December Board Binders TAB E, Sub-tab 2

December 16, 2004 Board Meeting
Public Hearing on Exposure Draft
Inter-Entity Cost Implementation: Amending SFFAS 4 Managerial Cost Accounting Standards and Concepts
Agenda of Speakers

Speakers Providing Testimony

9:00-9:30	Dan Fletcher, Department of Interior, Office of the Chief Financial Officer
9:30-10:00	John D. Webster, Library of Congress, Chief Financial Officer
10:00-10:30	Anna D. Gowans Miller, AGA Financial Management Standards Board

Public Hearing on *Inter-Entity Cost Implementation: Amending SFFAS 4 Managerial Cost Accounting Standards and Concepts*

Speakers Providing Testimony

A. Biography

Daniel L. Fletcher

Mr. Fletcher is the Associate Director for Financial Reporting and Systems with the Department of the Interior, which he joined in April of 2004. Prior to DOI he was a senior financial manager with the Office of Personnel Management, where he was also with the Office of Inspector General as a senior audit manager. He is a Certified Public Accountant with a BS in Business Administration and is currently pursuing a Masters in Information Technology. He is a member of the American Institute of Certified Public Accountants and the Association of Government Accountants.

B. Statement or Remarks

Thank you for the opportunity to comment on the Federal Accounting Standards Board Exposure Draft, "Inter-Entity Cost Implementation - Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts."

The Department of the Interior does not concur with proposal in the Exposure Draft to rescind paragraph 110 and a portion of paragraph 111 of Statement of Federal Financial Accounting Standards (SFFAS) No. 4. While we firmly believe that the identification of the full cost of agency operations is important, we do not believe that this proposal is the correct approach, as it does not provide enough structure and guidance to agencies. This lack of structure is likely to result in costly and time consuming "hunts" for imputable costs that would not add value to the quality or usefulness of cost data. We believe that a more measured, alternative approach, such as that presented by Mr. Robert Reid in Appendix B, would better accomplish the Board's objectives and ensure that agencies appropriately capture the full cost of operations.

The guidance adopted in SFFAS 4 provides three factors to consider in determining whether an inter-entity cost is material to the receiving entity, specifically:

- i. Significance to the entity;
- ii. Directness of relationship to the entity's operations; and
- iii. Identifiably.

SFFAS 4 further states that inter-entity cost recognition is not required if the underreimbursed or non-reimbursed costs are related to broad and general support, and that imputed costs should be limited to those identified by the Office of Management and Budget (OMB).

The Department believes that this guidance in its entirety is correct and appropriate. The review and input of OMB or another authoritative source is critical due to the vast number of initiatives and activities that cross Federal agencies. Read literally, and without the stipulation for outside review, agencies would likely be required to impute small and insignificant costs. Materiality is an audit concept, not an accounting preparation concept. Preparers are rightly expected to record all financial transactions. The purchase of $2.00 box of pencils is recognized in the accounting system. Without appropriate limits, agencies would likewise be expected to identify and record any benefit received from other agencies.

For example, the standard setting activity by FASAB requires that time be spent by individuals at other Federal agencies to research accounting issues, respond to staff inquiries, review Exposure Drafts, and otherwise participate in the standard setting process. One could argue that the cost of those services, being critical to the standard setting process, should be imputed by FASAB and included in the "full cost" of developing accounting standards. This, of course, is not a reasonable interpretation. However, there is nothing in the current SFFAS #4 as amended, to indicate that such an interpretation would be incorrect.

Without clear and specific guidance as to where to "draw the line" regarding the costs to be imputed, this proposal is very likely to result in expensive and time consuming accounting exercises, and unresolvable disputes with auditors.

Accordingly, we do not concur with the proposal in the Exposure Draft. However, we suggest that the following actions be taken by OMB, in their role provided by SFFAS #4:

1. A task force or committee should be established to publish case studies illustrating costs that should and should not be imputed; and
2. OMB should establish a dollar threshold, such as 5% of total costs, with the provision that an agency not be required to seek out, research or report potential imputed costs under that amount.

The considerations that should be considered by OMB and/or this task force include:

- A mechanism for identification of highly significant costs that should be imputed;
- Language and guidance to ensure that marginal costs are not caught up in the imputed cost guidance.
- Consideration of whether the costs would impact the calculation of billings to the public, along with recognition that billings to the public based on cost of services is relatively rare (the vast majority of Federal services are intended to be funded by General Fund receipts); and
- Guidance for the provider and receiving entity to ensure appropriate accounting treatment by both parties. Specifically, while it might be appropriate for one entity to impute costs, it does not follow that the providing entity should "impute" revenue. If the range of imputed costs is to be expanded, then additional guidance is needed for the providing agency.
- A clearance process for questions raised by auditors or other 3rd parties.

Marginal costs include both costs that are minor in comparison to the statements taken as a whole, and minor in terms of their relationship to the role and decisions of the agency. For example, costs of participation in the standard setting process incurred by other Federal agencies are marginal to FASAB.

