Federal Accounting Standards Advisory Board

November 16, 2007

To: Members of the Board

From: Richard Fontenrose, Assistant Director

Thru: Wendy M. Payne, Executive Director

Subject: Social Insurance,[1] Tab G

At the September meeting, the Board began to discuss what social insurance information is essential and how to communicate it. For the December meeting, the Board requested that the staff discuss specific essential information and potential displays. The paper in this Tab addresses these topics.

The discussion of essential information and, especially, display necessarily involves consideration of the current FASAB model and ongoing projects. In this regard, the social insurance project is mindful of the two other FASAB projects – fiscal sustainability and communication methods – that are developing information and considering display. The intent is for these projects to complement each other.

The scope of the social insurance project is narrow. It focuses primarily on the effect of past transactions and events on the Government's financial position during the period, and on effective ways to communicate that information to the users of federal financial reports. In addition, the social insurance project is modifying an existing standard, SFFAS 17. The fiscal sustainability project's scope is broader. Its objective is "to provide information to assist readers of the CFR in assessing whether future budgetary resources of the U.S. Government will likely be sufficient to sustain public services and to meet obligations as they come due." However, several "placeholders" are included in the accompanying staff paper to signify the possibility or probability of integration with the fiscal sustainability project.

The paper contains two recommendations:

Staff Recommendation #1 – The staff recommends four items for consideration as essential information. (See pages 4-10. The recommendation is on page 10.) Only one item would be new. The other items – the statement of social insurance (SOSI), a statement of changes in the SOSI net present values, and the current SFFAS 17 required supplemental information (RSI) – are listed in order to be comprehensive and understandable. The members' comments indicate

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

that they support these items. The new item represents the social insurance "benefit obligation" based on past earnings and past work in covered employment as of a valuation date. I have labeled this item the ***accrued benefit obligation*** for reasons explained in the accompanying paper. The change in the ***accrued benefit obligation*** caused by transactions and events attributable to the reporting period on an accrual basis, i.e., the accrued cost increments, would be considered essential information as well. There are, of course, alternative labels for such a measure and/or alternative measures, and they are discussed as well.

Recommendation #2 – Staff recommends a general display approach that is discussed in the paper using pro forma illustrations. (See pages 11-23. The recommendation is on page 23.)

Finally, the paper includes several appendices. Appendix A (see page 24) contains the growing list of consensus items that has been included in past briefing memoranda. Appendix B (see page 25) contains the "table of FASAB decisions" that was included in the October 2005 FASAB briefing materials. The table should be a useful reference as the Board moves forward in 2008 toward a revised social insurance standard. It reflects the Board's decisions that lead to the initial draft of a social insurance exposure draft in January 2006 and, eventually, to the preliminary views document. Staff will update the table and add decisions as the Board moves forward with the current initiative. Appendix C (see page 32) contains authoritative material with respect to the meaning of "accrual accounting," which is referenced in the paper.

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I. What Social Insurance Information Is Essential and How Should It Be Communicated?

The discussion of essential social insurance information should begin with SFFAS 17, *Accounting for Social Insurance*, SFFAS 25, *Reclassification of Stewardship Responsibilities and Eliminating the Current Services Assessment*, and SFFAS 26, *Presentation of Significant Assumptions for the Statement of Social Insurance: Amending SFFAS 25*. SFFAS 17, 25, and 26 establish that ***net present values (NPV) in the statement of social insurance (SOSI)*** are essential information.

In addition, during the course of the social insurance (SI) project, the Board has concluded that ***the components of the change in SOSI NPV*** are essential information. The Board is considering whether to display the components of the change within the SOSI or in a new statement.

Regarding the question of what additional essential information is needed beyond the current SOSI and changes in SOSI, the members' comments at the September 2007 FASAB meeting are relevant and are discussed in the following paragraphs.

September FASAB Meeting

The members comments at the September FASAB meeting regarding what distinguishes the estimated "economic cost" of SI from the cost of other programs, given the objective of the statement of net cost (SNC),[2] are relevant to the question of what SI information is essential. During the September meeting, a member asked about the meaning of "economic cost." However, before turning to that question, I note a question raised in September about the meaning of the term "economic cost." Although FASAB standards do not define it, the concept of economic cost is often used synonymously with the concept of accrual accounting. FASAB standards define "accrual accounting" as the process that records the effects on a reporting entity of transactions and other events and circumstances in the periods in which those transactions, events, and circumstances occur rather than only in the periods in which cash is received or paid by the entity.[3] Hence, this paper will use the term "***accrued cost***" instead of "economic cost."

Some members believe that the accrued cost of SI is the total change in the SOSI NPV. For example, if the NPV of the social insurance commitment last year were $44 trillion and this year it is $45 trillion, then the accrued cost would be $1 trillion. They did not see anything that would distinguish the accrued cost of social insurance from the accrued cost of other programs.

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[2] Statement of Federal Financial Accounting Concepts (SFFAC 2), *Entity and Display*, par. 86. According to SFFAC 2, "the main purpose of a statement of net costs is to provide an understanding of the net costs of each organization and each program that the government supports with taxes and other unearned monies. Another important purpose for the statement is to provide gross and net cost information that can be related to the amounts of outputs and outcomes for the programs and/or organization. Thus the statement of net costs should present the amounts paid, the consumption of other assets, and the incurrence of liabilities as a result of rendering services, delivering or producing goods, or carrying out other operating activities."
[3] See the FASAB *Consolidated Glossary*.

As the Board knows well, the SOSI presents the ***open group NPV***. The open group population includes everyone who will participant in the program over a 75-year period. The ***SOSI open group NPV*** includes all payroll and income taxes that will be paid by or on behalf of, and all benefits payments that will be paid to, current and future participants over 75 years.

The 75-year timeframe is derived from the Social Security Trustees Report. It is the traditional period for analysis. The 75-year timeframe is used for all primary measures noted in the Social Security Trustees' Report -- (1) the annual cost and income as a percentage of taxable payroll, (2) the trust fund ratios, (3) the actuarial balance (also as a percentage of taxable payroll), and (4) the ***open group unfunded obligation*** (expressed in present-value dollars).[4]

Also as the Board knows, the SOSI displays three age cohorts that facilitates calculation of the ***SOSI closed group NPV***, which excludes the NPV for future participants. The ***SOSI closed*** (and ***open***) ***group NPV*** include future benefits based on both past and future earnings and work in covered employment.

