems, controls, and compliance may be incorporated in the GPFFR by reference to another report or reports. (As noted previously, pilot agencies are including these assertions in their accountability reports.) FASAB expects to consider whether a new statement of standards is needed to assure that Federal financial reports adequately address objective four of Federal financial reporting, "Systems and Controls." As noted in paragraph 41, MD&A should include a description of any major deficiencies in the management systems and internal controls designed to provide reasonable assurance that management responsibilities are satisfactorily carried out. It also should describe the corrective action planned.

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## Accountability Reports

59. The Board notes that the concept and practice of the "Accountability Report" continue to evolve through the pilot project voluntarily undertaken by several agencies. The Board supports this evolution and encourages agencies to participate in the pilot project. The concepts and standards FASAB recommends are intended to be applicable to the GPFFR of Federal entities, whether those reports are prepared pursuant to the Chief Financial Officers Act, the Government Management Reform Act, or some future law that might establish a statutory basis for Accountability Reports. In the event of such future legislation, OMB will need to resolve any questions about how to apply existing Federal accounting standards in the context of new legislative requirements.

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## Incorporation by Reference

60. Some respondents were disturbed by the notion of providing program performance information through reference. Some were concerned that, if readers are merely directed to other reports for this information, the GPFFR will become irrelevant. They believe that the GPFFR should contain information about program performance, systems, and controls, not only in MD&A but also in discrete sections, such as the Statement of Program Performance discussed and illustrated in SFFAC 2, paragraphs 106-111 and Appendix 1-F.
61. The Board agrees that, as is stated in paragraph 20, "it is necessary to include at least some information about performance with the financial statements . . . so that people who use the GPFFR can understand why the costs reported in the financial statements were incurred and the consequences of doing so."
62. The Board acknowledges that SFFAC 2 calls for and illustrates a Statement of Program Performance Measures. (Footnote 13 in SFFAC 2 explains that this statement is not "basic" information as that term is used in audit standards: "The Statement of program performance



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measures is not a basic financial statement. Nevertheless, it is an important component of the financial reports.”) The Board continues to believe that performance information is a vital, integral part of general purpose financial reporting. It should be noted, however, that SFFAC 1 and SFFAC 2 were issued before the performance planning and reporting requirements of GPRA became effective. The Results Act creates an elaborate new planning and reporting environment that is still evolving. Some details of the reporting model that were envisioned conceptually in SFFAC 2 may accordingly need to be revised slightly.

63. This statement of concepts is intended to be consistent with the previously stated goals and concepts of the Board, while recognizing that some details of how best to achieve those goals in the new context still need to be defined. OMB will play a key role in this process; FASAB may also provide further guidance in future projects. FASAB agrees that the GPFFR should not address performance, systems, and controls only by means of reference to other reports. The standards for MD&A require that MD&A do more than refer to other documents.
64. Others expressed concern that, if MD&A is to be regarded as RSI, audit problems might arise from “incorporation by reference” in MD&A of information drawn from other sources that might not be subject to audit or review as basic or required supplementary information, and for which authoritative guidance had not been provided by a standard setter. The Board noted that most of those who commented, including most auditors, did not appear to be greatly concerned about this potential problem. The Board concluded, therefore, that any such problems were not likely to be insurmountable. The Board did, however, agree to defer by one year the implementation date of the standard to allow OMB and GAO time to resolve any audit issues that may arise.

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## Appendix B: Glossary

See Consolidated Glossary in “Appendix E: Consolidated Glossary.”

TAB G

MD&A AMENDMENTS

APPENDIX A

## **Project History and Milestones**

**MD&A AMENDMENTS BEGINNING APRIL 2019**

[RISK ASSUMED/REPORTING October 2016 – December 2018]

**JUNE 2019**

## PROJECT OBJECTIONS

The issuance of [Statement of Federal Financial Accounting Standards \(SFFAS\) 51, Insurance Programs](#), on January 18, 2017, effectively concluded the first phase of risk assumed. For the history of the risk assumed project and milestones for phase I, please see <http://www.fasab.gov/ra-insurance-programs/>.

