

Addendum #4 Memo Leases

February 16, 2023

To: Members of the Board
From: Ricky A. Perry, Jr., Senior Analyst
Thru: Monica R. Valentine, Executive Director
Subject: **Letter from David Horn, Health & Human Services** (Topic E addendum #4)

On February 15, 2023, the Chairman received the enclosed letter from the Department of Health and Human Services (HHS or “the Department”). Staff requests that members carefully study this cover memo and the enclosed letter.

The enclosed letter does not affect the implementation themes, observations, and conclusions reached by staff under Topic E. HHS was not among the eight CFO Act reporting entities interviewed by staff, as discussed in the methodology section of Topic E. However, the implementation activities, themes, and staff observations in Topic E are generally consistent with the matters raised by HHS in the enclosed letter. Staff did not propose any tentative Board decisions or recommendations for reasons discussed under Topic E. Staff hereby reaffirms this position.

Staff analysis of the enclosed letter:

1. Statement 54, *Leases*, was issued in April 2018 after extensive due process and deliberations. The Statement received unanimous Board approval. HHS commented on the exposure draft (ED) and concurred with the accounting, disclosure, and transition proposals therein (see [p. 1-5 of comment letter, Q1-11](#)).¹ As part of the due process, the Board duly considered comments from all interested parties, including those that expressed alternative views and disagreements with the proposals within the ED.
2. Statement 58, *Deferral of the Effective Date of SFFAS 54, Leases*, was issued in June 2020 after extensive due process and deliberations. The Statement received unanimous Board approval. As part of the due process, the Board duly considered ED comments that expressed alternative views. HHS submitted a comment letter concurring with a proposed two-year deferral and stating that “the proposed two-year deferral will provide sufficient time for a successful implementation” (see [p. 1 of comment letter](#)).
3. Board post-issuance actions, such as implementation guidance, clarifying amendments, and other guidance, are not a basis to delay implementing

¹ HHS suggested one additional year in response to Q12.

significant changes in generally accepted accounting principles. The Board's post-issuance project activities did not alter the requirements of Statement 54 or delay implementation activities. Rather, they modestly reduced implementation burden. HHS suggested that FASAB "allow more time to re-evaluate the standard and to coordinate with stakeholders to identify the comprehensive set of revisions to avoid the need for continued amendments." The Board has already completed these tasks.

4. The Department summarized several management challenges in the enclosed letter. These are consistent with the management challenges and themes summarized by staff under Topic E related to organizational change management, project management, and systems.
5. Management is responsible for implementing significant changes in accounting principles in accordance with transition requirements and the effective date of the Board's final pronouncements. This entails project management and modifications to systems and controls. The Board duly considered the costs and challenges of the standard. See SFFAS 54 paragraphs A23-A27, A33, A36, and A38-A41 for examples.

Closing staff remark:

The federal financial reporting objectives are "a framework for assessing the existing financial reporting systems of the federal government and for considering how new accounting standards might help to enhance accountability and decision-making in a cost-effective manner."² Topic E and the management challenges discussed in the enclosed letter highlight the anticipated benefits of Statement 54 and its expected contributions to the federal financial reporting objectives when the Statement becomes effective in fiscal year 2024.

Enclosure

² Statement of Federal Financial Accounting Concepts 1.



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of the Secretary

 Office of the Assistant Secretary for
 Financial Resources
 Washington, D.C. 20201

Mr. George A. Scott
 Chairman
 Federal Accounting Standards Advisory Board
 441 G. Street, NW, Suite 1155
 Washington, DC 20548

Dear Chairman Scott:

The Department of Health and Human Services (HHS) presents this letter to the Federal Accounting Standards Advisory Board (FASAB) to share significant concerns and implementation challenges we encountered during our efforts to comply with requirements of the Statement of Federal Financial Accounting Standards 54 (SFFAS 54), *Leases*. HHS respectfully requests FASAB to consider delaying the implementation deadline of SFFAS 54 requirements until fiscal year (FY) 2028.

