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Question #1 – What attribute should be measured for social insurance? **Staff recommends present value.** The objective regarding the measurement attribute for social insurance should be the same as FASB's "fair value." Fair value is essentially market value but "for some assets and liabilities, management's estimates may be the only available information." Present value is a component of FASB's fair value hierarchy. Moreover, present value is required in various current FASAB standards that require long-range projections, including SFFAS 5 (for pension, retirement healthcare, insurance, and other liabilities), SFFAS 17, and others. Also, the Social Security Trustees use present value extensively in their Annual Report.	The members agreed with the recommendation.	No disagreement was expressed.
Question #2 – Should OASDI and Medicare liabilities include projected amounts in excess of the current statutory limit? Staff recommends including the full cost and full liability to the participants. The probability that the Government would ignore the shortfall and then default on a large percentage of the benefits is remote. [*Staff Note: Regarding this issue, staff notes two points. First, the cap involves the open group projection, which, as the Board is well aware, includes all participants and all revenue and cost over 75 years. It is a different measure than the liability the staff recommended, which measures the gross cost of benefits for a specific, limited population group. No taxes to be paid in the future or benefits to be credited in the future would be included in the liability. Assets (i.e., Treasury securities), which represent accumulated excess revenue received as of the reporting date, would be accounted for separately under the proposal.* *Secondly, this appears to be a "funding" issue, and the*	Messrs. Patton, Schumacher, Reid, and Mosso, and Ms. Cohen agreed with the staff recommendation, with the statutory limitation reported either on the face of the financial statements or in a footnote. <u>Some of the rationales expressed</u>: Mr. Reid said that a computation that was limited to statutory provision would be incomplete. Ms. Cohen said that current law does not limit the benefits per se. The projection shows a shortfall, but the projection is based on assumptions and estimates and may be change. Current law merely makes it a self-financing program.	Three members disagree with recommendation (GAO, OMB, CBO). One member (Mr. Farrell) was concerned about what he viewed as inconsistent application of the current law notion, but he did not express a position. <u>Some of the rationales expressed</u>: Mr. Torregrosa said that since the Board is using current law as the basis for liability decisions and current law specifies that funding is cut off, the projection should be based on what is available. Mr. Dacey said that amounts should not be projected in excess of the statutory limit. Although accruing liabilities for other unfunded programs is appropriate, these programs are unique because of the public

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Board has said that funding should not affect liability recognition. *Also, the cap would affect the Medicare liability sooner than the Social Security. The statutory provisions for Medicare will be inefficient to pay 100 percent of HI claims (SMI, Part B, re doctor bills has access to the General Fund and therefore has no such "cap") will arrive much sooner than for Social Security.]*		communication that full benefits will not be paid in the future. However, the full exposure or responsibility for the federal government should be communicated in the SOSI.
Question #3 – What assumptions should be used in projecting cash flow? **The staff recommends a general requirement as in SFFAS 5 with a reference to actuarial standards of practice.** The recommendation is a pragmatic approach to this very difficult subject and has been effective for past FASAB standards. Also, from a cost-benefit perspective, one might question not availing of the current process.	The members agreed with the recommendation.	No disagreement was expressed.
Question #4 – How should uncertainty be illustrated? In addition to the recommendations below regarding display, disclosure and RSI, the staff recommends exploring the use of "expected present value" as an alternative to present value based on the "best estimate." The expected cash flow approach accommodates the use of present value techniques when the timing of cash flows is uncertain. The expected cash flow approach focuses on explicit assumptions about the range of possible estimated cash flows and their respective probabilities. The "best estimate" approach is well known and perhaps even "generally accepted" with respect to Social Security and Medicare, and yet the EPV approach is gaining is	The members agreed with the recommendation and decided that the exploration would be part of the measurement project or at least not part of the Social Insurance Liability Project.	No disagreement was expressed.