In phase II, the Board will holistically review significant risk events other than adverse events covered by SFFAS 51, Insurance Programs, to determine accounting standards that provide concise, meaningful, and transparent information regarding the potential impact to the fiscal health of the federal government.

## HISTORY OF BOARD DELIBERATIONS

### October 19-20, 2016 Board Meeting

At the October 19, 2016, Board meeting, the risk assumed – phase II began.

The Board reviewed staff's high-level gap analysis presented in table 1: Analysis of Federal Accounting Standards in Relation to the IMF [International Monetary Fund] Recommendations for Disclosing Fiscal Risks and table 2 from the Australian Statement 8: Statement of Risks.

The Board agreed that an extensive gap analysis is necessary to determine the risk information that the consolidated financial report of the U.S. Government includes and how it is presented, the extent to which FASAB can align with enterprise risk management (ERM) as prescribed by The Office of Management and Budget Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, and the Board's preference for presenting risk assumed information going forward.

For the gap analysis, the Board agreed to determine the following:

- If federal government reporting is transparent enough for estimates and uncertainty around significant risks with a focus on broad risk categories, such as an economic downturn where revenues go down and benefit program costs go up
- If there is a significant gap in reporting to be addressed for individual risk items, such as treaties, commitments by the federal government, and intergovernmental dependencies with state and local governments
- How to present summarized risk events at the government-wide level for cross-cutting agency efforts, such as disaster relief, with access to detail at the agency level

**December 19-20, 2016**

At the December 20, 2016, Board meeting, the Board approved a framework for the risk assumed gap analysis. Members agreed that categories should not be a laundry list of events but instead should be principle-based and broad enough to encompass current and future significant risk events. The scope will include past and future events and whether uncertainty is adequately explained. Staff will review past financial reports to understand what was included before and after recent large events, such as the 2008 financial crisis, at the agency and government-wide levels.

Staff will utilize roundtable discussions to discover if current disclosures are clear, relevant, and add value in relation to the available standards. If roundtable participants do not feel that current disclosures are clear, relevant, or valuable, the group will discuss what is missing and should be included.

Staff will work on the gap analysis over the next several months and present findings and recommendations to the Board upon completion.

**June 21-22, 2017**

Members did **not** want to include discussions that

- predict unforeseen catastrophes and their potential financial effect;
- trends for using emergency funding as an indicator of fiscal exposure to risk shocks;
- comparisons of estimates to actuals;
- how past risk events were managed; or
- a separate risk section [as presented in the USAFacts 10-K Report -risk section—Item 1A Risk Factors] within federal financial reports.

Members **did want to**

- include past events that affect the current financial position;
- include and define major risk events with a relationship to long-term sustainability that are not already reported;
- use the principle-based broad risk categories as a foundation for continuing the gap analysis; and

- present meaningful streamlined information as a broad analysis rather than specific details.

### October 25-26, 2017

According to the project objective, the risk assumed project strives ... to determine accounting standards that provide concise, meaningful, and transparent information regarding the potential impact to the fiscal health of the federal government. However, understanding what risks affect U.S. financial sustainability and why they do is very challenging. Therefore, as part of the ongoing gap analysis, staff reviewed SFFAS 2, Accounting for Direct Loans and Loan Guarantees, to learn how risk is currently disclosed in the financial statements.

Staff conducted research with the Department of Education, Department of Housing and Urban Development, Small Business Administration, and the Government Accountability Office and learned that agencies cannot specifically identify their users. In addition, reporting is inconsistent, extremely detailed, and burdensome. This not only affects preparers, but also users.

On October 26, 2017, staff presented these findings at the Board meeting to determine if members wanted to pilot amendments to SFFAS 2 to develop a framework for how to address risk assumed holistically.

Members agreed and requested that staff

- identify user groups to analyze risk factors, beyond those used to calculate credit subsidy reestimates, to help build a risk profile;
- develop a framework for how to discuss measurement uncertainty;
- consider how to discuss the “why” behind the “what” of risk;
- present sensitivity analysis at a future meeting; and
- pilot amendments to SFFAS 2 to develop a model/framework for how to address risk assumed holistically.

