



Federal Accounting Standards Advisory Board

August 13, 2020

Memorandum

MEMBER ACTIONS REQUESTED:

Please review the materials and answer the questions by **August 20, 2020**

To: Members of the Board
From: Ross Simms and Robin Gilliam, Assistant Directors
Through: Monica R. Valentine, Executive Director
Subject: Reporting Model – Note Disclosures – **TAB G¹**

MEETING OBJECTIVE

In support of the reporting model initiative, the Note Disclosures (ND) meeting objective is to review the timeline of Board decisions made to reach the current approach and proposed concepts for types of information to include in ND concepts.

BRIEFING MATERIALS

The briefing materials include this memorandum and Appendix I: Reporting Model Comparison that discusses differences between the FASAB and Financial Accounting Standards Board (FASB) reporting models.

You may electronically access the briefing material at <https://fasab.gov/board-activities/briefing-materials/>

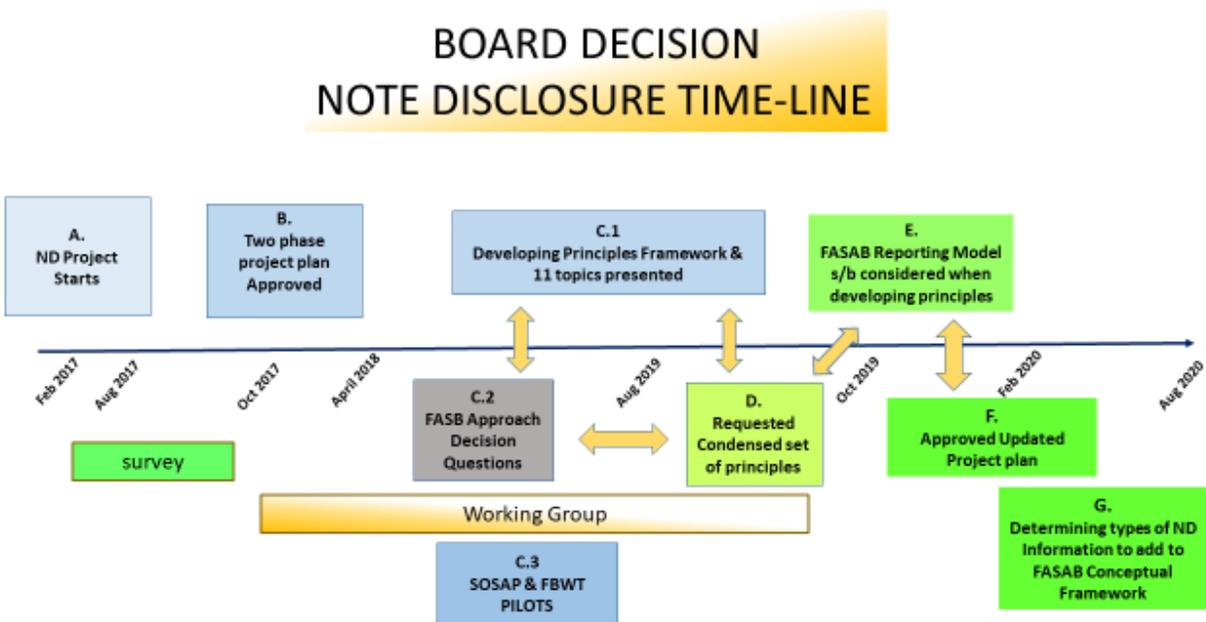
¹ The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

DEVELOPMENT PHASE

The project is currently developing concepts – types of information appropriate for note disclosures – to add to the conceptual framework.

BACKGROUND

At the **June 2020** meeting, some members wanted to understand how the current approach to developing proposed note disclosure concepts mapped to the previous work done. This section will provide an overview of the timeline of Board decisions that led to the current approach.



- A. In **February 2017**, the Board approved the ND project and requested a survey that was sent to stakeholders.
- B. At the **October 2017** meeting,

1. The Board reviewed the survey results:

Summarized from the meeting notes – on the [project page](#):

On August 31, 2017, FASAB initiated an online note disclosure survey. The survey results confirmed the need to improve disclosures and targeted areas for improvement. Most respondents agreed that providing principle guidance would give flexibility to the agency while adhering to the objectives and increasing consistency. The respondents stated that the causes of note disclosure issues vary. These could

be due to compliance with Circular A-136, input from the Certificate of Excellence in Accountability Reporting reviewers, or the auditor's requirements (which are more rigorous than those required by FASAB).