Some members would limit what they characterize as the ***accrued cost*** of SI programs to the portion of the change in SOSI NPV attributable to past work in covered employment.[5] Similarly, some members believe it is essential to know how much of the change in NPV is driven by things attributable to the current period on an accrual basis. Several members have said that people should be told, first, what the ***cost increment*** is for the current year on an accrual basis if social insurance were subject to a pension plan calculation; and, second, they should be told what ***the liability number*** is to which the ***cost increments*** add up. In short, they have said that the present value of benefits attributed to work already done needs to be presented separately from the present value of benefits attributed to work to be done in the future.

One member was concerned about referring to changes in the SOSI as "costs." He preferred calling the changes something else because, in his view, the term "cost" conveys a certain meaning related to the provision of goods and services, which is the stated objective of the SNC; but he does not think "cost" relates to changes in SOSI NPV. He said the SOSI does not purport to relate to that which <u>will happen</u>. It projects receipts and benefits, and it shows that Social Security and Medicare Part A cannot pay benefits in excess of their resources. He said SOSI is not trying to show accrued cost. Like a statement of sustainability, the SOSI is trying to show what <u>would happen if</u> the program continued as it is. In short, SOSI information differs from what is shown in the SNC. He noted, however, that the ***changes in the SOSI NPV*** is a valuable measure as well.

Members discussed the incurrence of a liability as a criterion for determining ***accrued cost***. One member said that the SNC relates to prior periods and captures actual expenditures, which he distinguished from other ***things that are going to be owed in the future***. He said the key filter for deciding whether an item is a cost that should flow into the SNC has been whether a

[4] 2007 Social Security Trustees' Report, p. 7.

[5] These members did not address the affect of other causes of change, e.g., interest on the obligation and changes in assumptions, but presumably the accrued cost would include all changes in NPV associated with past work in covered employment.

liability is incurred. He said changes in values should rise to the level of liabilities if they are to affect the cost statement. Some things are too uncertain to affect the SNC, for example, the prospect of an environmental disaster or military conflict. He concluded that the Board has used the liability filter to determine whether things belong on the SNC, and it comes back to that question. He needed to know whether a liability is triggered to say whether an accrued cost has been incurred. His answer would be different depending on the answer to the liability question.

Another member agreed with the liability-trigger criterion. That criterion is why he feels there is no difference between social insurance costs and other costs; and that there is a social insurance liability beyond "due and payable."

Some members expressed interest in an accrual measure that would be consistent with what the Social Security Trustees and/or the Social Security Administration (SSA) publish, rather than one unique to the FASAB, e.g., the 40-quarter/substantial eligibility measure. A member has mentioned that a measure used in *The 2007 Annual Report of the Board of Trustees of the Federal Old-age and Survivors Insurance and Federal Disability Insurance Trust Funds* ("Social Security Trustee's Report") and/or in a SSA Actuarial Note might be more generally accepted than one that is unique to the Board.

Social Security's Accrual Measures

The Social Security Trustees' Report contains both an open and a closed group accrual measure. So, too, does SSA's periodic Actuarial Note, "Unfunded Obligation and Transition Cost for the OASDI Program" ("Actuarial Note"). The Social Security Trustees' Report includes the "unfunded obligation" for both the open and closed group, while the Actuarial Note emphasizes "transition costs."

The staff concludes that, in addition to the SOSI and the changes in SOSI NPV, there is support among members for displaying ***the portion of the change in SOSI NPV attributable to past work in covered employment*** and ***the change*** in NPV due to things ***attributable to the current period on an accrual basis***. There was support for the notion that people want to see what liability-type measures would be. Some members noted that doing this would respond to a call in the comment letters and at the hearings for disclosing, if not recognizing, what the liability would be.

The following bulleted items are alternatives for such a measure.

- The ***accrued benefit obligation***, as defined in SSA's Actuarial Note, is a measure of the future benefit obligation based on past earnings and past work in covered employment as of the valuation date. Only current participants are included.[6] Future payroll taxes to be paid by the current participants and benefits attributable to earnings and work in covered employment in the future are excluded. However, any income taxes to be paid by current participants on future benefits under the current plan are subtracted. The ***accrued benefit obligation*** is a gross number; Treasury securities – or

[6] SSA Actuarial Note 2006-1, Definitions, page 3.

other assets – held by the program at beginning of the projection period are not subtracted. See ***maximum transition cost*** immediate below for the same measure net of assets.[7]

- The ***maximum transition cost***, as defined in the Actuarial Note, is the ***accrued benefit obligation***, less the Treasury securities – or other assets – held by the program at beginning of the projection period.[8]

- Because they are frequently mentioned, I note two other terms used in pension accounting: the ***accumulated benefit obligation*** and the ***projected benefit obligation***. The ***accumulated benefit obligation***, for which the abbreviation "ABO" is frequently associated, is the actuarial present value of benefits (whether vested or non-vested) attributed by the pension benefit formula to employee service rendered before a specified date and based on employee service and compensation (if applicable) prior to that date. The ***projected benefit obligation***, for which the abbreviation "PBO" is frequently associated, differs from the ***accumulated benefit obligation*** merely in that it includes assumptions about future compensation levels. For plans with flat-benefit or non-pay-related pension benefit formulas, the ***accumulated benefit obligation*** and the ***projected benefit obligation*** are the same.[9]

- The ***open group SOSI NPV*** is the difference between:

  (1) the present value of the benefits to be paid over the projection period; and,
  (2) the present value of future tax income – both payroll and income tax on benefits received – over the projection period.

  A 75-year projection period is used for the open group measure.