### FEBRUARY 21-22, 2018

The Board hosted an **ERM risk profiling education session**. The panel discussed the following:

- Ms. SallyAnne Harper, a founding member and immediate past president of the Association for Federal Enterprise Risk Management (AFERM), provided a high-level review of federal ERM.
- Mr. Tom Brandt, the Chief Risk Officer at the Internal Revenue Service (IRS) and AFERM President Elect, presented a review of IRS's risk profiling processes, including risk identification, categorization, assessment, quantification, measurement, and modeling.
- Mr. Mike Wetklow, Deputy Chief Financial Officer (CFO) and Division Director for Financial Management, National Science Foundation (NSF), presented NSF's ERM implementation process, including a discussion about risk appetite as an integral part of risk profiling.
- Mr. Daniel Fodera, Lead Management Analyst, Program Management Improvement Team, Directors of Field Services, Federal Highway Administration (FHWA), explained the tools used in ERM risk profiling, including the use of a heat map at FHWA.

The Board learned the following main points:

- Risk assessment is integrated into strategic planning and investment decision making to determine priorities and objectives.
- Senior management is responsible for setting risk appetite to determine the most significant risks that could impact the organization's strategic mission.
- Risk appetite includes an analysis of both the likelihood and impact of events.
- Most agencies are just beginning to develop their ERM processes; a few are moving into a more mature model.

**Directly following the education session, the Board discussed whether to leverage ERM risk profiling as identified in OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*.**

The Board agreed that staff should explore how to incorporate OMB A-123 risk profiling in the project; however members noted the following concerns:

- The Board should determine what type of risks to focus on: performance/programmatic—MD&A and/or financial impact—disclosure notes.
- The Board should determine what risks are not currently included in financial reports through working groups and determine the consequences of not including certain risks.

- The Board should consider producing best practices guidance if the standards are complete and agencies need additional help.
- The Board should prevent risk identification from turning into a compliance exercise that might affect the ERM process.
- The Board should consider how agency internal ERM processes might be affected by external financial reporting and the related audit.

#### APRIL 25-26, 2018

During the April 2018 meeting, staff presented the gaps for reporting RA as identified from the nine round tables conducted over the past year. Many round table participants were interested in reporting on full program costs, including key risk factors and assumptions. Some believed a **clearer understanding of uncertainties regarding estimates** would help facilitate better management decisions and **an understanding of financial performance**. These gaps will help to establish a framework for reporting RA holistically in the financial reports. This framework may include new or updated note disclosures and improvements to management's discussion and analysis (MD&A).

For MD&A improvements the RA and MD&A Improvements projects collaborated to present recommendations to improve MD&A. The projects collaborated because the findings from the separate round tables were the same—**financial statement users want to understand the financial performance for major programs and not have to sift through dense, duplicative strategic performance information that can be found in the agency performance report**. As a result, staff recommended a new Statement that would maintain the current principles but rescind Statement of Federal Financial Accounting Concepts (SFFAC) 3, *Management's Discussion and Analysis*, and Statement of Federal Financial Accounting Standards (SFFAS 15), *Management's Discussion and Analysis*.

The Board directed staff to consider previously discussed concerns regarding MD&A, review existing MD&A concepts and standards, and determine what changes might be needed. Staff will also collaborate with the Office of Management and Budget to determine whether form and content guidance could help guide improvements.

#### JUNE 27-28, 2018

The RA and MD&A Improvements projects continued to collaborate to request a more integrated format for MD&A.

Members agreed to remove the requirement to segment information in the MD&A. SFFAS15 currently requires management to discuss topics in discrete sections of the MD&A. Removing this requirement would allow flexibility in formatting MD&A and facilitate an integrated discussion about financial performance. The discussion should include the rationale for material changes in accounting elements, such as assets, liabilities, and/or net costs.



Staff originally presented a framework that would include a financial performance discussion for each responsibility segment presented in the statement of net cost. The discussions would inform users on the financial impact of key risks to the segment. However, the Board determined that key risk factors may affect entities at different levels and requested staff to present an alternative framework. The framework should be flexible enough to integrate risks that had or will have a significant financial impact at the level best defined by management.