Department of the Interior Imputed Cost Examples

Interior has identified two imputed costs, beyond those presently identified by OMB. First, Interior identified a significant non-reimbursed inter-entity cost related to the Bureau of Reclamation's Water and Irrigation Projects prior to the adoption of SFFAS #4. These costs are a necessary component of full cost for determining billings to the public, and include estimated interest during construction and costs incurred by other Federal agencies, such as the Western Area Power Administration, Bureau of Public Debt and Corps of Engineers. Interior discussed this situation with the Office of Management and Budget after the adoption of SFFAS #4, and it was determined that Reclamation should continue to impute these costs.

Second, Interior may soon have another cost which we would impute. The Department is purchasing a new accounting system, which will be capitalized and depreciated centrally by a Working Capital Fund located in the Office of the Secretary. The total cost of this system is expected to be in excess of $120 million. Given the cost of the system and direct benefit of the system to the bureaus, the Department intends to apply the imputed cost model to ensure full costs are reported at the bureau level. Under the current accounting standards, the Department would most likely forward this situation to OMB for concurrence, and impute the costs in order to fairly state bureau level operations.

This situation provides an opportunity to identify the issues and guidance needed by the Department. These issues include:

- What procedures, such as OMB concurrence, are needed under the current guidance, and what procedures would be appropriate across the federal government on an ongoing basis.
- How should the amount of costs to be imputed be determined? In the DOI Accounting System example, the system is expected to be brought on over a four-year period, thus costs will need to be recognized by the first bureaus to come up, while “Construction in Progress” continues for the remaining bureaus and system as a whole.
- What accounting model should be used by the “providing agency”? For fair presentation of DOI-wide activity, the costs reported by the Office of the Secretary should be reduced as costs are reported by bureaus. However, we have not determined whether the “imputed costs” recognized by a bureau would be equal to the depreciation expense recorded by the Office of the Secretary in the same period.

Reimbursable Agreements

The question in the Exposure Draft regarding the uses of reimbursable agreements between agencies makes a valid point that the wider use of reimbursable agreements for specific transactions between agencies would reduce the need for imputed costs. However, decisions regarding the increased use of reimbursable agreements must weigh the additional costs of the administrative burden against the benefits. Further, we do not believe that management decisions regarding methods of funding and reimbursement should be driven by the ease of accounting.

Decisions regarding the number of reimbursable agreements and the situations in which reimbursable agreements are appropriate should be made by agency management, the Office of Management and Budget and Congress based on what is most appropriate and efficient for the management of the government. There is a real cost associated with establishing and monitoring reimbursable agreements, and with the transfer of funds between operations and agencies. It should be left to managers at all levels of government to determine the cost-benefit of reimbursable agreements. Increasing the amount of paperwork (i.e. reimbursable agreements) between federal agencies will not increase the accuracy or usefulness of management information. Reimbursable agreements are one of many tools available to management and should not be viewed as a “one-size fits all” solution.

It should also be noted that providing services to other government agencies is a relatively small part of the mission and operations of most government agencies. Likewise, most public services provided by the Federal government are funded by general fund receipts, primarily income tax receipts, and the beneficiaries of those services are not billed.

In summary, while we fully support the identification and reporting of the full cost of agency operations, OMB or another body should retain the authority to define the specific costs to be imputed, to ensure a reasonable and balanced application of this standard.

Thank you for the opportunity to comment on this Exposure Draft.

Dan Fletcher, Department of Interior, Office of the Chief Financial Officer
--

C. Department of Interior Comment Letter Previously Submitted

Ms. Wendy M. Comes
Executive Director
Federal Accounting Standards Advisory Board
441 G Street, NW
Washington, D.C. 20548

Dear Ms. Comes:

Thank you for the opportunity to comment on the Federal Accounting Standards Board Exposure Draft, "Inter-Entity Cost Implementation - Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts." We recognize that full cost identification and recognition, when done appropriately, improve the value of financial information. Implementing the proposed approach will result in more costs than benefits and no increased value or benefit to other Federal agencies and taxpayers.

Accordingly, the Department of the Interior does not concur with the Exposure Draft's proposed rescission of paragraph 110 and a portion of paragraph 111 of Statement of Federal Financial Accounting Standards (SFFAS) No. 4. We support the alternative approach presented by Mr. Robert Reid in Appendix B. His recommended approach would better accomplish the Board's objectives and ensure that agencies appropriately capture the full cost of operations.

Please see our responses to specific questions in the enclosure. Thank you again for the opportunity to comment on this Exposure Draft. Please contact Daniel Fletcher at 202-208-5225 if you wish to discuss our comments further.

Sincerely,

P. Lynn Scarlett
Assistant Secretary-Policy, Budget and Management

Enclosure

1) This exposure draft proposes that the inter-entity cost provisions of SFFAS 4 (par. 105 – 115) be fully implemented for reporting periods beginning after September 30, 2007. Do you agree with this proposal? If not, please explain your reasons and any alternative that you would prefer.