- The ***open group unfunded obligation***, as defined in the Social Security Trustees' Report (and also in SSA's Actuarial Note), is the same as the ***open group SOSI NPV*** described immediate above except that Treasury securities – or, theoretically, other assets – held by program at the beginning of the projection period are subtracted. According to the Trustees, the ***open group unfunded obligation*** indicates the size of the excess of cost over income over the projection period in present value dollars.[10] The

[7] The Social Security Trustees' Report does not use the term ***accrued benefit obligation***.
[8] SSA Actuarial Note 2006-1, Definitions, page 4. The Social Security Trustees' Report does not mention the ***maximum transition cost***.
[9] SFAS 87, *Employers' Accounting for Pensions*, Glossary, "Accumulated Benefit Obligation." Users of federal financial reports have asked whether a given measure of the ***SOSI NPV*** is like the ABO or the PBO. They understandably want to know how ***SOSI NPV*** relate to private sector pension accounting standards. Although care is needed when comparing pension accounting methods with methods used for the national SI program, the staff notes that it may be helpful to stipulate – since the question persists – that SSA's ***accrued benefit obligation*** is more like the PBO than the ABO. Both the ***accrued benefit obligation*** and the PBO attempt to project future wage levels, albeit for different orders of magnitude.
[10] Social Security Trustees' Report, page 41. Another primary measure used by the Trustees is the notion of ***actuarial balance***, which is the excess of cost over income as a percentage of taxable payroll. A negative actuarial balance is called the "actuarial deficit."

Social Security Trustees' Report discusses both a 75-year and an infinite horizon ***open group unfunded obligation***.[11]

- The ***closed group SOSI NPV*** (which can be calculated from the SOSI cohorts) is the same as the ***open group SOSI NPV*** except that future participants are excluded.

- The ***closed group unfunded obligation***, [12] as defined in the Social Security Trustees' Report, is computed like the ***open group unfunded obligation*** (described above), except that future participants are excluded and the projection period is extended to capture the lifetime of current participants, e.g., to 100 years rather than 75 years.[13] In addition, the difference between the ***closed group unfunded obligation*** and the ***SOSI closed group NPV***, i.e., the NPV that can be calculated from the SOSI, is merely that the Treasury securities held by the program are subtracted to derive the former but not the latter.

One member said the ***trend in the open group actuarial liability*** and the ***amount and causes of changes therein*** resonated with him. Staff assumes that this measure would be the same as the ***open group SOSI NPV***. In addition, this member said that the ***cross-over point*** and ***cash flow as a percent of GDP*** are good because economists can use them. The latter is and would continue to be required as supplementary information, i.e., RSI.

Thus, from the members' comments at the September meeting, <u>essential information</u> about social insurance that is not currently presented pursuant to FASAB standards would include the following:

1. The SOSI, which is a given but is offered here for the record, so that the list is complete.

2. The components of the changes in SOSI NPV during the reporting period (see Display 6 below). Again, this is a given but is here for the record.

3. An accumulated accrued cost measure to which the accrued cost increments add up. The term ***accrued benefit obligation*** is being used in this paper. The Board may eventually prefer another name. Several measures (and names) have been suggested above for this purpose. A decision will have to be made with respect to the question of

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[11] The 75-year ***open group unfunded obligation*** for Social Security and Medicare, Part A, was $4.7 trillion and $11.6 trillion, respectively, using a January 1, 2007, valuation date. See the 2007 Social Security Trustees' Report, p. 58-9 and Table IV.B6, p. 59; and the Medicare Trustees' Report, p. 62. The Social Security Trustees note on page 59 of the 2007 Report that extending the calculations beyond the 75-year horizon, i.e., beyond 2081 "adds $8.9 trillion ($13.6 trillion – $4.7 trillion) in present value to the amount of the unfunded obligation estimated through 2081. That is, over the infinite horizon, the OASDI open group unfunded obligation is projected to be $13.6 trillion. The $8.9 trillion increment reflects a significant financing gap projected for OASDI after 2081. Of course, the degree of uncertainty associated with estimates beyond 2081 is substantial." For Medicare, Part A, the infinite horizon adds $17.9 trillion ($29.5 trillion – $11.6 trillion). See 2007 Medicare Trustees' Report, p. 66.

[12] The SSA Actuarial Note uses the term ***closed group transition cost*** rather than ***closed group unfunded obligation***, but the methodology is the same.

what to call the accumulated accrued cost line item. The staff suggests that the criteria for deciding on the label include that (1) it reflect the measurement methodology that the Board eventually uses, and (2) it is readily and intuitively understandable to a general reader. With respect to methodology, a principal difference among alternatives is whether future taxes and benefits to the accumulated in the future are included, for example, the ***accrued benefit obligation*** vs. the ***open*** or ***closed group SOSI NPV***. The spectrum includes the following:

	Current Participants' Accumulated Accrued Benefits?	Current Participants' Future Payroll Tax Contributions & Benefits Accrued in Future?	Future Participants' Payroll Tax Contributions & Benefits Accrued in Future (over a 75-year or Infinite Horizon)?	Subtract Treasury Securities Held by Program?
Accrued benefit obligation	Yes	No	No	No
Closed group unfunded obligation	Yes	Yes	No	Yes
Closed group SOSI NPV	Yes	Yes	No	No
Open group unfunded obligation	Yes	Yes	Yes	Yes
Open group SOSI NPV	Yes	Yes	Yes	No

The change in the ***accrued benefit obligation*** caused by transactions and events attributable to the current period on an accrual basis, i.e., the accrued cost increments, also would be essential information.

4. The current SFFAS 17 RSI is also valuable information.

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[13] The ***closed group unfunded obligation*** for Social Security and Medicare, Part A, was $14.4 trillion and $11.5 trillion, respectively, using a January 1, 2007, valuation date. See the 2007 Social Security Trustees' Report, p. 60-1 and Table IV.B7, p. 61; and the 2007 Medicare Trustees' Report, p. 67.

Staff Recommendation #1 – The staff recommends that items 1 through 4 above be considered essential information, including the ***accrued benefit obligation***. The methodology used for the ***accrued benefit obligation*** isolates the accumulated accrued cost and accrued cost increments. In addition, the term would be understandable to the general reader. The term "***maximum transition cost***," which has been mentioned seems off-putting and not readily or intuitively understandable. On the other hand, it would be familiar to many Social Security analysts.

Does the Board agree with the staff's recommendation?