Members requested that staff develop principle-based standards to address the different types of risks that may have a significant financial impact on the government-wide financial position, condition, or results of operations. To tell the entire financial story, members believed that management should discuss what actions are being taken to address current and future risk drivers, as well as forward-looking information.

### **August 29-30, 2018**

To better reflect the objectives, the risk assumed – phase II project was **renamed to the risk reporting project**.

The Board reviewed the measurement uncertainty framework it had requested at the October 2017 meeting. Because measurement uncertainty affects a number of estimates throughout the financial statements, the Board revisited the status of the risk assumed project. Members noted that the focus on risk assumed improved decisions in a number of projects despite the challenge of identifying specific risk measures as implied by the term “risk assumed.”

Members agreed that the risk assumed project should continue but is not likely to result in a specific measure of “risk assumed.” To avoid this expectation, the Board decided to change the project name to “risk reporting.” Members directed staff to work with the project leads of the reporting model phase I: MD&A and stewardship investments improvements project and the note disclosures project. Through this collaboration, the risk reporting project could address the principles needed for reporting financial and non-financial risks as well as the principles needed to account for measurement uncertainty.

### **December 19-20, 2018**

At the December 2018 meeting, members discussed the current status of risk reporting under SFFAS 15, paragraph 3 on forward-looking information. During the meeting, the Board discussed the intent of SFFAS 15 in relation to the forward-looking information provided by agencies’ in their 2017 MD&As.

Members agreed that the original intent for forward-looking information was to focus on the financial effects of risks on amounts in the financial statements even though the word “financial” was not specifically included in SFFAS 15, paragraph 3. However, this is not the information that agencies are providing.

Members also agreed that forward-looking information should include a discussion of the short-term financial effects, as well as the possible long-term material financial effects of

financial statement balances. Short-term effects relate to the budget cycle, while long-term effects may be defined by an agency's life cycle to complete program missions.

Members agreed that staff should prepare an Interpretation to clarify how to discuss risk in MD&A and explain what is meant by financial effect and time horizon. Additional guidance may be included in the Interpretation, such as sensitivity tests and/or best practices. To develop the Interpretation, staff will conduct a number of agency interviews to understand what guidance preparers need to discuss short- and long-term financial effects of risks.

Members agreed that the Interpretation addressing forward-looking information discussed in SFFAS 15, paragraph 3 will be separate from the Interpretation that will address MD&A structure. This is to avoid losing the risk reporting clarification within the formatting clarification.

## **RISK REPORTING MERGES INTO MD&A AMENDMENTS PROJECT**

**April 24-5, 2019**

At the April 2019 Board meeting, the risk reporting project and reporting model phase I: MD&A and stewardship investments improvements project staff recommended amendments to Statement of Federal Financial Accounting Standard (SFFAS) 15.

Risk reporting project staff recommended a number of amendments to SFFAS 15 instead of developing an Interpretation—which was previously approved—because “financial effects” of risk events were not clearly stated in the standards, and therefore could not be interpreted. Staff also emphasized that Statement of Federal Financial Accounting Concepts (SFFAC) 3 was written as standards which should be included in SFFAS 15.

To understand the history and development of SFFAC 3 and SFFAS 15, Ms. Payne shared the following:

*The Board originally worked on MD&A during the window seeking GAAP recognition from the AICPA. Concept 3 was written more like a standard to holistically describe MD&A; but exposed as a concept statement.*

*During the response period, the audit and preparer community said that if FASAB wanted to achieve a GAAP based statement that always included MD&A, the Board must create a standard that required it. The Board, therefore, quickly used the MD&A outline from Concept 3 and proposed standard 15 as required supplementary information (RSI).*

*In Ms. Payne's opinion, the concepts in SFFAC 3 are not concepts at all but standards, and a must read by preparers to really understand what should be included in MD&A.*

The reporting model phase I: MD&A and stewardship investments improvements project staff also proposed an amendment to SFFAS 15 to rescind Paragraph 2 and references in

paragraphs 3 and 4 to the format requirements for sections. This amendment would permit reporting entities to structure MD&A in a manner most appropriate for communicating with general purpose federal financial report users.