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acceptance in the private sector and is worth exploring for social insurance.		
Question #5 – What should be recognized as social insurance "expense" or "cost"? **The staff recommends four components.** For OASDI and HI the four components of cost describe above – "service cost," interest on the liability, actuarial gains and losses, and prior service cost – are consistent with the benefit promise expressed for OASDI and HI as a given amount per year of work in covered employment as well as the changes therein in subsequent periods. For SMI staff recommends the insurance accounting provided in SFFAS 5 and FAS 60. The staff recommends that SMI be characterized as short-term health insurance because it has the short-term characteristics discussed in FAS 60, e.g., SMI provides insurance protection for a fixed period, and the Government may adjust the provisions of coverage at the end of any coverage period. The cost of SMI would be the all claims incurred during the period, including, when appropriate, those not yet reported and contingencies that meet the criteria for recognition; and a provision for premium deficiency, if any. As short-duration insurance SMI is not likely to have premium deficiency. The SMI would involve a shorter-range estimate than Social Security and HI, but where longer-range estimates were necessary, present value would be appropriate. In the case SMI cost would include components like those measure for OASDI and HI, i.e., present value, interest on the obligation, actuarial gains and losses.	A majority of the Board agreed with the recommendation.	No disagreement was expressed but Mr. Patton raised an issue regarding what the cost or expense would be for. He noted that the staff memo, on page 1, notes that a majority of the Board tentatively decided that the obligating event for Social Security and Medicare Hospital Insurance (HI) occurs when participants meet the 40-quarters of work in covered employment (or equivalent) condition. On page 2, the memo says that a key component of cost is the present value of future outflows attributable to obligating events occurring in the reporting period. He said these two statements did not appear to work together, unless work in covered employment after 40 quarters is also an obligating event. He asked what the obligation occurring at 40 quarters is for? He suggested it was for the present value of the full amount due when the participant retires rather than only the amount credited to the participant at 40 quarters, plus the annual increments after that, based on work covered employment to the reporting date. He said the subsequent increments were being treated as if an earnings process was taking place, which he disagreed with. But if the latter is the Board's position, then the subsequent work in covered employment was also an obligating

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		event. Mr. Dacey said he also saw a comparison issue between the staff recommendation for measuring Social Security as an incremental cost versus the SMI approach. He said future revenue should be included because it is a realistic assumption that participants will be paying the premium when they are getting the benefits. He said he did not know why that was not being recommended for Social Security as well. Mr. Torregrosa said that CBO does not distinguish between Social Security and Medicare Hospital Insurance, Part A, on the one hand and Medicare SMI, Part B, on the other. Thus, CBO would reject the insurance accounting approach for SMI, Part B, and in particular would not count any future premium income in the estimate because that would not be done for Social Security. He said CBO favors accelerating the recognition point for SMI to 40 quarters.
Question #6 – What should be recognized as the social insurance liability? **The staff recommends that liability be the accumulated cost.** Accrued costs and liabilities for social insurance would exclude costs attributable to obligating events occurring in the future.	Chairman Mosso polled the Board. A majority agreed with the staff recommendation that the liability is the accumulated cost.	No disagreement was expressed regarding the notion that the liability should be the accumulated cost. Mr. Patton raised an issue discussed in Question #5 above. Mr. Zavada said that the staff paper had only been available for a short period of time and he had not had time to consult with SSA or HHS on the different questions, which he wanted to do

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		before weighing-in.
Question #7 – What should be displayed for social insurance on the statement of net cost, balance sheet, and other statements? **October 5, 2005 –** <u>Staff Display Recommendations</u> ***Balance Sheet*** Staff recommended a single liability line item for the balance sheet that references a revised SOSI. ***Statement of Net Cost*** Staff recommended that service cost and interest on the obligation be displayed as separate components of "operating cost;" and actuarial gains or losses and prior service costs, if any, presented as a separate component after operating cost, but as part of the total cost on the SNC. ***Statement of Changes in Net Position*** Staff did not recommend any changes to the statement of changes in net position display. ***Statement of Social Insurance*** Staff recommended retaining and revising the SOSI to display an amount reported as the liability amount on the balance sheet and other new subtotals.	**August 18, 2005 —** The Board did not have an opportunity to address this question at this time. However, Mr. Reid suggested a separate presentation for actuarial gains and losses for social insurance and all other programs where they are significant. He said he has a very strong preference for not commingling operating expenses with changes actuarial assumptions and for finding some place other than the statement of net cost to put the effects of changes in assumptions. Mr. Reid said his goal is to display the components of a change in the liability rather than aggregating it in one number. This would highlight, for example, frequent changes in assumptions that have little economic justification. He said he wants to avoid having hundred billion(s) dollar swings affecting the statement of net cost. He prefers that the latter display the cost of running the government for a year. Mr. Reid said there would be several choices for displaying actuarial gains and losses when they arise. He suggested, for example, that they could be capitalized and amortized; or, they could be booked directly to a statement that displays these effects, which could be closed to net position; or they could be displayed as a line item on the statement of changes in net position so that, in effect, they do not hit the operating cost in the year the changes in assumptions occur. He said that changing the bottom line on this statement to "operating cost" would be a possibility. Chairman Mosso said he preferred that actuarial gains and losses not be reported directly to net	