II. Display – How to Communicate Essential Information

Regarding how to display this essential information, i.e., "geography," the members discussed the challenge of understanding multiple financial statements and the desirability of ***a highlights document***. The Board discussed Table 1 from the CFR's executive summary, which was Exhibit F of Tab C in September. The members noted that ***a highlights document*** could capture, in one or two lines, e.g., costs and exchange revenue, net cost of operations, assets and liabilities, and social commitments, without saying one is more important than the other; and it could refer to other sections of the report where more information would be available. Some members felt it was very important to show the ***accrued social insurance numbers juxtaposed against other traditional accounting concepts*** like net operating costs, assets, and net position of the government. A member suggested that the Board construct the statements to disclose, for example, information program-by-program and/or group-by-group, and then ***summarize it separately in a cover sheet the way people are used to seeing it***. He felt that it is very helpful to explain somewhere in the report how the number is derived, that the Board is obliged to summarize in a way that brings the information together, even though the pieces are presented in various places.

One member said this information would be displayed in the ***statement of sustainability*** that the Board is developing. He envisioned the information for such a statement to be forward-looking, with different components, e.g., the traditional liabilities, social insurance responsibilities, and other exposures like PBGC liabilities and deferred maintenance.[14]

There was a concern that constraints would be placed on the preparer regarding the construction of a summary like Table 1 in the consolidated *Financial Report of the United States Government's* (CFR) executive summary. Table 1 apparently came about because the preparer had flexibility to construct a user-friendly presentation. There seemed to be a consensus among members that ***flexibility should be preserved.***

Staff concludes from comments at the September meeting that the members want to consider the following:

1. Social insurance information in a highlights presentation that links to the current basic statements. The presentation would include information regarding costs and exchange revenue, net cost of operations, assets and liabilities, and social commitments; and it could refer the reader to other sections of the report where more information would be available.

[14] Staff notes that some of the display issues are similar to those in "Phase B" of the joint FASB/IASB financial statement presentation project. Phase B topics include: (1) principles for aggregating and disaggregating information in each financial statement; (2) totals and subtotals to be reported in each financial statement (that might include categories such as business and financing): and (3) components of other comprehensive income – whether they should be recycled/reclassified to profit or loss and, if so, the characteristics of the transactions and events that should be recycled and when recycling should occur. The initial output for Phase B will be a preliminary views document expected in the second quarter of 2008.

In addition to a highlight presentation, other financial statements would be affected, as follows:

2. Additional line items on the current balance sheet, operating statement, statement of changes in net position, and SOSI.
3. Display of the components of all the changes in the SOSI NPV, either within the SOSI or in a separate statement.
4. And, possibly, additional note disclosures, e.g., for the CFR, disaggregations of the ***accrued benefit obligation*** to show the amounts for each SI program.

The following pro forma table, which is entitled "Display #1," illustrates a ***highlights document***. Other pro forma statements follow and are numbered sequentially (Display 2, Display 3, etc.). The displays are straightforward and generally familiar to the members. In some cases, a line item (or items) has been added to an existing financial statement as was done for the pro forma illustrations in the September briefing material (Displays 2, 3, 4, and 5). In other cases, a new statement is presented, but the Board has previously seen these pro forma illustrations, for example, the Alternative View's illustrative "statement of changes in SOSI amounts" (Display 6).

Display #1 – Highlights Table for Management's Discussion and Analysis

As the social Insurance project staff conceives it, the information in Display #1 immediately below would be "required supplementary information" presented in the MD&A section of the CFR. The staff proposes that the standard not require a specific format for the display but rather require specific information in a tabular form, for which the Treasury Department would choose the specific format. This would continue current flexibility.

The categorization (and placement) of the information in the pro forma illustration is, of course, very much for the purpose of discussion. The social insurance project is working in conjunction with two other projects – the fiscal sustainability and communication methods projects -- that may affect categorization and/or placement.

As stated, the pro forma illustration is based on Table 1 from the executive summary of the FY 2006 CFR, but the line items have been rearranged. The first section, entitled "Measuring Result during the Period," contains:

(1) budget receipts and outlays and the net deficit;
(2) "GAAP" expenses, earned and other revenue, and net operating costs;
(3) the increase (decrease) in the ***accrued benefit obligation*** (the change in the NPV attributable to participation during the period) and net operating cost and SI cost for the period; and,
(4) the "decrease (increase) in "fiscal imbalance" during the period. This is a placeholder. It would be consistent with what the Board decides regarding fiscal sustainability. "Fiscal imbalance" is defined in the material for the fiscal sustainability project.

The next section of the table, entitled "Financial Status at the End of the Period," contains line items for:

(1) Total assets, liabilities and net position.
(2) The ***accrued benefit obligation*** and the Treasury securities held by the program in a subsection entitled "social insurance commitments." Two things to note here: (1) The line item for Treasury securities held by the program would be useful whether or not the eventual accrued benefit obligation measure was net of assets. If it were net of assets, including this disclosure on Treasury securities would "gross up" the measure; if not, then the gross measure could be compared with assets held by the program. The usual disclaimers regarding the intra-government nature of such assets would have to be included or referenced. And, (2) the term "commitments" is not the same as the term "responsibilities" that Treasury used for this section of Table 1 in the FY 2006 CFR. The term "commitment" is used here because it denotes a stronger bond than does the term "responsibility." Some alternatives along the spectrum, e.g., "obligation," are stronger still.
(3) The ***open group unfunded obligation*** using a 75-year period. A line item for the infinite horizon could be added.
(4) In addition, a line item is included to illustrate that there would be linkage to the fiscal sustainability reporting. For example, there is a line entitled "Fiscal Imbalance **(FINAL TO BE CONSISTENT WITH FISCAL SUSTAINABILITY RECOMMEDATIONS)."** Thus, this line item is essentially a placeholder. The social insurance and fiscal sustainability projects overlap. In the spirit of brainstorming and creative thinking, the SI project staff is hoping for synergies rather than confusion.

I propose that, generally, line items in the table should cross-reference the basic financial statements, where applicable.