We do not concur with the proposal in the Exposure Draft. The full cost of agency operations is necessary for true program management. However, the proposal does not provide enough structure and guidance to agencies. This lack of structure will result in unnecessary searches for imputable costs that do not add value to the quality or usefulness of cost data.

There are a vast number of initiatives and activities that cross Federal agencies. For example, the standard setting activity by FASAB requires that time be spent by individuals at other Federal agencies to research accounting issues, respond to staff inquiries, review Exposure Drafts, and otherwise participate in the standard setting process. One could argue that the cost of those services, being critical to the standard setting process, should be imputed by FASAB and included in the "full cost" of developing accounting standards. This, of course, is not a reasonable interpretation. However, there is nothing in SFFAS #4 as amended by the current exposure draft to indicate that such an interpretation would be incorrect.

Without clear and specific guidance to define the costs to be imputed, this proposal is very likely to result in expensive and time consuming accounting exercises, and potential disputes with auditors.

We support a more targeted approach, such as the one proposed by Mr. Reid.

2) Appendix B presents the alternative views of one member, Mr. Robert Reid. Do you agree with his proposal to implement the inter-entity cost provisions by identifying specific costs to be recognized on a step-by-step basis as envisioned in SFFAS 4? Please explain your reasons for agreeing or disagreeing.

On the whole, we concur with the alternative views presented by Mr. Robert Reid. We concur that a measured, step-by-step, practical approach to implementing the inter-departmental costing standard is critical. Such an approach, agencies will provide the guidance needed to make consistent and appropriate decisions on which costs are to be recognized. This approach should include:

- A generally accepted approach and methodology for identification of significant costs that should be imputed;
- Consideration of whether the costs would impact the calculation of billings to the public, along with recognition that billings to the public based on cost of services may have to be increased to cover these costs. Currently these costs are overwhelmingly funded by General Fund receipts; and
- Guidance for the provider and receiving entity to ensure appropriate accounting treatment by both parties. Specifically, while it might be appropriate for one entity to impute costs, it may not follow that the providing entity should "impute" revenue. If the range of imputed costs is to be expanded, then additional guidance is needed for the providing agency.

3) Do you believe there are now non-reimbursed or under-reimbursed inter-entity costs meeting the recognition criteria established in SFFAS 4, par. 111-113 (see page19)? Please provide examples and/or explain your answer.

Yes, there are non-reimbursed inter-entity costs that meet the SFFAS recognition criteria. The Department of the Interior identified one such circumstance related to the Bureau of Reclamation's Water and Irrigation Projects prior to the adoption of SFFAS #4. These costs are a component of full cost for determining billings to the public, and include estimated interest during construction and costs incurred by other Federal agencies, such as the Western Area Power Administration, Bureau of Public Debt and Corps of Engineers. Interior discussed this situation with the Office of Management and Budget after the adoption of SFFAS #4, and it was determined that Reclamation should continue to impute these costs.

We are not aware of other costs that should be imputed for fair presentation of financial statements or for accurate management and billing information. However, a procedure should exist to ensure that such costs are captured and imputed. These procedures should be specific enough to ensure that only costs significant to the agency are imputed and that time and resources are not devoted to insignificant items.

4) Do you believe that federal entities will seek additional reimbursable agreements or modify existing reimbursable agreements (e.g., by increasing fees) because non-reimbursed or under-reimbursed inter-entity costs may be recognized? Please explain your answer.

Seeking additional reimbursement for newly recognized expenses is a logical expectation. If costs are recognized, anti-deficiency laws would require corresponding revenue increases or other cost decreases. These complications make predicting the likelihood of wholesale fee increases unrealistic, and if there is no intent to increase fees these efforts are unnecessary. Accounting procedures should accurately capture the substance of transactions, and timely, accurate and reliable accounting information must be available to managers for decision-making. However, it does not follow that the desire to simplify accounting procedures should drive management decisions.

Decisions regarding the number of reimbursable agreements and the situations in which reimbursable agreements are appropriate should be made by agency management, the Office of Management and Budget and Congress based on what is most appropriate and efficient for the management of the government. In addition, it should be recognized that there is a real cost associated with establishing and monitoring reimbursable agreements, and with the transfer of funds between operations and agencies. It should be left to managers at all levels of government to determine the cost-benefit of reimbursable agreements. Increasing the amount of paperwork between federal agencies by increasing the number of reimbursable agreements will not increase the accuracy or usefulness of management information. Reimbursable agreements are one of many tools available to management and should not be viewed as a "one-size fits all" solution.

It should also be noted that providing services to other government agencies is a relatively small part of the mission and operations of most government agencies. In addition, most public services provided by the Federal government are funded by general fund receipts, and the beneficiaries of those services are not billed.