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	position. They ought to flow through a statement. **October 5, 2005 –** Board agreed with the staff recommendations.	
Question #8 – What should be disclosed about social insurance in the notes? **The Board did not have an opportunity to address this issue at the August 18, 2005 meeting.** **October 5, 2005 –** Staff recommended the following be disclosed in the **notes**: • Actuarial present value of benefits accrued by participants with less than 40 quarters of work in covered employment. • The amount of future outlays in excess of future resources over 75 year for the open group. • Components of the change in the liability account, and • Assumptions. Staff recommended the following for **RSI:** The staff recommended retaining the current RSI except for the sensitivity example. Staff recommended a stochastic simulation to be designed with the assistance of SSA and/or others as in the above graph.	**October 5, 2005 –** The Board agreed with the staff recommendations.	
Question #9 – What should be done with RR Retirement, Unemployment Insurance, and Black Lung Benefits? **Th**e Board did not have an opportunity to address this issue at the August 18, 2005 meeting. Staff recommended the following**:**	**October 5, 2005 –** The Board did not object to the staff recommendation. The members discussed other types of sensitivity analysis for consideration and requested additional examples.	

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Railroad Retirement – analogize to OASDI and SMI. Unemployment Insurance – continue to apply SFFAS 17 Black Lung Benefits – continue to apply SFFAS 17 Railroad Retirement program features are similar enough to OASDI and Medicare to apply the same approach. Unemployment insurance is unlike OASDI and SMI and for the present the SFFAS 17 is adequate. Black Lung Benefits is immaterial and is phasing-out and SFFAS 17 requirements are adequate.		
Question #10 – What is the reporting objective for social insurance? **The staff recommended that the objective should be to report the costs incurred in during the reporting period based on obligating events in that period.** The objective of the communication should be to report the costs incurred in during the reporting period and the amount of those costs that will have to be financed in future budgets. The latter are sometimes referred to as "legacy costs" or "sunk costs." They represent the accrued liability portion of long-term actuarial projections. Other measures are either macro economic or pertain to a specific aspect of the plan, e.g., return on investment..	A majority of the Board agreed with the recommendation.	The Board did not express disagreement but see Mr. Patton's issue in Question #5 above.
October 5, 2005 – **Issue #11 – Are Increments In The Liability For Social Security After 40 Quarters Obligating Events?** Staff recommends alternative #1: One obligating event: 40 quarters. Cost increments after 40 quarters would be characterized as a function of the required measurement procedures. Cost is the present value of the benefit that the participant will receive based initially on 40 quarters of work in covered employment and incremented thereafter by each additional quarter-month-day of work in covered employment attributable to the reporting period.	**October 5, 2005 –** The Board did not object to the staff recommendation. Chairman Mosso asked board members having view on those three questions, to communicate them to Rich directly. Several members did communicate via e-mail. One member subsequently communicated his belief to the staff that the Board didn't really have a full opportunity to object or agree with staff at the meeting. He believes more discussion of these issues is necessary.	

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October 5, 2005 – **Issue #12 – How Should the Medicare HI Cost Be Attributed?** Staff recommended recognizing the present value of the entire obligation at 40 quarters. The goal is for the service cost component of expense to be the actuarial present value of benefits attributed by Social Security's benefit formula to (1) 40 quarters of work in covered employment and (2) subsequent quarters (or months or days) of work, in the periods that these are attained. For Medicare, no additional expense is attributed to subsequent quarters of work.	**October 5, 2005 –** The Board did not object to the staff recommendation. Chairman Mosso asked board members having view on those three questions, to communicate them to Rich directly. Several members did communicate via e-mail. One member subsequently communicated his belief to the staff that the Board didn't really have a full opportunity to object or agree with staff at the meeting. He believes more discussion of these issues is necessary.	Post-October FASAB meeting comments from the Treasury Dept. Board member state that he believes fair presentation of the financial statements requires that Medicare HI costs be spread out evenly over the participant's working years in covered employment to properly match revenues with expenses in a fashion similar to OASD:. I agree with staff's conclusion and recommendation for OASDI and I agree with staff's conclusion that the liability for OASDI is the accumulated cost. Therefore, staff should apply the same method for recognizing Medicare HI costs as OASDI to achieve a consistent accounting treatment and for matching costs with revenues.] Post-October FASAB meeting comments from CBO regarding the proposed accounting for Medicare: "… CBO favors the current financial accounting treatment of Medicare and other ---only a liability for the amount due and payable is booked and none of the comments that follow change that view. "First, Medicare is a benefits program not an insurance program, so the accounting model for insurance