Display #1 – Highlights Table for Management's Discussion and Analysis

This table is based on FY 2006 CFR Executive Summary Table 1: Key Financial Indicators: FY 2004 - FY 2006			
(billions)	2006	2005	2004
MEASURING RESULTS DURING THE PERIOD			
Budget Deficit:			
Receipts	$2,407	$2,153	$1,880
Less: Outlays	(2,654)	(2,472)	(2,292)
Budget Deficit	($248)	($319)	($412)
Gross Expenses	(3,128)	(3,175)	(2,732)
Less: Earned (Program) Revenue	226	225	207
Subtotal --net cost	(2,901)	(2,950)	(2,525)
Less: Taxes & Other Revenues	2,441	2,186	1,913
Net Operating Cost	($460)	($764)	($612)
Increase (decrease) in the accrued benefit obligations (the change in the NPV attributable to participation during the period)	$ XXX	$ XXX	$ XXX
Plus: Net Operating Cost	$ XXX	$ XXX	$ XXX
Net Operating Cost and SI Cost for the Period	$ XXX	$ XXX	$ XXX
Decrease (Increase) in Fiscal Imbalance during the Period (FINAL TO BE CONSISTENT WITH FISCAL SUSTAINABILITY RECOMMEDATIONS)	**$X, XXX**	**$X,XXX**	**$X,XXX**
FINANCIAL STATUS AT THE END OF THE PERIOD			
Assets	$ 1,497	$ 1,448	$ 1,397
Less: Liabilities, comprised of:			
Debt to the Public	(4,868)	(4,624)	(4,329)
Federal Employee & Veterans Benefits	(4,679)	(4,492)	(4,062)
Other Liabilities	(866)	(799)	(716)
Net Position (Assets Net of Liabilities)	($8,917)	($8,467)	($7,710)
Social Insurance Commitments (75-year projection):			
Accrued benefit obligation – all SI programs (pertains to current participants)	$XX,XXX	$XX,XXX	$XX,XXX
Treasury securities held by all SI programs (contributed by current participants)	$ X,XXX	$ X,XXX	$ X,XXX
[The Board may wish to consider adding the infinite horizon here as well] Open Group Unfunded Obligations (75-year period)	$X,XXX	$X,XXX	$ X,XXX
Fiscal Imbalance **(FINAL TO BE CONSISTENT WITH FISCAL SUSTAINABILITY RECOMMEDATIONS)**	$ X,XXX	$ X,XXX	$ X,XXX

The following table, which would be required in a footnote, provides disaggregated amounts:

FOOTNOTE DISCLOSURE:

Accrued Benefit Obligation	2007	2006	2005	2004
Social Security	Not Avail.	$15,800	$14,500	$13,500
Medicare -- Part A	Not Avail.	Not Avail.	Not Avail.	Not Avail.
Medicare -- Part B	Not Avail.	Not Avail.	Not Avail.	Not Avail.
Medicare -- Part C	Not Avail.	Not Avail.	Not Avail.	Not Avail.
RR Retirement benefits	Not Avail.	Not Avail.	Not Avail.	Not Avail.
Other	Not Avail.	Not Avail.	Not Avail.	Not Avail.
Accrued Benefit Obligation, all SI programs	$XX,XXX	$XX,XXX	$XX,XXX	$XX,XXX

The table includes a line item for Treasury securities. I propose note disclosure similar to that immediately above for Treasury securities held by the SI programs.

Display #2 – Balance Sheet

Many members favored expanding the balance sheet display to include ***a new line item***. Some members preferred the line item with a dollar amount and some preferred no dollar amount, much like the current "commitments and contingencies" line item. In either case, the line item would refer readers to the SOSI where they could see the commitment amount in the full context of the program. There could also be a reference to the ***highlights table***.

The following is a pro forma balance sheet with line items at the bottom for the ***accrued benefit obligation*** and for Treasury securities held by the program. This a slightly abbreviated balance sheet from the FY 2006 CFR. It is also illustrative of the Social Security Administration's and other SI entities' balance sheets, except that a line item for Treasury securities would not be needed for component entities because they are reported as assets on the balance sheet.

United States Government
Balance Sheets
as of September 30, 2006, and September 30, 2005

(billions)	2006	2005
Assets:		
Cash and other monetary assets (Note 2)	$98	$86
Accounts and taxes receivable, net (Note 3).................................	69	66
Loans receivable, net (Note 4)	221	222
* * *	* * *	* * *
Total assets..	$ 1,497	$ 1,448
Stewardship property, plant, and equipment		
Stewardship Land (Note 24) and Heritage Assets (Note 25)		
Liabilities:		
Accounts payable (Note 9)	$ 58	$ 68
Federal debt securities held by the public and accrued interest……	4,868	4,624
Federal employee and veteran benefits payable (Note 11)	4,679	4,492
Environmental and disposal liabilities (Note 12)............................	305	260
Benefits due and payable (Note 13)..	129	117
Insurance program liabilities (Note 14)..	73	93
Loan guarantee liabilities (Note 4)..	66	48
Other liabilities (Note 15)	234	213
Total liabilities	10,413	9,915
Contingencies (Note 18) and Commitments (Note 19)		
Net position:		
Earmarked funds (Note 20)	419	
Non-earmarked funds...	(9,336)	
Total net position	(8,916)	(8,467)
Total liabilities and net position	$1,497	$1,448
***Social Insurance Commitments:**		
Accrued benefit obligation	$XX,XXX	$XX,XXX
Treasury securities held by the SI program	$X,XXX	$X,XXX

* See the Highlights Table and the Statement of Social Insurance for more.

Display #3 – Operating Statement and Statement of Changes in Net Position

The following pro forma operating statement is a modified version of the FY 2006 CFR "statement of operations and changes in net position." The pro forma statement below condenses FY 2006 CFR information and adds a new section at the end of the statement for "total cost attributed to the current period."

Staff intends that this pro forma statement illustrate both the governmentwide and component entity operating statements. Staff notes that the format of the CFR operating statement and component entities' operating statements differ. Following SFFAC 2, *Entity and Display* (and Circular A-136), component entities, of course, title their operating statement "statement of net cost," which displays total costs less earned/exchange revenue. Non-exchange and other financing sources are displayed on the component entities' statement on change in net position.