---

5) Because this proposal includes a time period during which additional guidance may be sought (consistent with the task force recommendation found on page 16), the Board wishes to gather additional information that would be useful in planning for that guidance. Thus, the following questions are intended to assist the Board in planning and do not relate directly to the provisions of this proposal.

a. SFFAS 4 provides three factors to consider in determining whether an inter-entity cost is material to the receiving entity. (See SFFAS 4, par.112 at page 19.) The factors are:

> ***i. Significance to the entity -- The cost of the good or service is large enough that management should be aware of the cost when making decisions.***
>
> ***ii. Directness of relationship to the entity's operations -- The good or service provided is an integral part of and necessary to the output produced by the entity.***
>
> ***iii. Identifiability -- The cost of the good or service provided to the entity can be matched to the entity with reasonable precision.***

Is additional guidance needed to apply these factors? If so, please indicate what specific questions you have regarding the application of these factors.

b. SFFAS 4 provides that inter-entity cost recognition is not required if the underreimbursed or non-reimbursed costs are related to broad and general support. Broad and general support is provided by a providing entity to all or most entities of the federal government and is not an integral part of the receiving entities' output. Is additional guidance needed to apply this exception? If so, please identify any activities that may be broad and general support but for which the above description does not resolve the classification.

For both A. and B. above, we believe that the guidance in SFFAS #4 is clear, and that the guidance in the above paragraphs is sufficient as long as reasonable and well-defined procedures for the identification of imputed costs is adopted. However, if the proposal in the Exposure Draft is adopted, we do not believe that any amount of clarification of the above paragraphs will prevent the standards from being applied to insignificant and inappropriate costs.

A. Biography

LIBRARY OF CONGRESS
JOHN D. WEBSTER
BIOGRAPHY

Mr. Webster is the Chief Financial Officer at the Library of Congress. He was appointed to that position in November 1989 and is responsible for strategic planning, budget, accounting operations, financial reporting, financial systems, and disbursing functions. During his tenure with the Library, he has received the Librarian's award for Meritorious Service and many performance awards for his work in improving the Library's financial management. The Library's Independent Auditor's have issued an unqualified opinion on the Library's consolidated financial statements for the past eight fiscal years.

Previously, Mr. Webster worked for 14 years with the Office of Personnel Management (OPM) in a number of positions associated with Government-wide benefits programs. His last position with OPM was Deputy Assistant Director for Financial Control and Management, with responsibility for accounting, budget, management information, quality assurance, and administrative services for the Retirement and Insurance Group. He received the Director's award for Distinguished Service at OPM for improving the financial management of the benefit systems.

Before joining the Federal Government in 1975, Mr. Webster was a senior accountant with Haskins & Sells, where he specialized in C.P.A. audits and systems development for public and private corporations.

Mr. Webster has also received the Department of the Treasury's award for Distinction in Payments Management in 1990 for his work in improving the cash management of the Federal Employees' Health Benefits system, the Achievement of the Year Award in 1997 from the Association of Government Accountants' Washington Chapter for improving the Library's financial management, and the Association of Government Accountants' President's award in 2000 for outstanding work as National Treasurer and Chair of the Finance and Budget Committee.

Mr. Webster is a Certified Public Accountant and Certified Government Financial Manager. He also passed the Certified Internal Auditor examination in August 1980. He holds a bachelor of science degree in accounting from the University of Maryland. He has taught accounting and auditing courses at the Northern Virginia Community College and Howard County Community College in Columbia, Maryland. Mr. Webster is a member of the Washington Chapter of the Association of Government Accountants (AGA) and the American Institute of Certified Public Accountants. Mr. Webster is on the AGA Journal board, National Board of Directors, and Awards committee. Mr. Webster is also co-chairman of the Legislative Branch Financial Managers Council.

B. Library of Congress Comment Letter Previously Submitted

> *1) This exposure draft proposes that the inter-entity cost provisions of SFFAS No. 4 (para. 105 – 115) be fully implemented for reporting periods beginning after September 30, 2007. Do you agree with this proposal? If not, please explain your reasons and any alternative that you would prefer.*

The Library of Congress (the Library) is in a unique position to comment on the exposure draft (ED) because it has already recognized inter-entity costs beyond those that are required by Office of Management and Budget (OMB) Bulletin No. 01-09. The Library recognizes four inter-entity costs: (1) Office of Personnel Management (OPM), (2) U.S. Treasury Judgement Fund (USTJF), (3) Architect of the Capitol (AOC), and (4) Government Printing Office (GPO). Items (1) and (2) are required by OMB Bulletin No. 01-09; although not required by OMB Bulletin No. 01-09, items (3) and (4) have been included as imputed costs and financing sources in the Library's financial statements since FY 1998.