2. The Board provided suggestions on the following topics:

Summarized from the meeting notes – on the [project page](#):

- Audiences of the future note disclosure principles – While it is critical to identify the primary users of both the component reporting entities' financial reports and the consolidated financial report of the U.S. Government, it might be more relevant to make the note disclosures appealing to different groups. As identified in Statement of Federal Financial Accounting Concepts (SFFAC) 1, *Objectives of Federal Financial Reporting*, both internal and external users will be considered in the project: citizens, Congress, federal executives, and federal program managers. Instead of defining the primary users, this project will utilize the objectives defined in SFFAC 1 as guidance to develop the note disclosure principles. SFFAC 1 summarizes the objectives as such: "The objectives are designed to guide the Board in developing accounting standards to enhance the financial information reported by the federal government to (1) demonstrate its accountability, (2) provide useful information, and (3) help internal users of financial information improve the government's management.
- Principle-based framework with a concentration on providing relevant information – If an entity engages in the type of activity required by a note, and amounts involved are material, then the entity should present the information in the note. Disclosure should not be optional.
- Judgment – Materiality should be described in both qualitative and quantitative terms, and it should be evaluated at the component level.
- Improve clarity, consistency, and comparability – Taking a two-tiered approach to setting standards would not be particularly helpful. There are pros and cons for providing illustrations and/or a checklist. Principles addressing readability would help the clarity and increase consistency of the note disclosures.

3. The Board approved the two phased project plan:

Summarized from the meeting notes – on the [project page](#):

- Phase I – Identify and develop a set of principles for disclosure to be used by the Board to reduce repetition and improve relevance and consistency in note disclosure.

- Phase II – Use the principles to modify the existing note disclosure requirements for component reporting entities to improve the disclosures' usefulness and effectiveness.

C. At the **April 2018** meeting, the Board approved a focus on the FASB note disclosures model that included decision questions based on the March 4, 2014, FASB issued exposure draft (ED), *Proposed Statement of Financial Accounting Concepts, Conceptual Framework for Financial Reporting, Chapter 8: Notes to Financial Statements*.

Research Phase: from **April 2018 to August 2019**, staff and working group mapped the 19 FASB decision questions to topics and presented separate principles in a draft concept statement.

D. At the **August 2019** Board meeting, staff and working group presented 11 topics for note disclosures (ND) based on the FASB decision questions and the draft principles concept document.

Per the meeting notes: The **Board generally agreed** with the proposed decision questions and the method to categorize by topic

E. At the **October 2019** meeting, the Board reviewed the updated note disclosures principles outline.

Per the meeting minutes,

- the Board discussed condensing the principles to a few core principles. The Board noted that the principles should not be tied to any one topic.
- The Board noted that the reporting model should be considered when developing the principles, including the relationship between the financial statements and the note disclosures.
- The Board agreed to continue reviewing the core principles. Staff will research and provide recommendations for the remaining core principles.

F. At the **December 2019** Board meeting, staff presented the reporting model collaboration education session.

G. At the **February 2020** Board meeting, staff presented an updated project plan. Phase I would now focus only on developing concepts based on the FASAB reporting model, rather than concurrently developing concepts and a set of decision questions based on the Financial Accounting Standards Board (FASB) ND model.² The approach reaffirmed the Board's October 2019 request to consider the FASAB

² FASAB February 26-27, 2020 minutes.

reporting model. Appendix I: Reporting Model Comparison discusses differences between the FASAB and FASB reporting models.

Members approved the updated project plan at the **February 2020** Board Meeting and the following is a comparison of the original to updated project plan.

COMPARING ORIGINAL PROJECT PLAN TO UPDATED PROJECT PLAN		
Phase	Original Project Plan Approved Oct 2017	Updated Project Plan Approved February 2020
1	Phase I consists of identifying and developing a set of principles for disclosure to be used by the Board and preparers to reduce repetition and improve relevance and consistency in note disclosure.	Phase I. Develop the Note Disclosures Conceptual Framework Statement from existing note disclosures concepts to guide the Board in reexamining existing standards and developing accounting and financial reporting in the future.
2	Phase II consists of using the principles to modify the existing note disclosure requirements for component reporting entities to improve the disclosures' usefulness and effectiveness.	Phase II. Evaluate existing note disclosures to identify opportunities for improving financial reporting. This phase will be conducted as part of the Reexamination of Existing Standards project and a technical plan for the project will be developed at that time. The project will also use the Note Disclosures Conceptual Framework developed during Phase I to coordinate with the Budget Information Improvement project to improve the usefulness of budgetary information.