HHS is committed to sound internal controls, effective and responsible financial management, and transparent financial reporting, proven through 24 consecutive unmodified audit opinions on its financial statements. We evaluated our internal controls and financial management systems and we identified several challenges in our leases implementation activities that would significantly disrupt our current financial, operational, and information technology business processes (e.g., HHS participation in government-wide initiatives such as G-Invoicing and COVID-19 response activities). Through this assessment, HHS concluded it will not be able to comply with SFFAS 54's effective implementation deadline of FY 2024, as summarized below:

- I. **Substantial Changes in Accounting and Operational Processes:** SFFAS 54 requirements include complex accounting changes with cross-agency and cross-entity impacts on financial, budgetary, programmatic, and operational business processes.
 - a. Policy Development – Policy development demands extensive collaboration among a wide range of stakeholders, including financial and accounting management, operational administration, information technology personnel, and real property and procurement subject matter experts (SME). SFFAS 54 implementation activities have significantly multiplied these demands. Additionally, inconsistent leases guidance between FASAB and the Office of Management and Budget (OMB) makes it difficult to efficiently develop leases-related departmental policies, hindering our efforts to prepare for the FY 2024 implementation deadline.
 - b. Real Property Offices – Current real property and logistics business processes require significant updates to identify, assess, record, and maintain new lease agreements and/or arrangement records to comply with new lease types in accordance with SFFAS 54.

- c. Office of Acquisitions – Procurement SMEs follow Federal Acquisition Regulations to establish contracts and/or agreements; Contracting Officers are generally not familiar with financial reporting standards. As a result, procurement SMEs require substantial training to understand new lease definitions/terminology and properly identify contracts and/or agreements in accordance with SFFAS 54 terminology. Similarly, accounting SMEs are generally unfamiliar with acquisition regulations and must dedicate significant effort to understand the different lease types and new definitions. This understanding is further hindered by inconsistencies between FASAB and OMB lease guidance. A particularly challenging activity is identifying ‘embedded leases,’ which requires substantial manual effort to review ‘all existing’ procurement documentation, some of which spans hundreds of pages per contract and/or agreement. Authoritative bodies have not provided specific guidance on identifying embedded leases, and the activity is further confused by potential contradictions between legal definitions and terminology used by procurement SMEs. HHS has considered employing artificial intelligence for this activity, but additional funding will be required.

- II. **Adverse Impact on Effective Corrective Actions:** HHS has made significant progress to remediate audit deficiencies related to the high volume of financial adjustments. HHS has automated financial reporting processes, developed corrective action plans, updated current business practices, completed extensive data clean-up efforts to eliminate unnecessary entries, and published a Department-wide Financial Adjustments policy. SFFAS 54 will require significant manual financial adjustments to comply with leases accounting and reporting requirements; those adjustments will be based on complex and incomplete accounting scenarios (Fiscal Service is currently updating USSGL scenarios). Implementation of the standard will adversely impact HHS’ remediation efforts by significantly increasing the volume of financial adjustments and the severity of financial audit findings.
- III. **Untimely Guidance Further Delayed by Ongoing Updates to the Standard:** FASAB continues to develop an Omnibus amendment to SFFAS 54 requirements, while the Fiscal Service Leases Working Group continues updating guidance to accommodate complex accounting scenarios. The lack of timely final guidance hinders HHS’ ability to fully update its financial and IT system processes to successfully comply with SFFAS 54 requirements by FY 2024. Finance personnel must effectively prepare and train to implement SFFAS 54 requirements and to accurately record transactions; however, the Department faces an abbreviated training timeline once final guidance is eventually published. The untimely issuance of guidance also extends to OMB’s Financial Reporting Requirements (Circular A-136) for FY 2024, which all agencies need for the presentation of financial statements and notes disclosures. The collective lack of timely guidance is hindering HHS’ ability to effectively plan a successful implementation of SFFAS 54 requirements. HHS believes additional time would also benefit FASAB by allowing more time to re-evaluate the standard and to coordinate with stakeholders to identify the comprehensive set of revisions (Omnibus amendment) to avoid the need for continued amendments. HHS encourages the development of an implementation government-wide working group that focuses on resolving challenges, providing comprehensive criteria over