The Board agreed to the following for both the risk reporting and MD&A Improvement projects:

- To expand the project to amend SFFAS 15 with the standard-type language currently included in SFFAC 3; noting the following
  - merely moving certain paragraphs from SFFAC 3 to SFFAS 15 will not address the issue that SFFAC 3 holds the actual standards language;
  - amendments should occur simultaneously on SFFAC 3 and SFFAS 15;
  - SFFAS 15 should become a standalone document that helps to change behavior; and
  - amendments to SFFAS 15 should be principle based and not overly prescriptive.
- To remove guidance in SFFAS 15 requiring sections and allow for more flexible reporting;
- To amend paragraphs 3 and 4 in SFFAS 15 to
  - include SFFAC 3 standard-type language;
  - include a discussion on how to include “financial effects” in MD&A; and
  - include a distinction between risks versus problems, and financial versus non-financial.
- To improve financial analysis for material balance differences.
- To ensure amendments to SFFAS 15 encourage agencies to improve risk reporting as ERM processes evolve and improve.

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TAB G

MD&A AMENDMENTS

APPENDIX B

**SFFAS 15**

***Management's Discussion and Analysis***

JUNE 2019

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# Statement of Federal Financial Accounting Standards 15: Management's Discussions and Analysis

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## Status

<b>Issued</b>	August 12, 1999
<b>Effective Date</b>	For fiscal periods beginning after September 30, 1999
<b>Interpretations and Technical Releases</b>	
<b>Affects</b>	None.
<b>Affected by</b>	None.

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## Summary

This document establishes standards for preparing Management's Discussion and Analysis (MD&A). MD&A is an important vehicle for (1) communicating managers' insights about the reporting entity, (2) increasing the understandability and usefulness of the general purpose federal financial report (GPFFR),<sup>1</sup> and (3) providing understandable and accessible information about the entity and its operations, service levels, successes, challenges, and future. Some federal agencies also refer to MD&A as the "overview."

The basic concept that underlies the standards for MD&A is:

Each general purpose federal financial report (GPFFR) should include a section devoted to management's discussion and analysis (MD&A). It should address the reporting entity's performance measures, financial statements, systems and controls, compliance with laws and regulations, and actions taken or planned to address problems. The discussion and analysis of these subjects may be based partly on information contained in reports other than the GPFFR. MD&A also should address significant events, conditions, trends and contingencies that may affect future operations.

A separate document titled *Concepts for Management's Discussion and Analysis* explains the conceptual basis for the role and importance of MD&A, the general content of the GPFFR, and the elements of MD&A. The concepts provide a foundation for the standards presented in this document. The concepts include suggestions about the contents of MD&A, but those suggestions are not accounting standards or principles for federal reporting entities. In particular,

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<sup>1</sup>The term "general purpose federal financial report," abbreviated GPFFR, is used as a generic term to refer to the report that contains the entity's financial statements that are prepared and audited pursuant to the CFO Act of 1990, as amended. Entities may refer to these reports using different terms, such as "Annual Report," "Accountability Report," "Financial Management Report," etc. Paragraphs 54-112 and Appendix 1 of Statement of Federal Financial Accounting Concepts 2, Entity and Display, describe and illustrate the contents of the GPFFR.

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the concepts are not “prescribed guidelines” for required supplementary information as discussed in section 558 of the *Codification of Statements on Auditing Standards* published by the American Institute of Certified Public Accountants (AICPA). The only standards and prescribed guidelines for MD&A are in paragraphs 1-8 of this document.

The standards require MD&A to be included in each GPFFR as required supplementary information (RSI). MD&A should address:

- the entity’s mission and organizational structure;
- the entity’s performance goals and results;
- the entity’s financial statements;
- the entity’s systems, controls, and legal compliance; and
- the future effects on the entity of existing, currently-known demands, risks, uncertainties, events, conditions and trends.