The Library, AOC, and GPO are members of the Legislative Branch Financial Management Council (LBFMC). The Library's membership and participation in the LBFMC have been instrumental in providing the cooperation and exchange of information needed to obtain the cost data for AOC and GPO inter-entity costs and the Library has fine-tuned this process over several years. The work performed through this committee since FY 1998 has supported the Library's decision to recognize the AOC and GPO inter-entity costs of these legislative branch Agencies. However, the Library is not subject to the requirements of the CFO Act and is not a member of the CFOs Council; therefore, the Library has not had similar access to the executive branch Agencies.

Based on its experience with the inter-entity costs of AOC and GPO, the Library feels that an implementation date of FY 2008 does not provide adequate time to fully implement the inter-entity cost provisions of SFFAS No. 4. Furthermore, the Library supports the alternative view taken by Mr. Reid to implement the inter-entity cost provisions by identifying specific costs to be recognized on a step-by-step basis. The Library believes that the standard, as amended by the ED, remains unclear on a number of issues; these issues are described below:

> a. There is no clear delineation between (i) an Agency that is providing goods and services for another Agency versus (ii) an Agency that partners with other Federal, State, and local Agencies to implement a program.
>
> For example, through a national network of cooperating libraries, the National Library Service for the Blind and Physically Handicapped (NLS/BPH) administers a free library program of braille and audio materials circulated to eligible borrowers in the United States by postage-free mail. To implement this program, regional and subregional libraries receive funding from State, local and Federal sources and there is an additional appropriation to the U.S. Postal Service (USPS) for free matter for the blind or handicapped. The USPS is required to provide free postage for this program (as well as other programs) under 39 U.S.C. 3403; the statute requires the USPS to provide free postage to individuals,

libraries, and other noncommercial organizations serving blind and physically handicapped persons.

The standard is unclear as to whether the NLS/BPH (i) is receiving free postage for the program or (ii) works as a partner with the USPS, State, local, and other Federal agencies to implement this program. NLS/BPH uses the services of USPS because the USPS is legally required to provide it as a free service. If the service were not free, a number of shipping vendors would be able to provide the service.

b. There is no clear delineation as to the purpose and scope for which the providing Agencies perform the services. Providing Agencies may perform these services for various reasons; a particular service may be (i) an integral part of the providing Agency's mission and represent the majority of its activity, (ii) administrative in nature and benefits from specialization and economies of scale (such as cross-servicing under the Economy Act), or (iii) historically and traditionally performed by the providing Agency, may be related to its mission, but is only a minor activity.

The standard makes a specific exemption for Agencies that provide broad and general support for all entities, but there is no exemption for Agencies that perform services for another Agency because that is an integral part of their mission. For example, the Congressional Research Service (CRS) provides services to the Congress. Is it the standard writers' intention that the Library be compelled to report the inter-entity cost of CRS' services to the House, Senate, or other Agencies? The Library would not support such an approach, and if required, the Library would need to identify these costs, identify a cause-and-effect cost driver for each type of cost, and collect cost driver statistics. The Law Library and Library Services are other Service Units within the Library whose missions serve a number of constituencies (Congress, other libraries, and the public).

c. The standard requires recognition of inter-entity costs when they are material to the receiver, but ignores inter-entity costs that are material to the provider. If a small Agency provides goods and services to a large Agency, the inter-entity costs may be immaterial to the receiver, but very material to the provider.

Conversely, if the inter-entity costs are material to the receiver, but immaterial to the provider, the large Agency is compelled to provide cost data to the receiving Agency. The Library provides goods and services to many small Agencies such as the Office of Compliance, Open World Leadership Center, Abraham Lincoln Commission, and Capitol Preservation Commission. The services the Library may provide to these Agencies are immaterial to the Library as the provider, but may be material to them as the receiver. Currently, the Library's reimbursable agreements with these Agencies do not include the inter-entity costs of the Architect of the Capitol (AOC) and the Office of Personnel Management (OPM).

As described above, the Library believes that the lack of clear definitions and guidance will lead to inconsistent implementation of this standard, especially in the current time-constrained environment of interim and accelerated year-end reporting requirements.

> *2) Appendix B presents the alternative views of one member, Mr. Robert Reid. Do you agree with his proposal to implement the inter-entity cost provisions by identifying specific costs to be recognized on a step-by-step basis as envisioned in SFFAS No. 4? Please explain your reasons for agreeing or disagreeing.*

Yes, the Library agrees with the alternative views of Mr. Reid. We agree with his proposal to implement the inter-entity cost provisions by identifying specific costs to be recognized on a step-by-step basis as envisioned in SFFAS No. 4. The Library provided examples in our response to 1) above that describe the reasons why the proposed standard (as amended by the ED) would be difficult to apply and implement. However, we suggest that the standard encourage providing and receiving Agencies to work with each other and FASAB to identify and recognize material inter-entity costs and help ensure consistent accounting treatment.

> *3) Do you believe there are now non-reimbursed or under-reimbursed inter-entity costs meeting the recognition criteria established in SFFAS No. 4, para. 111 -- 113 (see page 19)? Please provide examples and/or explain your answer.*

Yes, the Library believes that there are now non-reimbursed or under-reimbursed inter-entity costs meeting the recognition criteria established in SFFAS No. 4, paragraphs 111 through 113. In our response to 1) above, we provided examples for the Library as a receiver of services (GPO and AOC).