As staff conceives it, both the CFR and the component entities' operating statements would contain a line item such as the one shown at the bottom of the pro forma statement below. Thus, the final section of the operating statement would include a line item for the usual net cost (or net revenue), plus (or minus) the illustrated line item increase/decrease in ***accrued benefit obligation*** for the current year, and minus any increase in Treasury securities held by the programs. These three line items would capture critical changes.

Financial Report of the United States Government
Statements of Operations and Changes in Net Position
For the year ended September 30, 2006

billions	Non-earmarked funds	Earmarked funds	Consolidated
Operating Revenue and Costs			
Revenue	$ 1,532.2	$ 1,093.9	$ 2,626.1
Eliminations			(185.3)
Net revenue			2,440.8
Net cost	1,820.4	1,266.2	3,086.6
Eliminations			0.2
Net cost			3,086.8
Intragovernmental transfers	(344.3)	334.3	(10.0)
Net operating revenue or (cost) (**to equity**)	($632.5)	$162.0	($470.5)
Change in Net Position			
Net position, beginning of period	($8,714.1)	$247.2	($8,466.9)
Net operating revenue or (cost) (**to equity**)	(632.5)	162.0	(470.5)
Net position, end of period	($9,346.6)	$409.2	($8,937.4)
Total Cost Attributed to Current Year			
Net operating revenue or (cost) (**to equity)**	($632.5)	$162.0	($470.5)
Increase in accrued benefit obligation in current year		(1,114.0)	(1,114.0)
Increase (decrease) in Treasury securities		186.0	186.0
Total cost attributed to current year	($632.5)	($766.0)	($1,398.5)

Display #4 – Statement of Social Insurance

The following pro forma SOSI is a modified version of the FY 2006 CFR SOSI. First, it is abbreviated. It contains only the CFR SOSI's Social Security section. Second, staff proposes that the SOSI contain two new line items for each program's section of the CFR SOSI – and for each program's SOSI – for each program's ***accrued benefit obligation*** and holdings of Treasury securities. Third, the staff proposes that the CFR contain a final section summarizing combined totals for all SI programs. Such a section could be optional. It is not currently required by SFFAS 17.

From FY 2006 CFR -- OASDI and Medicare, Part A

United States Government

Statements of Social Insurance

(In billions of dollars)	**2006**	**************** **2005**	********UNAUDITED*********** **2004**	**2003**	**2002**
Federal Old-Age, Survivors and Disability Insurance (Social Security):					
Contributions and Earmarked Taxes from:					
Participants who have attained age 62	$ 533	$ 464	$ 411	$ 359	$ 348
Participants ages 15-61	16,568	15,290	14,388	13,576	13,048
Subtotal -- closed group	17,101	15,754	14,799	13,935	13,396
Future participants (under age 15 and births during period)	15,006	13,696	12,900	12,213	11,893
All current and future participants	32,107	29,450	27,699	26,148	25,289
Expenditures for Scheduled Future Benefits for:					
Participants who have attained age 62	5,866	5,395	4,933	4,662	4,402
Participants ages 15-61	26,211	23,942	22,418	21,015	20,210
Subtotal -- closed group	32,077	29,337	27,351	25,677	24,612
Future participants (under age 15 and births during period)	6,480	5,816	5,578	5,398	5,240
All current and future participants	$ 38,557	$ 35,153	$32,929	$31,075	$29,852
Net present value of future expenditures less future revenue (closed group)	$ 14,976	$ 13,583	$12,552	$11,742	$11,216
Net present value of future expenditures less future revenue (open group)	$ 6,450	$ 5,703	$ 5,230	$ 4,927	$ 4,563
Accrued benefit obligation	$15,800	$14,500	$13,500	$12,600	$12,200
Treasury securities held by program	$2,000	$1,800	$1,600	$1,400	$1,300

* * *

Total -- All SI Programs	**2006**	**2005**	**2004**	**2003**	**2002**
Contributions and Earmarked Taxes from:					
Participants who have attained eligibility age	$ 1,312	$ 1,178	$ 1,071	$ 774	$ 728
Participants who have not attained eligibility age	27,160	25,081	23,767	20,274	19,352
Subtotal -- closed group	28,472	26,259	24,838	21,048	20,080
Future participants	21,227	19,442	18,457	16,715	16,287
All current and future participants	49,699	45,701	43,295	37,763	36,367
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age	10,920	10,160	9,430	7,945	7,355
Participants who have not attained eligibility age	61,699	56,137	52,687	39,961	36,944
Subtotal -- closed group	72,619	66,297	62,117	47,906	44,299
Future participants	15,937	15,097	14,546	10,687	9,961
All current and future participants	$ 88,556	$ 81,394	$76,663	$58,593	$54,260
Net present value of future expenditures less future revenue (closed group)	$ 44,147	$ 40,038	$37,279	$26,858	$24,219
Net present value of future expenditures less future revenue (open group)	$ 38,857	$ 35,693	$33,368	$20,830	$17,893
Accrued benefit obligation	$ X,XXX	$ X,XXX	$X,XXX	$X,XXX	$X,XXX
Treasury securities held by program	$2,100	$1,900	$1,700	$1,500	$1,400

Display #5 – SOSI and Changes in SOSI Amounts

The next pro forma statement would combine the current SOSI information with information regarding the accrued cost portion of the SOSI NPV.