The discussion and analysis of these subjects may be based on information in other discrete sections of the GPFFR or it may be based on reports separate from the GPFFR. The standards are effective for reporting periods that begin after September 30, 1999.

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## Management's Discussion And Analysis

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### Statement Of Standards

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1. A report that presents a Federal reporting entity's financial statements in conformance with Federal accounting principles should include management's discussion and analysis (MD&A) of the financial statements and related information. MD&A should provide a clear and concise description of the reporting entity and its mission, activities, program and financial performance, systems, controls, legal compliance, financial position, and financial condition. MD&A should provide a balanced presentation that includes both positive and negative information about these topics. MD&A should be regarded as "required supplementary information" as that term is used in auditing standards.<sup>2</sup>
2. MD&A should contain sections that address the entity's:
  - mission and organizational structure;
  - performance goals, objectives, and results;
  - financial statements; and
  - systems, controls, and legal compliance.
3. MD&A should include forward-looking information regarding the possible future effects of the most important existing, currently-known demands, risks, uncertainties, events, conditions and trends. MD&A may also include forward-looking information about the

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<sup>2</sup>See section 558, "Required Supplementary Information," in *Codification of Statements on Auditing Standards*, American Institute of Certified Public Accountants (AICPA)

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possible effects of anticipated future demands, events, conditions, and trends.<sup>3</sup> Forward-looking information may comprise a separate section of MD&A or may be incorporated with the sections listed above.

4. MD&A should discuss important problems that need to be addressed, and actions that have been taken or planned. Actions needed, taken, and planned may be discussed within the sections listed above or in a separate section of MD&A.
5. Because MD&A must be concise if it is to be useful, management must select the most important matters to discuss. This means that some items that are material to the financial statements, notes, and other sections of the GPFFR may not be discussed in MD&A.
6. MD&A should deal with the “vital few” matters; i.e., the most important matters that will probably affect the judgments and decisions of people who rely on the GPFFR as a source of information. (The specific topics mentioned in *Concepts for Management’s Discussion and Analysis* are examples of items that might be relevant for MD&A of a given entity.) Matters to be discussed and analyzed are those that management of the reporting entity believes it is reasonable to assume could:
  - lead to significant actions or proposals by top management of the reporting unit;
  - be significant to the managing, budgeting, and oversight functions of Congress and the Administration; or
  - significantly affect the judgment of citizens about the efficiency and effectiveness of their Federal Government.
7. Management of the reporting unit is responsible for the content MD&A.
8. The standards are effective for reporting periods that begin after September 30, 1999.

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<sup>3</sup>The word “anticipated” is used in a broad, generic sense in this document. In this context the term may encompass both “probable” losses arising from events that have occurred, which should be recognized on the face of the basic or “principal” financial statements, as well as “reasonably possible” losses arising from events that have occurred, which should be disclosed in notes to those statements. “Anticipated” may include the effects of future events that are deemed probable, for which a financial forecast would be appropriate. The term may also encompass hypothetical future trends or events that are not necessarily deemed probable, for which financial projections may be appropriate. Such information about the possible effects of anticipated future demands, events, conditions and trends, if presented, should include the term or label “projected” or “projection,” and the key hypothetical underlying assumptions should be explained. As with other information presented in MD&A, no examination of this information by the auditor is now routinely included within the scope of an audit of a federal entity’s financial statements; however, preparers and auditors may find useful background information in the AICPA’s Statements on Standards for Attestation Engagements Nos. 1 and 4, codified as section 200, “Financial Forecasts and Projections,” of the AICPA’s *Codification of Statements on Standards for Attestation Engagements*.

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***This Statement of Recommended Standards was adopted unanimously by the eight members of the Federal Accounting Standards Advisory Board serving on the Board in April 1999.***

## Appendix A: Basis For Conclusions

This Statement may be affected by later Statements. The FASAB Handbook is updated annually and includes a status section directing the reader to any subsequent Statements that amend this Statement. Within the text of the Statements, the authoritative sections are updated for changes. However, this appendix will not be updated to reflect future changes. The reader can review the basis for conclusions of the amending Statement for the rationale for each amendment.