> *4) Do you believe that Federal entities will seek additional reimbursable agreements or modify existing reimbursable agreements (e.g., by increasing fees) because non-reimbursed or under-reimbursed inter-entity costs may be recognized? Please explain your answer.*

Yes, depending upon the circumstances, we believe that Federal entities may seek additional reimbursable agreements or modify existing agreements because non-reimbursed or under-reimbursed inter-entity costs may be recognized. However, clearer guidance must be established on how inter-entity costs will be treated on reimbursable agreements; for example, under what circumstances should a providing Agency charge for services it receives from another entity (non-reimbursed, under-reimbursed, and reimbursed). Also, it may be appropriate to consider whether the providing and/or receiving Agencies are included in the Financial Report of the U.S. Government (FRUSG). The FRUSG includes the executive, legislative, and judicial branches, and other independent establishments and Government corporations, plus a number of independent executive agencies.

> *5) Because this proposal includes a time period during which additional guidance may be sought (consistent with the task force recommendation found on page 16), the Board wishes to gather additional information that would be useful in planning for that guidance. Thus, the following questions are intended to assist the Board in planning and do not relate directly to the provisions of this proposal.*

a. SFFAS No. 4 provides three factors to consider in determining whether an inter-entity cost is material to the receiving entity. (See SFFAS No. 4, para. 112 at page 19.) The factors are:

i. Significance to the entity – The cost of the good or service is large enough that management should be aware of the cost when making decisions.

ii. Directness of relationship to the entity's operations – The good or service provided is an integral part of and necessary to the output produced by the entity.

iii. Identifiability – The cost of the good or service provided to the entity can be matched to the entity with reasonable precision.

Is additional guidance needed to apply these factors? If so, please indicate what specific questions you have regarding the application of these factors.

Additional guidance should be given on applying the criteria. For example, should all criteria, two out of three criteria (and in what combinations), or only one criterion apply?

In the first criterion, the Library believes that "significance to the entity" should go beyond the consideration of whether a cost is large and consider the importance of the goods or services to the receiving entity. A cost may not necessarily be material, but may still be integral and necessary in the fulfillment of the receiving Agency's mission. In this example, the second criterion is met, but not the first.

Who is doing the matching in the third criterion, the provider or the receiver? Depending upon the circumstances, either the provider or the receiver may provide the most accurate data. Does the matching imply direct tracing, or will the standard accept cost assignment or cost allocation as long as the same methodology is consistently used?

In FY 2003, the Library recorded an inter-entity cost and imputed financing source of approximately $178,000 for the U.S. Treasury Judgement Fund (USTJF). If the Library were to apply the three criteria to this inter-entity cost, (i) the cost may not be significant to management and (ii) there is no relationship of this service to the Library's outputs; but, (iii) the cost of the service can be matched to the Library. Therefore, only one out of the three criteria from the standard may be met. However, the Library has consistently recognized this inter-entity cost in its financial statements for those years that the cost has occurred because it is specifically listed as a cost that "reporting entities are required to recognize" per OMB Bulletin No. 01-09 (page 31).

b. SFFAS No. 4 provides that inter-entity cost recognition is not required if the under-reimbursed or non-reimbursed costs are related to broad and general support. Broad and general support is provided by a providing entity to all or most entities of the Federal government and is not an integral part of the receiving entities' output. Is additional guidance needed to apply this exception? If so, please identify any activities that may be broad and general support but for which the above description does not resolve the classification.

The standard states"The cost of such broad services should not be recognized as an expense (or asset) by the receiving entities when there is no reimbursement of costs (Paragraph 112)." The standard does not mention under-reimbursement. Please include "under-reimbursement" in the language of the standard if the Board intends to exclude both under-reimbursed and non-reimbursed costs.

Additional guidance should be given for defining broad and general services. Guidance should be provided to distinguish services provided by an Agency that are (i) broad and general because they are provided to all or most entities of the Federal government as opposed to (ii) Agency-specific and not broad and general. The General Accounting Office (GAO) may be an example of an Agency that provides some services that may be considered broad and general and some services that are Agency-specific. For example, services relating to the Single Audit Act or to the Chief Financial Officers Act may be considered broad and general, whereas services related to special studies, reviews, or performance audits on specific programs may not be broad and general. Perhaps the Board could develop additional criteria for determining whether a particular type of service is broad and general, such as whether the service is (i) seasonal, recurring, and/or routine; (ii) in support of legislation that requires compliance by all or most Federal Agencies; or (iii) in support of legislation that requires the providing Agency to provide oversight and guidance over all or most Federal Agencies. Also, guidance should be provided regarding which entity is really benefitting from and receiving the service. Continuing with GAO as the example, is the receiving Agency the Congress (who may request the service) or the entity being reviewed/audited?