United States Government **Statement of Social Insurance** **Present Value of Long-Range (75-year) Actuarial Projections**		2006			2005	
FEDERAL OLD-AGE, SURVIVORS AND DISABILITY INSURANCE (SOCIAL SECURITY)						
Contributions and earmarked taxes from:						
Participants who have attained age 62		$ 533			$ 464	
Participants ages 15-61		16,568			15,290	
Total closed group revenues			$ 17,101			$ 15,754
Expenditures for scheduled future benefits						
Participants who have attained age 62						
Ending balance previous year	$ 5,395			$ 4,933		
Estimated net benefits attributable to work performed in current yea	238			0		
Other	233			462		
Ending balance		5,866			5,395	
Participants ages 15-61						
Ending balance previous year	23,942			22,418		
Estimated net benefits attributable to work performed in current yea	1,062			0		
Other	1,207			1,524		
Ending balance		26,211			23,942	
Total closed group benefits			32,077			29,337
Total closed group imbalance			(14,976)			(13,583)
Contributions and earmarked taxes from:						
Future participants (under age 15, new births, immigrants)		15,006			13,696	
Expenditures for scheduled future benefits						
Future participants (under age 15, new births, immigrants)		6,480			5,816	
Total surplus from future participants			8,526			7,880
Total open group imbalance			($6,450)			($5,703)

Display #6 – Separate Statement of Changes in SOSI Amounts

The next pro forma statement is a separate statement of changes in SOSI amounts that is very similar to the Alternative View. Changes in SOSI NPV will involve both the ***accrued benefit obligation*** and other components of SOSI NPV. As the staff conceives it, the statement would be disaggregated to show changes in (1) the ***accrued benefit obligation*** and (2) the obligation for all other, not-yet-accrued benefits (this is not illustrated).

Illustrative Statement of Changes in Social Insurance
For the Year Ended September 30, 20XX
(the Alternative View pro forma)
(in billions of dollars)

	Social Insurance				
	Social Security	Medicare HI	Medicare SMI	Other (e.g.,Railroad Retirement)	Total
Social Insurance, Beginning of Year	$ XXX	$ XXX	$ XXX	$ XXX	$12,000
Additional benefits accrued	XXX	XXX	XXX	XXX	XXX
Interest on the obligation	XXX	XXX	XXX	XXX	XXX
Changes in Valuation Period	XXX	XXX	XXX	XXX	XXX
Changes in Demographic Data and Assumptions	XXX	XXX	XXX	XXX	XXX
Changes in Economic Data and Assumptions	XXX	XXX	XXX	XXX	XXX
Changes in Medicare Provider Assumptions		XXX	XXX		XXX
Legislative Changes	XXX	XXX	XXX	XXX	XXX
Methodological Changes	XXX	XXX	XXX	XXX	XXX
Other changes	XXX	XXX	XXX	XXX	XXX
	X,XXX	X,XXX	X,XXX	X,XXX	X,XXX
Less: benefits paid during the period	(XX)	(XX)	(XX)	(XX)	(XX)
Net Change in Social Insurance	$ XXX	$ XXX	$ XXX	$ XXX	$ XXX

The components of the change in SOSI NPV include the following:

A. Increase in benefits. As illustrated in the Primary View pro forma SOSI and other pro forma illustrations, some of the increase in the NPV would relate to the ***accrued benefit obligation***, i.e., it would represent the present value of future benefits attributable to work in covered employment during the current period. In pension accounting, this is called normal or service cost.
B. Interest on the obligation.
C. Changes in valuation period – the SOSI is a 75-year projection. Each year a new 75-year period is projected. A year becomes the current year and last year's year 76 becomes year 75, etc. The valuation date, which is January 1, also could conceivably change, but that unlikely.

D. Assumption changes -- demographic, economic, healthcare.
E. Changes in program features (prior service costs).
F. Changes in methodology.

Recommendation #2 – Although the discussion above is not specific regarding the details of the highlights table and other displays, staff recommends this general approach.

Does the Board agree with the staff's recommendation?

Appendix A – Table of FASAB Points of Consensus

Points of Consensus

There is a consensus among members regarding the following components of a social insurance standard, which primarily involve display:

1. Retain the Statement of Social Insurance (SOSI). Some aspects of the format for the SOSI are yet to be determined, but the staff assumes that the SOSI will continue to require five years of data and therefore provide information about trends.

2. Add a statement of changes in SOSI amounts. The format for the statement of changes is yet to be determined. The Primary View proposed expanding the SOSI. The Alternative View proposed a separate statement. Mr. Reid recently suggested expanding the SOSI to explain, for example, how much of the change is due to work in covered employment in the current year, how much is due to benefits paid out during the current year, and how much to changes in assumptions.

3. Retain the SFFAS 17 required supplementary information (RSI).

4. Consider changes to the Statement of Changes in Net Position and other basic financial statements to display social insurance information. The possibilities include a new line item(s) and/or section(s) for the current statements as well as a new basic statement to bridge the Balance Sheet, Statements of Changes in Net Position and of Net Cost, and/or the SOSI.

5. Congress's ability to change a social insurance program, by itself, does not mean that obligations under the program are not a liability.

6. Proposals regarding social insurance display eventually will be explained in the context of the current FASAB accounting and reporting model. New information and displays may or may not align with this model. Alternatives will be evaluated against the elements definitions, current concepts of recognition versus disclosure, and implications for other statements in the model.

Appendix B – Table of FASAB Decisions from October 2005

	Board Majority View	Board Minority View
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	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,	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.

	Board Majority View	Board Minority View
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 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.]	but the projection is based on assumptions and estimates and may be change. Current law merely makes it a self-financing program.	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 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 members agreed with the recommendation.	No disagreement was expressed.

	Board Majority View	Board Minority View
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.		
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 acceptance in the private sector and is worth exploring for social	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.

	Board Majority View	Board Minority View
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	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 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

	Board Majority View	Board Minority View
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.		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 before weighing-in.
Question #7 – What should be displayed for social insurance on the statement of net cost, balance sheet, and other statements? **The Social Insurance project staff recommends a total amount for cost on the statement of net cost and liability on the balance sheet representing all components of accrued cost and liability. The totals could be disaggregated by, for example, age cohort, and/or by degree of uncertainty, and/or by "service cost" plus interest on the liability and actuarial gains and losses.**	The Board did not have an opportunity to address this question at this time. 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	

	Board Majority View	Board Minority View
With respect to employee pensions and other retirement benefits the FASAB precedent is to recognize all components of net cost in the year of incurrence. The conclusion has been that, for example, amortizing actuarial gains and losses over X number of years produces a "smoothing" effect that can be misleading and in the private sector has allowed the preparer to manage earnings.	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 position. They ought to flow through a statement.	
Question #8 – What should be disclosed about social insurance in the notes? **The staff recommends … to be determined.**	The Board did not have an opportunity to address this question at this time.	
Question #9 – What should be done with RR Retirement, Unemployment Insurance, and Black Lung Benefits? **Staff recommends the following:** **Railroad Retirement – analogize to OASDI and SMI.**	The Board did not have an opportunity to address this question at this time.	