### Background, Rationale, and Project History

9. The Board identified MD&A as a topic for its agenda shortly after the Board's inception. The Board deferred work on this topic, however, until it completed recommendations for an initial set of basic accounting standards.
10. FASAB published an initial exposure draft on MD&A in January, 1997. It was presented as a statement of recommended concepts rather than standards. The Board proposed that it would deal with MD&A conceptually, with the understanding that OMB would provide authoritative guidance on MD&A to implement the concepts. This approach would have been similar to the one used to deal with the topics of entity and display. The Board dealt with those topics conceptually in SFFAC 2. OMB then provided authoritative guidance in its Bulletin on Form and Content.
11. The Board received comment letters on the initial exposure draft from the following sources:

	<b>Federal (internal)</b>	<b>Nonfederal (external)</b>	<b>Total</b>
Citizens, users, academics and others <sup>4</sup>		4	4
Auditors	7	3	10
Preparers and financial managers	16		16
<b>Totals</b>	<b>23</b>	<b>7</b>	<b>30</b>

<sup>4</sup>This category includes representational organizations, retired federal employees, federal employees responding as individuals, and federal contractors, as well as academics and other GPFFR users.

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## Concepts and Standards

12. The first exposure draft asked respondents whether all or part of the exposure draft's provisions should be issued as recommended standards rather than recommended concepts. Responses were mixed; most of those who commented on this question favored concepts, but a significant number expressed the view that standards would be appropriate. The Board concluded that, given the importance of MD&A as an integral part of the GPFFR, it would be appropriate for federal accounting principles to include standards for MD&A.
13. At the same time, the Board concluded that MD&A should be treated as required supplementary information. The Board agreed that it would recommend no detailed requirements or guidelines for MD&A at this time, beyond those in paragraphs 1-8. In other words, a discussion and analysis by management that addresses the listed topics should be required, because it is an essential part of a complete GPFFR. At the same time, management should have great discretion regarding what to say about those topics, subject only to the criteria in paragraphs 1-8 and the pervasive requirement that MD&A not be misleading. The standard itself, therefore, is not extremely prescriptive.
14. Because of this change from what was originally exposed for comment, the Board decided to expose separately the proposed standards and concepts for further comment. The exposure drafts were issued in October, 1998; responses were requested by January 1999. The proposed standard, like the final recommended standard, would require the auditor to note the omission of MD&A or the failure to address the specified topics. At the same time, RSI status for MD&A—coupled with the lack of specific, detailed, prescriptive standards for the content of MD&A—would minimize the requirement for the auditor to scrutinize MD&A. This, the Board believed, would provide the flexibility appropriate for dealing with topics such as performance measurement at this point in the evolution of federal financial reporting.

## Responses to Second Exposure Draft

15. The Board received comment letters on the second exposure draft from the following sources:

	Federal (internal)	Nonfederal (external)	Total
Citizens, users, academics and others		3	3
Auditors <sup>5</sup>	3	3	6
Preparers and financial managers	11		11
<b>Totals</b>	<b>14</b>	<b>6</b>	<b>20</b>

16. Most comments were generally favorable, but comments were mixed regarding some points. A few auditors and preparers expressed some concern about requiring forward-looking information as RSI. Others expressed support for doing so. After considering these responses, the Board agreed to defer the recommended implementation date of the standard by one year and to make minor editorial changes to the standards and concepts that were exposed for comment.
17. Although the resulting standard differs from private sector standards, the Board expects that, in practice, the effect on auditors will not be greatly different.<sup>6</sup> In the private sector, corporations frequently include with their annual financial report the MD&A that they are required to file with the SEC. Because it is required by the SEC rather than by accounting standards, the auditor engaged to audit the corporation's financial statements normally treats MD&A as "accompanying information" that is not audited in the context of the audit of the financial statements. The auditor also may review the submission to the SEC and may have certain responsibilities in that regard, but the auditor's usual role regarding MD&A is, nevertheless, fairly limited.
18. Because this standard defines MD&A for federal reporting entities as RSI, auditors will have certain responsibilities regarding it; however, both the accounting standards specified here and the auditing standards specified by the AICPA (and incorporated in Government Audit Standards) for RSI are rather general. Therefore, the Board does not expect that this standard will cause the auditor to be deeply involved in reviewing the contents of MD&A.