A. Biography

Anna D. Gowans Miller, MBA, CPA

Anna. D. Gowans Miller is Technical Manager and Director of Research at the Association of Government Accountants (AGA), with dual responsibilities: staffing the AGA Financial Management Standards Board; directing AGA research programs in improving federal financial and performance management. She is a Certified Public Accountant (CPA), licensed to practice in Texas and the District of Columbia. She first worked with Touche Ross (now Deloitte & Touche), in Houston Texas. She taught accounting at the University of Houston, where she gained a Masters in Business Administration. She was senior auditor for the Corporation for Public Broadcasting and then Technical Manager at the American Institute of Certified Public Accountants (AICPA) in Washington, DC.

From 1995 to 1997 she was the professional staff member responsible for CFO Act and GPRA issues on the House of Representatives Government Management, Information, and Technology Subcommittee of the Committee on Government Reform and Oversight. While there, she monitored and developed changes to government accounting and auditing standards and reviewed and reported on the status of financial management and various management improvement initiatives, and was the House staff person responsible for directing into legislation the Federal Financial Management Improvement Act of 1996 and the Single Audit Act Amendments of 1996. She advised various Executive Branch agencies on how to improve their strategic plans as part of their GPRA implementation.

From 1997 to 2003, as an independent contractor, she verified, validated and certified results of Quality Management implementation in organizations of the Department of Defense (DoD) for the Office of the Secretary of Defense/Quality Management Office. She evaluated initiatives undertaken by Department of the Army, Navy, including Marine Corps, Air Force, Special Operations Command, Joint Commands, and Defense Agency units throughout the world, including applicants for the President's Quality Award over a period of seven years

She has aided the OUSD AT&L Directorate in its development of performance measures for incorporation into the annual budget submission for O&M programs. She advised units on how to integrate their performance measures with the goals of the overall DoD strategic plan, and helped prepare and participated in a tutorial to help units refine and finalize their individual submissions. She has provided assistance to the Asia-Pacific Center for Security Studies, advising the Center staff on how to develop outcome measures aligned with the Center's strategic goals and objectives.

Since the late seventies, she has been teaching and advising on cost and financial accounting techniques and analysis methods. She has written continuing professional education courses for the AICPA on governmental and nonprofit accounting and auditing. She has written and taught courses to staff throughout DoD on using financial data to validate process improvements and on how to use cost data to improve information used in A-76 competitive sourcing studies.

B. AGA Financial Management Standards Board Comment Letter Previously Submitted

July 30, 2004

AGA

Advancing Government Accountability

2208 Mount Vernon Ave
Alexandria, VA 22301

(703) 684-6931
(703) 548-9367 (fax)

Wendy Comes, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Ms. Comes:

The Association of Government Accountants (AGA) Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments on the Federal Accounting Standards Advisory Board's (FASAB) Exposure Draft *"Inter-Entity Cost Implementation: Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts" (ED).* The FMSB, comprising 21 members with accounting and auditing backgrounds in federal, state and local government, academia and public accounting, reviews and responds to proposed standards and regulations of interest to AGA members.

The majority of FMSB members agree with the proposal to set an implementation date for requiring costs covered by other reporting entities to be included in the full cost of outputs to be included in general purpose financial reports. The amendment would ensure that all material costs are included in full cost measures. Inter-entity costs need to be accounted for, and their inclusion results in a truer picture of the actual costs of services being provided by federal departments. It also allows for comparability between federal services and private providers. However, one also needs to consider the costs associated with compiling and reporting this information, and whether it simply adds another layer of bureaucracy to the process. The proposed requirement does allow entities time to develop internal guidance on recognizing inter-entity costs, seek implementation guidance, or establish reimbursable agreements. FMSB responses to the specific questions asked by FASAB, including the concerns of one member who has some issues with the proposal, are included as an attachment to this letter.

The FMSB appreciates the opportunity to comment on the ED. This response letter represents a consensus of the views of the FMSB members. No FMSB members objected to its issuance. We would be pleased to discuss this letter with you at your convenience. You can contact me at hintonrw@audits.state.ga.us or (404) 656-2174 or Anna D. Gowans Miller, CPA, AGA's Technical Manager and facilitator for this project, at amiller@agacgfm.org or (703) 684-6931, ext. 203.

Sincerely,

Russell W. Hinton

Russell W. Hinton, CGFM, Chair,
AGA Financial Management Standards Board

CGFM

ATTACHMENT A

Questions for Respondents

1) This exposure draft proposes that the inter-entity cost provisions of SFFAS 4 (par. 105–115) be fully implemented for reporting periods beginning after September 30, 2007. Do you agree with this proposal? If not, please explain your reasons and any alternative that you would prefer.

The majority of FMSB members agreed with the proposal. Several suggested that an even earlier date should be considered, as this information is relatively easy to determine for full costing. One member had some issues with the proposal as identified in the paragraphs below.