various operational, internal control, information system configuration, and programmatic business processes that are broader in scope, not just concentrating on financial accounting impacts. Similar approaches have proven successful through the implementation of working groups that focused on Heritage Asset, Stewardship Land, and DATA Act.

- IV. **IT Systems Implementation:** The complexities of SFFAS 54 require automated processes, internal controls, and data interfacing to properly comply. For example, this standard requires updates to feeder systems, financial reporting systems, managerial reporting modules, existing lease databases, and other internal and external reporting processes. These system and process modifications cannot be initiated until SFFAS 54 guidance is complete, clear, and finalized in time to give each impacted process area time to assess, plan, develop, test, and deploy changes.

Similar to other Federal agencies, HHS requires reasonable time and resources to assess, evaluate, and determine the necessary changes across three instances of the Department's core financial management system. This includes additional funding for proper mitigation and testing strategies to ensure IT system updates are implemented and working properly.

As a result of the delayed federal guidance, HHS's ability to fully verify the functionality of IT system updates is severely impacted, which prevents proper and timely IT deployment.

- V. **HHS Limited Resources – Response to High-Priority Mission Operations:** Like other federal agencies, HHS must prioritize our limited resources to support mission-critical activities. In recent years, HHS has received significant supplemental funding to support the on-going HHS response efforts:

COVID-19 Response – HHS is the federal agency leading the COVID-19 pandemic response, through various legislative and authoritative laws such as the CARES Act and *American Rescue Plan Act of 2021*. As a result, HHS received substantial supplemental funding to properly respond to individual, families, and businesses affected by COVID-19, including funding that required extensive oversight by regulatory agencies.

Unaccompanied Children (UC) – HHS responded to challenges presented by the historically high number of UC referrals as children arrived at the southern U.S. border. HHS significantly expanded its presence by standing up emergency intake sites around the country to manage the UC influx. As a result, HHS expended substantial resources to ensure the safety, security, and welfare of UCs.

Refugees – Similar to the UC effort, HHS devoted significant resources to help refugees from Afghanistan and other countries integrate into new communities and adjust to life in the U.S. through HHS-funded support services. These diverse services enable refugees to learn English, find jobs, and start the process towards citizenship.

Emergency and Disaster Response – HHS continuously responds to both natural disasters (e.g., hurricanes, fires) and emergency response activities (e.g., COVID-19,

monkeypox). HHS spends significant funding and resources to help individuals and communities suffering from natural disasters, including evacuation activities. Additionally, HHS spends significant time responding to healthcare misinformation, connecting people to care, and training health care workers and communities to better prepare for future health emergencies.

HHS sincerely appreciates FASAB's consideration of our request to delay implementation of SFFAS 54 requirements until FY 2028. If you have any questions or need clarification on this request, please contact David Horn, Director of the Office of Financial Policy and Reporting, at David.Horn@hhs.gov or (202) 697-3631. We look forward to hearing from you soon.

Respectfully,

David C.
Horn -S

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David C. Horn -S
Date: 2023.02.15
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David C. Horn
Director
Office of Financial Policy and Reporting

Cc: Acting Controller, Office of Management and Budget
Assistant Secretary for Management and Chief Financial Officer, Department of Veterans Affairs
Deputy Chief Financial Officer (CFO), Department of Energy
Comptroller, Department of State
Principal Deputy Assistant Secretary exercising the Delegated Authorities of the Assistant Secretary and CFO, Department of Interior
Executive Director, FASAB
Commissioner of the Bureau of the Fiscal Service, Department of the Treasury