	Board Majority View	Board Minority View
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 recommends 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.	No disagreement was expressed, but see Mr. Patton's issue in Question #5 above.

Appendix C – Definition of Accrual Accounting

FASAB Consolidated Glossary –

> Records the effects on a reporting entity of transactions and other events and circumstances in the periods in which those transactions, events, and circumstances occur rather than only in the periods in which cash is received or paid by the entity. Accrual accounting is concerned with an entity's acquiring of goods and services and using them to produce and distribute other goods and services. It recognizes that the buying, producing, selling, distributing, and other operations of an entity during a period, as well as other events that affect entity performance, often do not coincide with the cash receipts and payments of the period. Compare with cash accounting." See Financial Accounting Standards Board Statement of Financial Accounting Concepts (SFAC) 4, *Objectives of Financial Reporting by Nonbusiness Organizations*, paragraph 50; SFAC 6, *Elements of Financial Statements*, pars. 139-141, 144-5; and Congressional Budget Office, *Glossary of Budgetary and Economic Terms*, "Accrual Accounting."] (SFFAS 24)

SFAC 4. par. 50 –

> The information described in paragraphs 47-49 measured by accrual accounting generally provides a better indication of an organization's performance than does information about cash receipts and payments.[22] Accrual accounting attempts to record the financial effects of transactions, events, and circumstances that have cash consequences for an organization in the periods in which those transactions, events, and circumstances occur rather than in only the periods in which cash is received or paid by the organization. Accrual accounting is concerned with the process by which cash is obtained and used, not with just the beginning and end of that process. It recognizes that the acquisition of resources needed to provide services and the rendering of services by an organization during a period often do not coincide with the cash receipts and payments of the period.[23]

SFAC 6, pars. 139-141, 144-5 –

> Accrual Accounting
>
> 139. Accrual accounting attempts to record the financial effects on an entity of transactions and other events and circumstances that have cash consequences for the entity in the periods in which those transactions, events, and circumstances occur rather than only in the periods in which cash is received or paid by the entity. Accrual accounting is concerned with an entity's acquiring of goods and services and using them

[22] [omitted]

[23] Accrual accounting is concerned with the timing of recognizing transactions, events, and circumstances that have financial effects on an organization. This paragraph is not intended to prejudge specific recognition and measurement issues involved in applying accrual accounting in the nonbusiness area. For example, whether certain inflows of financial resources, such as taxes, grants, and contributions should be recognized in the period when a claim arises, when they are received, with they are appropriated for use, when they are use or when other events occur, is beyond the scope of this statement.

to produce and distribute other goods or services. It is concerned with the process by which cash expended on resources and activities is returned as more (or perhaps less) cash to the entity, not just with the beginning and end of that process. It recognizes that the buying, producing, selling, distributing, and other operations of an entity during a period, as well as other events that affect entity performance, often do not coincide with the cash receipts and payments of the period (FASB Concepts Statement No. 1, Objectives of Financial Reporting by Business Enterprises, tparagraph 44, and FASB Concepts Statement No. 4, Objectives of Financial Reporting by Nonbusiness Organizations, tparagraph 50).

140. Thus, accrual accounting is based not only on cash transactions but also on credit transactions, barter exchanges, nonreciprocal transfers of goods or services, changes in prices, changes in form of assets or liabilities, and other transactions, events, and circumstances that have cash consequences for an entity but involve no concurrent cash movement. By accounting for noncash assets, liabilities, revenues, expenses, gains, and losses, accrual accounting links an entity's operations and other transactions, events, and circumstances that affect it with its cash receipts and outlays. Accrual accounting thus provides information about an entity's assets and liabilities and changes in them that cannot be obtained by accounting for only cash receipts and outlays.

Accrual and Deferral (Including Allocation and Amortization)

141. Accrual accounting attempts to recognize noncash events and circumstances as they occur and involves not only accruals but also deferrals, including allocations and amortizations. Accrual is concerned with expected future cash receipts and payments: it is the accounting process of recognizing assets or liabilities and the related liabilities, assets, revenues, expenses, gains, or losses for amounts expected to be received or paid, usually in cash, in the future. Deferral is concerned with past cash receipts and payments—with prepayments received (often described as collected in advance) or paid: it is the accounting process of recognizing a liability resulting from a current cash receipt (or the equivalent) or an asset resulting from a current cash payment (or the equivalent) with deferred recognition of revenues, expenses, gains, or losses. Their recognition is deferred until the obligation underlying the liability is partly or wholly satisfied [54] or until the future economic benefit underlying the asset is partly or wholly used or lost. Common examples of accruals include purchases and sales of goods or services on account, interest, rent (not yet paid), wages and salaries, taxes, and decreases and increases in marketable securities accounted for at lower of cost and market. Common examples of deferrals include prepaid insurance and unearned subscriptions.[55]

Recognition, Matching, and Allocation

144. Accrual accounting recognizes numerous noncash assets, liabilities, and transactions and other events that affect them (paragraphs 139-141). Thus, a major difference between accrual accounting and accounting based on cash receipts and outlays is timing of recognition of revenues, expenses, gains, and losses. …

[54] [omitted]
[55] [omitted]

145. Accrual accounting uses accrual, deferral, and allocation procedures whose goal is to relate revenues, expenses, gains, and losses to periods to reflect an entity's performance during a period instead of merely listing its cash receipts and outlays. Thus, recognition of revenues, expenses, gains, and losses and the related increments or decrements in assets and liabilities—including matching of costs and revenues, allocation, and amortization—is the essence of using accrual accounting to measure performance of entities. The goal of accrual accounting is to account in the periods in which they occur for the effects on an entity of transactions and other events and circumstances, to the extent that those financial effects are recognizable and measurable.

Congressional Budget Office, *Glossary of Budgetary and Economic Terms*

Accrual Accounting: A system of accounting in which revenues are recorded when earned and outlays are recorded when goods are received or services performed, even though the actual receipt of revenues and payment for goods or services may occur, in whole or in part, at a different time. Compare with **cash accounting**.