H. **March – June 2020:** In response to the **February 2020** Board decision, Staff prepared a draft outline for a draft exposure draft (ED) to present at the April 2020 meeting. Then along came the COVID-19 pandemic and the Note Disclosures project was not schedule for the April 2020 meeting. However, staff sent the draft ND outline to members for comments to maintain momentum with the ND project. Staff incorporated member comments on the draft outline into a draft ED and presented it at the **June 2020** meeting for pre-ballot. The Board requested that staff discuss the rationale for the types of information note disclosures should provide before a pre-ballot could be considered.

This concludes the Background section and review of Board decisions made for the last three years that led to the current approach.

STAFF ANALYSIS AND RECOMMENDATION

To complete the conceptual framework and codify the concepts for note disclosures, the Board will first need to determine the types of information appropriate for ND. The following is an analysis and recommendation for the types of information appropriate for ND to complete the conceptual framework.

During the June 2020 meeting, staff focused on the role of note disclosures in assisting users in understanding financial statement line items and proposed the following types of information that note disclosures may present:

- a. descriptions of accounting policies underlying amounts recognized in financial statements
- b. disaggregations of financial statement line items into the unique accounts included in the line item total
- c. descriptions about the nature of any material gains or losses
- d. descriptions of methods and assumptions used to prepare estimates

However, members suggested that staff discuss the basis for the types of information and some members noted the possibility that other types of information may be appropriate. Staff accordingly reconsidered the different types of information by conducting the following steps:

- a. examining the reporting objectives and users' needs for information discussed in SFFAC 1, *Federal Financial Reporting Objectives*
- b. reviewing the form and limitations of the face of financial statements in presenting information
- c. reviewing the form of possible note disclosure presentations, such as narrative, graph, table, or combinations thereof
- d. identifying items of information that may be appropriate for presentation in note disclosures

As a result, staff proposes the following broad types of information note disclosures may present:

1. supporting information for financial statement line items
2. context or background information regarding the reporting entity
3. past events, current conditions, and circumstances that have not been recognized but can affect an entity's resources

These types of information are broader than the earlier proposal to allow the Board more flexibility in developing note disclosure standards. In addition, considering the reporting objectives, they include more of the items of information users may need. For instance, the *supporting information* category alone encompasses the four groups of information staff initially proposed in paragraph 6 of the June draft exposure draft and provides the type of information to help users compare financial information among

reporting entities and prior periods. The following section discusses each of the new proposed broad types of information note disclosures may present.

New Proposed Types of Information Note Disclosures May Present

Financial statements assist users in assessing the reporting entity's budgetary integrity, operating performance, and stewardship. Financial statement line items include descriptions and amounts to assist users in their assessment; however, the descriptions and amounts may not provide users with enough information. Note disclosures provide information to assist users in understanding the financial statement line items and assessing the entity, including information to help users understand the impact of transactions, events, and conditions and underlying phenomenon or significant risk and uncertainties. For instance, to help users assess the entity's operating performance, users need information on the entity's assets and liabilities related to operations, such as the quantity, location, age, and condition of inventories and the condition of facilities.³

To assist users in understanding the entity's financial statements and assessing the entity's budgetary integrity, operating performance, and stewardship, note disclosures may provide the following types of information:

- a. **Supporting information for financial statement line items** - For example, note disclosures may provide disaggregation and reconciliations of items; descriptions of the nature, terms, or quality of the items; nature of a gain or loss; and/or methods and assumptions used.

Financial statements include many measurements that involve assumptions.⁴ Note disclosures may provide explanations to help users understand the uncertainties inherent in the measurements. In addition, to make assessments such as the operating performance of an entity, users may seek to compare the reporting entity's activities with other entities⁵ or with previous periods. Note disclosures may provide definitions, information on the components of a line item, and accounting methods to assist users in making comparisons.

Also, in assessing budgetary integrity and operating performance, users seek to understand the relationship among financial statement items, such as how budgetary outlays finance the net cost of operations and affect the assets and liabilities of the reporting entity. Note disclosures may accordingly provide reconciliations to help users understand such relationships.

- b. **Context or background information regarding the reporting entity** - Users are concerned about the government's goals, objectives, and policies.⁶ In

³ SFFAC 1, par. 97.

⁴ SFFAS 17, par. 28.

⁵ SFFAC 1, par. 93.