<sup>5</sup>Includes the AICPA's Federal Accounting and Auditing Subcommittee and the Comptroller General's Advisory Council on Government Audit Standards.

<sup>6</sup>The standard itself differs from the SEC's guidance for MD&A in ways that reflect the unique federal reporting environment. This will affect what financial statement preparers must do to comply with the standard. For example, reporting on performance of governmental programs requires measures in addition to net income or net cost.

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19. More specific requirements regarding the content of MD&A may be added later by OMB acting on its own authority or pursuant to future FASAB recommendations. For example, OMB might at some time in the future require preparers to address certain of the suggested items in Concepts for Management's Discussion and Analysis. OMB also may provide more specific guidance regarding the auditor's responsibility for MD&A. That guidance may call for more extensive review of all or parts of MD&A than the minimum contemplated by this accounting standard in the context of current auditing standards. For example, OMB might at some time in the future decide that the minimum scope of engagements to audit federal financial statements should be expanded to include a review or examination of all or parts of MD&A, consistent with attestation guidelines published by the AICPA.<sup>7</sup>
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## Accountability Reports

20. The Board notes that the concept and practice of the "Accountability Report" continue to evolve through the pilot project voluntarily undertaken by several agencies.<sup>8</sup> The Board supports this evolution and encourages agencies to participate in the pilot project. The concepts and standards FASAB recommends are intended to be applicable to the GPFFR of Federal entities, whether those reports are prepared pursuant to the Chief Financial Officers Act, the Government Management Reform Act, or some future law that might establish a statutory basis for Accountability Reports. In the event of such future legislation, OMB will need to resolve any questions about how to apply existing Federal accounting standards in the context of new legislative requirements.
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## Forward-looking Information

21. MD&A should include forward-looking information regarding the future effects of existing, currently-known demands, risks, uncertainties, events, conditions and trends. This kind of
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<sup>7</sup>See Statement on Standards for Attestation Engagements No. 8, *Management's Discussion and Analysis*, issued by the Auditing Standards Board of the AICPA, March 1998.

<sup>8</sup>Accountability reports are broader in scope than traditional general purpose financial reports. As explained by OMB: "Six pilot agencies volunteered to produce an 'Accountability Report' for FY 1995 to provide more useful information to decision makers by linking together information required by several management statutes... Accountability Reports integrate the following information: the FMFIA report, the CFOs Act Annual Report (including audited financial statements); management's Report on Final Action as required by the IG Act; Civil Monetary Penalty and Prompt Payment Act reports; and available information on agency performance compared with its stated goals and objectives, in preparation for implementation of GPRA." *Federal Financial Management Status Report and Five Year Plan*, June 1996, pp. 33-34. Twelve agencies produced accountability reports for FY 1997; eighteen plan to do so for FY 1998; the number will increase to 23 for FY 2000. (The requirement to include Civil Monetary Penalty and Prompt Payment Act reports has been deleted.)

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forward-looking information is required when management believes it would be important to people who read the financial report. Though not required, MD&A may also include forward-looking information about the possible effects of anticipated future demands, events, conditions, and trends. FASAB encourages management to include forward-looking information about the possible effects of anticipated future demands, events, conditions, and trends to the extent management believes such information would be useful and relevant. This information can be highly useful, but management should avoid turning this part of MD&A into mere “lobbying” for more budgetary authority.

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## Incorporation by Reference

22. Some respondents expressed concern that, if MD&A is to be regarded as RSI, audit problems might arise from “incorporation by reference” in MD&A of information drawn from other sources that might not have been subject to audit or review as basic or required supplementary information, and for which authoritative guidance had not been provided by a standard setter. The Board noted that most of those who commented, including most auditors, did not appear to be greatly concerned about this potential problem. The Board concluded, therefore, that any such problems were not likely to be insurmountable. The Board did, however, agree to defer by one year the implementation date of the standard to allow OMB and GAO time to resolve any audit issues that may arise.