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		should not be considered. "Second, the accounting for Medicare Parts A, B, and D should be consistent. All should have the same obligating event. If the Board continues to favor 40 quarters as the obligating event for Part A (rather than age 65), then it should similarly do so for Parts B and D too. About 96 percent of Part A participants enroll in Part B.
October 5, 2005 – **Issue #13 – Should Medicare SMI Be Accounted For As Short- or Long-Duration Insurance?** Staff recommended that SMI be treated as short-duration insurance. This recommendation is and for some time will remain tentative. Social insurance issues and insurance accounting are complex subjects. The accounting concepts in this project are expected to develop and be refined as the project continues.	**October 5, 2005 –** The Board did not object to the staff recommendation. Chairman Mosso asked board members having view on those three questions, to communicate them to Rich directly. Several members did communicate via e-mail. One member subsequently communicated his belief to the staff that the Board didn't really have a full opportunity to object or agree with staff at the meeting. He believes more discussion of these issues is necessary.	Post-October FASAB meeting comments from CBO regarding the proposed accounting for Medicare: … "[I[f the Board insists on accounting for Part A and Part B differently and applying an insurance model of accounting to Medicare, as staff is proposing, then CBO would prefer that Part B be characterized as a long-duration contract rather than a short-duration contract. Evidence shows that very few participants drop there coverage of Part B over time, in fact, enrollment increases. (Participants are, however, penalized for late enrollment--10 percent per year.)."
Question #14 – Does the Board agree that SFFAS 17 should be rescinded? Staff recommends rescinding SFFAS 17 even though the reporting standards for Unemployment Insurance and Black Lung benefits will be essentially carried forward. The staff does not believe that the mechanics of retaining certain paragraphs of SFFAS 17 while rescinding others is		

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workable. It will be much clearer to incorporate those paragraphs in this new standard as one package.]		
Question #15 – Does the Board agree that the new SOSI line items and the new SOSI section should be added? Staff is recommending a new SOSI section to include an explanation of changes in present values that were discussed at the October meeting.		
Question #16 – Does the Board agree that guidance for asset reporting should be included in this standard? If so, is the draft paragraph sufficient? SFFAS 17 is silent about assets. The staff recommends including a paragraph reflecting the approach used for federal pensions in SFFAS 5, par. 68. It would apply to component entities. The basis for conclusions explains that component entity assets are liabilities of the consolidate governmentwide entity		
Question #17 – With respect to assumptions, does the Board agree that the standard should include general guidance requiring the entity's best estimates of demographic and economic assumptions and refer to Actuarial Standards of Practice as proposed? Staff recommends providing general guidance in the new standard along with a reference to Actuarial Standards of Practice (ASP). The general guidance is based on SFFAS 17, par. 25. SFFAS 17 provided no other guidance. The reference to ASPs is from the FASAB pension standard in SFFAS 5, which provides general guidance and references actuarial standards practice.		
Question #18 – Does the Board agree that the sensitivity analysis requirement should provide an option for the preparer (either vary key assumptions or provide a stochastic analysis – or both) rather than require one or the other? **Question #18.2 –Does the Board agree that the**		