⁶ SFFAC 1.

assessing an entity's budgetary integrity, operating performance, and stewardship, users need to understand the entity's mission and activities. Note disclosures may provide information regarding the entity's nature, services, and any special restrictions or privileges that apply to line items. This information could help users assess the potential effect of financial statement line items on an entity's future financial position, condition, and performance.

The Board has noted that required supplementary information (RSI) may provide context or background type information regarding the reporting entity⁷ and providing similar information in notes might appear redundant. However, financial statements and note disclosures provide basic information needed for users to assess the budgetary integrity, operating performance, and stewardship of the entity. Users may consider RSI to obtain additional information regarding the entity and enhance their understanding.

- c. **Past events, current conditions, and circumstances that have not been recognized but can affect an entity's resources** - Users want help in assessing the likelihood that the government will continue to provide the current level of benefits and services to constituent groups, such as farmers, retirees, and the poor.⁸ The effects of some conditions and circumstances may not be recognized because they do not meet the basic recognition criteria; for example, existing or potential litigation, or dependency on another entity for continuing operation. Note disclosures provide this information to assist users in assessing the reporting entity's stewardship.

BOARD QUESTIONS

Do the types of information proposed in paragraphs a. through c. cover the information users would need in note disclosures? If not, what additional information should be considered?

NEXT STEPS

Staff will incorporate the approved types of information for note disclosures into a draft ED for Board deliberation to complete ND phase I.

⁷ SFFAC 2, par. 69.

⁸ SFFAC 1, par. 140.

MEMBER FEEDBACK

If you have any questions or comments, please email Mr. Simms at simmsr@fasab.gov and Ms. Gilliam gilliamr@fasab.gov, with a cc to Ms. Valentine at valentinem@fasab.gov, by August 19, 2020.

Appendix I: Reporting Model Comparison

During the October 2019 meeting, the Board noted the need to consider the federal reporting model and that staff should develop broad note disclosure concepts. To demonstrate the broad scope of the federal model and, consequently, the broad scope of information the Board might consider for note disclosures, the following analyses compares the FASAB reporting objectives to the FASB reporting objectives:

1. **Analysis Table:** *Highlights of Differences in the FASAB and FASB Reporting Objectives*; and
2. **Analysis:** *Discussion on the Differences in the FASAB and FASB Reporting Objectives*

1. ANALYSIS TABLE: Highlights of Differences in FASAB and FASB Reporting Objectives			
#	FASAB & FASB Reporting Objectives	Main Points	References
a	Objectives of Federal Financial Reporting	<p>The role, users, and accounting for federal financial reporting are unique because:</p> <ul style="list-style-type: none"> • FASAB considers internal and external users concerned about government efficiency & effectiveness • Users expect federal entities to demonstrate special accountability for their activities⁹ 	SFFAC 1, pars 23-27
b	FASB Objective of General Purpose Financial Reporting	FASB considers external users, such as potential investors, lenders, and other creditors	Statement of Financial Accounting Concepts No. 8; <i>Conceptual Framework for Financial Reporting</i> , Chapter 1 & 8

⁹ See SFFAS 27, *Identifying and Reporting Earmarked Funds*

2. ANALYSIS – Discussion on the Differences in the FASAB and FASB Reporting Objectives

Reporting objectives reflect the information needs of users and users of federal financial reports seek information for different purposes than users of the model FASB discusses. To highlight the broad scope of information that the Board might consider for federal note disclosures, the following analysis provides an overview of 1) FASAB's objectives of federal financial reporting; and 2) FASB's objectives of general purpose financial reporting.

a. Objectives of Federal Financial Reporting

The following is a review of SFFAC 1, *Objectives of Federal Financial Reporting*. SFFAC 1 discusses the budgetary integrity, operating performance, stewardship, and systems and control reporting objectives. The Board derived these objectives from studying the information needs of both internal and external users, a key distinction from the objectives of other accounting standards-setters. In particular, SFFAC 1, paragraphs 23 to 27, note that the reporting objectives are different from those of FASB and GASB because FASAB's information needs consider both internal and external users, while FASB and GASB consider the information needs for only external users.

23. The FASAB and its sponsors believe that any description of federal financial reporting objectives should consider the needs of both internal and external report users and the decisions they make. This implies a different role for the FASAB than for the Financial Accounting Standards Board (FASB) and the Governmental Accounting Standards Board (GASB). The FASB sets financial reporting standards for privately owned entities in the United States. The GASB sets financial reporting standards for state and local governments.