2) Appendix B presents the alternative views of one member, Mr. Robert Reid. Do you agree with his proposal to implement the inter-entity cost provisions by identifying specific costs to be recognized on a step-by-step basis as envisioned in SFFAS 4?Please explain your reasons for agreeing or disagreeing.

The majority of FMSB members opposed the alternative views proposal. Its opinion is that each federal agency should take responsibility for the accuracy and completeness of its financial information rather than relying on other parties such as the FASAB to deal with agency-specific issues or dictate which costs should be included. Although Mr. Reid correctly points out that the proposed statement goes beyond what SFFAS 4 had planned, the goal to fully disclose the cost of providing services remains. The proposed statement would appropriately be applied only to material items. It is likely that certain costs may be material to one department and not material to another. While the potential exists for reporting differing inter-entity costs among different departments, these inconsistencies should not bar the way to informing financial statement users of material costs incurred to provide the services of that government unit.

One member thought that Mr. Reid makes a valid point about the potential differences of opinion between auditors and preparers on what is material. This becomes a matter of "professional judgment." Currently, the two groups have disagreements on many other items related to financial statement preparation and "professional judgment". It would be unfortunate if this proposal were to add inter-departmental costs to the areas for potential disagreement.

His views here are influenced by the fact that no one has been able to identify any additional major inter-departmental costs that should be included in the financial statements. The AAPC was not able to identify such costs and FMSB members were not able to do to. The question that then arises is "are we tilting at windmills?" In his agency he knows of a few un-reimbursed inter-departmental costs, but none of them rises to the level of materiality that requires financial statement treatment.

Rather than just eliminate the current requirement, he would like to see if there are any costs that are really of concern, either government wide or for specific agencies, and then decide how to treat this matter. If there are large government wide inter-departmental costs, let us identify them (while continuing to exclude "broad and general" support). If not, let us examine if there are specific costs that need to be dealt with and make the decision then. He wondered whether the inclusion of inter-departmental costs in the financial statements has influenced any operating or investment decisions by any agency manager. They are not relevant for day-to-day decision-making.

3) Do you believe there are now non-reimbursed or under-reimbursed inter-entity costs meeting the recognition criteria established in SFFAS 4, par. 111-113 (see page19)? Please provide examples and/or explain your answer.

Although FMSB members were not aware of any specific examples, they thought that certain costs were likely to be missed, especially with the number of IT systems that do not "talk" to each other.

4) Do you believe that federal entities will seek additional reimbursable agreements or modify existing reimbursable agreements (e.g., by increasing fees) because non-reimbursed or under-reimbursed inter-entity costs may be recognized? Please explain your answer.

The FMSB thought it was possible, or even probable, that agencies would alter their agreements so as to capture the costs and recover them appropriately, if this new requirement identifies under or over charges. It also thought that there might be some anti-deficiency act issues, if it becomes apparent that some agencies are providing non-reimbursed services to other agencies out of their appropriated funds. If there will be significant additional reimbursable agreements, there may have to be a change in the way in which funds are appropriated. For example, if agency A provides non-reimbursed services valued at $1 million to agency B, those funds are included in the appropriation for agency A. If agency B now has to pay for those services, the $1 million should be appropriated to agency B; otherwise it will run into the anti-deficiency issue or will be required to reduce other mission related activities.

5) Because this proposal includes a time period during which additional guidance may be sought (consistent with the task force recommendation found on page 16), the Board wishes to gather additional information that would be useful in planning for that guidance. Thus, the following questions are intended to assist the Board in planning and do not relate directly to the proposal provisions.

a. *SFFAS 4 provides three factors to consider in determining whether an inter-entity cost is material to the receiving entity. (See SFFAS 4, par.112 at page 19.) The factors are:*

i. Significance to the entity -- The cost of the good or service is large enough that management should be aware of the cost when making decisions.

ii. Directness of relationship to the entity's operations -- The good or service provided is an integral part of and necessary to the output produced by the entity.

iii. Identifiability -- The cost of the good or service provided to the entity can be matched to the entity with reasonable precision. Is additional guidance needed to apply these factors? If so, please indicate what specific questions you have regarding the application of these factors.

The FMSB thought that this was appropriate and allowed for professional judgment. The three factors are sufficient to allow accountant and auditor to reach a consensus on which costs to consider material.

b. *SFFAS 4 provides that inter-entity cost recognition is not required if the under-reimbursed or non-reimbursed costs are related to broad and general support. Broad and general support is provided by a providing entity to all or most entities of the federal government and is not an integral part of the receiving entities' output. Is additional* *guidance needed to apply this exception? If so, please identify any activities that may be broad and general support but for which the above description does not resolve the classification.*

Additional guidance is not needed at this time; it should be left to the discretion of the accountant and auditor of the agency. FASAB should monitor agency implementation and be prepared to answer issues as they arise. It might be useful to develop a list of activities that would fall under this category to assist agencies in understanding this issue.