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governmentwide entity should be exempt from sensitivity analysis? The proposed standard does not require "sensitivity analysis" for the governmentwide entity. Staff recommends paragraphs to replace the SFFAS 17 sensitivity requirement, par. 27.4 ("Sensitivity Analysis)." Unlike SFFAS 17, the new requirement would apply to the expense and liability amounts instead of the cashflow projection that is part of the RSI, as currently in SFFAS 17. Mr. Patton mentioned that the uncertainty of the expense and liability and SOSI amounts, i.e., the estimates in the primary financial statements, should be addressed. Both SFFAS 17 and this proposed standard require sensitivity analysis of SOSI present values.		
Question #19 – Does the Board agree that Medicare HI should be recognized at 40 QC; or, should Medicare HI costs be spread evenly over the participant's working years in covered employment? This question essentially reiterates Question 12. The staff recommends recognizing the present value of the entire obligation at 40 quarters. The goal is for the service cost component of expense to be the actuarial present value of benefits attributed by the social insurance benefit formula to (1) 40 quarters of work in covered employment and (2) subsequent quarters (or months or days) of work, in the periods that these are attained. The present value of a future Social Security benefit continues to increase with work in covered employment. For Medicare, however, no additional expense is attributed to subsequent quarters of work.		The Treasury Dept. Board member state that he believes fair presentation of the financial statements requires that Medicare HI costs be spread out evenly over the participant's working years in covered employment to properly match revenues with expenses in a fashion similar to OASD:. I agree with staff's conclusion and recommendation for OASDI and I agree with staff's conclusion that the liability for OASDI is the accumulated cost. Therefore, staff should apply the same method for recognizing Medicare HI costs as OASDI to achieve a consistent accounting treatment and for matching costs with revenues "… CBO favors the current financial accounting treatment of Medicare and other ---only a liability for the amount due and payable is booked and none of the comments

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		that follow change that view.
Question #20 – Does the Board agree that the accounting treatment for Medicare HI and Medicare SMI should be the same? This question is similar to Question 13. The staff recommends that obligating event for Medicare SMI not be the same as for Medicare HI. The government has a present obligation for Medicare SMI when the Medicare SMI participant elects to take the insurance and to begin paying premiums. At that point the Medicare SMI participant is required to make a substantive decision to take the insurance and the government must stand ready to fulfill the obligation should the participant enroll. Conversely, Medicare HI participants are compelled to pay payroll taxes throughout their work in covered employment and do not have to make a decision when eligible for immediately benefits. Medicare SMI participants pay premiums, albeit a heavily subsidized one. Medicare HI participants do not pay premiums.		From CBO: “First, Medicare is a benefits program not an insurance program, so the accounting model for insurance should not be considered. “Second, the accounting for Medicare Parts A, B, and D should be consistent. All should have the same obligating event. If the Board continues to favor 40 quarters as the obligating event for Part A (rather than age 65), then it should similarly do so for Parts B and D too. About 96 percent of Part A participants enroll in Part B. …” [continued under question 21 immediately below]

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Question # 21 – Does the Board agree that Medicare SMI should follow accounting standards for short-duration or long-duration insurance contracts? This question essentially reiterates Question #13. The staff recommends that Medicare SMI should following short-duration standards. The agreement between the government and the participant is for protection for a fixed period. The government may cancel Medicare SMI or adjust its provisions at the end of any coverage period, for example, by adjusting the amount of premiums charged or changing the conditions under which coverage is provided. Most health insurance offered by private insurers is of this type. The periodic expense for Medicare SMI will include claims incurred resulting from insured events that have occurred as of the reporting date, including IBNR and contingencies.		From CBO: "However, if the Board insists on accounting for Part A and Part B differently and applying an insurance model of accounting to Medicare, as staff is proposing, then CBO would prefer that Part B be characterized as a long-duration contract rather than a short-duration contract. Evidence shows that very few participants drop there coverage of Part B over time, in fact, enrollment increases. (Participants are, however, penalized for late enrollment--10 percent per year.)."
Question #22 – Does the Board agree that sensitivity analysis should include the liability and expense amounts as well as the SOSI present values and exclude the cashflow projections? The staff recommends (1) focusing sensitivity analysis on the expense and liability and SOSI amounts, i.e., the estimates in the primary financial statements, should be addressed; (2) allowing the component entities the option of analyzing sensitivity either using the SFFAS 17 approach of varying key assumptions, or using a stochastic approach; and (3) no sensitivity for the governmentwide entity.		
Question #23 – Does the Board agree that expected value should be mentioned in the basis for conclusions? The staff recommends including a discussion of expected value. The topic is currently under discussion by IASB and FASB and others and is germane to the discussion of uncertainty.		

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Question #24 – Does the Board agree that the basis for conclusions ought to include a discussion of objectives? If so, are the draft paragraphs satisfactory? The staff recommends including a discussion of overall objectives of the new standard.		