24. Those Boards exist primarily to set standards for general purpose financial reporting to external users of financial reports. This is because those users, by definition, have limited ability to control the nature of the information made available to them. The FASB and the GASB do not need to weigh heavily managers' information needs because those individuals, by definition, are assumed to have ready access to the information they need about the financial transactions and events that affect the financial position, operations, and financial condition of the entities they manage.

25. The FASAB, on the other hand, considers the information needs of both internal and external users. In part, this is because the distinction between internal and external users is in many ways less significant for the federal government than for other entities. Officials who in theory should have ready access to information often find in practice that it is not available. Factors that contribute to this problem include the size and complexity of the government, the rapid turnover among senior political executives compared with the time required to install information

systems in large bureaucracies, and the division of authority in the federal government.

26. The FASAB's dual concern, with both internal and external reporting, is the result of such factors and of the Board's mandate. The FASAB was created to advise OMB and Treasury (agents of the President) and the GAO (an agent of the Congress) on accounting standards for federal agencies and programs in order to improve financial reporting practices.

27. The Board's sponsors have separate constitutional and statutory authorities for setting accounting policy for the government. The division of powers in the U.S. government means that different policymakers with independent authority find it useful to have a mechanism to coordinate their accounting policy activities. The Board and its public deliberative process also provide a new arena for the participants to deliberate and to discover how federal accounting and financial reporting can be improved.

The following presents an example of a unique federal note disclosure as required by Statement of Federal Financial Accounting Standards (SFFAS) 27, *Identifying and Reporting Earmarked Funds*. The Board developed SFFAS 27 to provide special accountability—in support of the stewardship reporting objective.

53. Although the Federal Government does not have a fiduciary relationship (as defined by the proposed standard, *Accounting for Fiduciary Activities*) with the potential beneficiaries of earmarked funds, the unique nature of earmarked funds necessitates additional explanation and disclosure in the basic financial statements. In SFFAS 7, *Accounting for Revenue and Other Financing Sources*, special accountability reporting provisions were applied to all “dedicated collections” regardless of whether or not they involved Government-owned funds or private funds. The concept of special accountability applies to earmarked funds.

54. All earmarked funds have characteristics that justify special accountability. While many Government programs raise implied commitments for the future, there is a more explicit commitment associated with the statutory establishment of earmarked funds. The Government raises an expectation on the part of the public that the Government will use the amounts collected from specific sources and accumulated in earmarked funds for their stated purpose. There is often a direct link between the source of fund revenues and designated activities, benefits or purposes in an effort to charge beneficiaries or users for benefits received. Resource inflow is accounted for separately from general tax receipts, allowing the program's status to be more easily examined. Many earmarked funds receive permanent appropriations in an amount equal to these inflows that become available without recurrent action by Congress through annual appropriations.

55. Earmarked funds are of interest to a universe of contributors, taxpayers and recipients, who have an expectation that earmarked revenues will be used for the purposes specified in the law authorizing the collection of the revenues. For example, current contributors to Social Security programs may assume that their earmarked taxes in excess of payments to current recipients will be available to fund future social security benefits. The likelihood of the public making this assumption may reasonably be expected when the Federal Government issues projections of the availability of accumulated balances for future payments.

These concepts provide evidence that the FASAB reporting model is appropriate for developing types of information for federal note disclosures because **FASAB serves the needs of both internal and external users.**

b. FASB Objective of General Purpose Financial Reporting

The following is a review of FASB's ND concepts concerning the users they serve. FASB notes that its financial information should help **external users** make decisions about investing, not the state of

Statement of Financial Accounting Concepts No. 8 As Amended Conceptual Framework for Financial Reporting Chapter 1, The Objective of General Purpose Financial Reporting

QB1. The objective of general purpose financial reporting [footnote omitted] is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to the entity. Those decisions involve buying, selling, or holding equity and debt instruments and providing or settling loans and other forms of credit; and

FASB: Statement of Financial Accounting Concepts No. 8 - Conceptual Framework for Financial Reporting Chapter 8, Notes to Financial Statements

D4. The primary purpose of notes to financial statements is to supplement or further explain the information on the face of financial statements by providing financial information relevant to existing and potential investors, lenders, and other creditors for making decisions about providing resources to an entity.

These FASB concepts provide evidence that FASAB's reporting model is appropriate for developing types of information for federal note disclosures because the FASB ND model only focuses on providing information to investors and creditors.

Based on the review and analysis presented above, staff determined that the FASAB reporting model was the most appropriate model for recommending types of information for federal note disclosures. As a result, staff developed an updated project plan to streamline phase 1 to focus only on developing concepts using the FASAB reporting model.