FASAB

Federal Accounting Standards Advisory Board

April 5, 2012

Memorandum

To: Members of the Board

From: Melissa Loughan, Assistant Director

Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subj: **Federal Reporting Entity--Tab B**[1]

MEETING OBJECTIVES

- To consider the component entity reporting section of the Exposure Draft (ED) and identify any remaining member concerns with other areas of the ED.

The objectives for the April Board meeting are to consider the developed component entity reporting section of the Exposure Draft (ED) and approve changes since the last meeting to the government-wide portions of the Draft ED. Staff would also like to identify any remaining member concerns with any other areas of the ED. (Note: the Related Party section of the ED will be provided for the June meeting.)

BRIEFING MATERIAL

The transmittal memorandum includes a discussion of issues and recommendations beginning on page 3 under Staff Analysis and Recommendations. A full list of Questions for the Board appears on page 8. In addition, the following items are attached:

- Attachment 1: Draft Exposure Draft (Related Party section is omitted.)

[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.

You may electronically access all of the briefing material at http://www.fasab.gov/board-activities/meeting/briefing-materials/

BACKGROUND

As you may recall at the February meeting, the Board deliberated several open issues related to the federal reporting entity project. The Board decided the following during February:

- The Board did not recommend any specific changes to the inclusion principles based on the presentation regarding the Federal Reserve pro forma disclosures. There were suggestions regarding the disclosures and examples of information that staff will consider in determining if the disclosure requirements could be enhanced.
- The Board agreed the standard should remain silent on uses of an other comprehensive basis of accounting for non-core entity disclosures and if there are differences with GAAP, it will be up to the professional judgment of the auditor and preparer to determine if they are significant.
- The Board agreed to deleting the phrase “access the organization’s assets” from par. 28b.
- The Board agreed further discussion of related parties will be addressed in conjunction with the component reporting entity phase within the next few meetings.
- The Board members unanimously agreed with the staff recommendation to further develop the administratively assigned approach for component reporting entities.

NEXT STEPS

Staff plans to address Related Party in June along with any other issues identified by the Board. The goal is to have a complete ED by the August 2012 meeting.

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MEMBER FEEDBACK

If you require additional information or wish to suggest another alternative not considered in the staff proposal, please contact staff as soon as possible. In most cases, staff would be able to respond to your request for information and prepare to discuss your suggestions with the Board, as needed, in advance of the meeting. If you have any questions or comments prior to the meeting, please contact me by telephone at 202-512-5976 or by e-mail at loughanm@fasab.gov with a cc to paynew@fasab.gov.

STAFF ANALYSIS AND RECOMMENDATIONS

1. <u>Component Reporting Entity Language</u>

At the February meeting, the Board unanimously agreed with the staff recommendation to further develop the administratively assigned approach for component reporting entities.

In developing the component reporting language, staff met with representatives from independent public accounting firms to gather feedback from the audit perspective regarding how difficult it would be for component reporting entities to ensure all core and non-core entities were identified. Staff also requested input on the clarity of the guidance, possible processes needed to identify organizations to include in reports, the magnitude of the likely change from current processes, and whether such changes might significantly increase audit effort and, therefore, cost.

The participants recognized there would be an initial cost but believed this was consistent with the implementation of any new standard or the initial consideration of the changes from a concept statement to a standard. The participants also recognized the increased cost is dependent upon the agency reporting, staff, legal counsel, complexity of the agency and prior results. The participants believed a common path could be established to consider a complete universe of organizations but it would require an across the government process and effort. The participants believed with coordinated guidance the approach for component reporting entities under consideration by the Board was reasonable.

Certain participants suggested a government-wide or other broad based, field test of the proposed standards. Staff questions whether such a large commitment of resources during the development of a <u>proposed</u> standard would be useful absent an audit or other assessment of the field test. Field tests – formal and informal - have been successful for specific issues such as natural resources and earmarked funds but have not previously been conducted across government. The cost benefit of performing field tests on a large scale during the exposure draft stage is questionable. Instead, a coordinated implementation approach guided by the central agencies during a long implementation period may yield better results, attain the goal of consistent application, and allow for development of any needed GAAP implementation guidance. Therefore, staff recommends an implementation period of 4 years.

See paragraphs 51-60 of the Draft ED for the proposed language for the component reporting entity.

As noted in the changes, much of the additional language focuses on criteria for those organizations it would be misleading to include. Staff also captured the notion a non-core entity can be included in more than one component reporting entity if administrative assignments have been made to multiple component reporting entities.

After further consideration, staff determined the same consolidation and disclosure requirements should apply to the Component Reporting Entity and Government-wide Reporting Entity. Therefore staff put the Component Reporting Entity section before the Consolidation and Disclosure requirements. Staff also slightly revised the wording so that section would apply to both because the factors, objectives and disclosures would be the same for non-core at the component and government-wide levels.

Staff also shared the Draft language with the Federal Entity task force for their comment on the clarity of the guidance provided for component reporting entities and any feedback regarding application. The members also provided additional comments, most of which were supportive. They believed the ED and flowchart were well written and clear and would provide for increased transparency and accountability.

Question 1 for the Board:

Does the board agree:

a) **with the proposed language for the component reporting entity section at paragraphs 51-60 of attachment 1?**
b) **that the disclosure requirements should be the same at the component and government-wide levels (see paragraphs 61-74)?**
c) **That an implementation period of 4 years is appropriate?**

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2. Updated Exposure Draft for Decisions at December Meeting and Other Changes

The goal of the session is to approve changes incorporated into the ED as well as identify any remaining member concerns with the ED. As you will see in the Marked Version of the ED, staff updated the document for the decisions made at the February meeting.

The Board did not recommend any specific changes to the inclusion principles based on the presentation regarding the Federal Reserve pro forma disclosures. However, there were suggestions regarding the disclosures and examples of information and staff was requested to consider those in determining if the disclosure requirements could be enhanced. Staff made the following changes to the ED:

Staff revised the "Disclosures for Non-core Entities" to emphasize the aggregation of information, referencing other disclosures when possible, additional focus on risk and other enhancements. Staff believes the revised standards for the non-core entity disclosure section will be helpful for complex relationships being described, transactions affecting multiple assets and liabilities being reported, and promote an integrated set of disclosures.

The revised wording is as follows and can be found in the ED par. 68-69:

> "In addition to the factors presented in par. 67 regarding the extent of disclosures, both qualitative and quantitative factors should be considered in determining whether the disclosures for a non-core entity should be presented separately due to its significance or aggregated with other non-core entities. If disclosures are aggregated, aggregation may be based on non-core entity type, or class, investment type, or a particular type of event deemed significant to the reporting entity.
>
> Disclosures should be integrated, concise, meaningful and transparent. Integration is accomplished by incorporating references to relevant disclosures elsewhere in the GPFFR with the required non-core entity disclosures or by providing a single comprehensive disclosure regarding the non-core entity and related balances. For example, reference may be made to a disclosure regarding investments in the non-core entity."

Staff also expanded the description of the Future Exposures objectives as follows (see par. 70 c. in the Draft ED):

> ***Future exposures:*** A description of financial and non-financial risks and potential benefits and, if possible, the amount of the federal government's exposure to gains and losses from the past or future operations of the non-core entity

Staff also made various changes to the examples of information to improve focus on the objectives, clarify and streamline. See par. 71 of the Draft ED.

In addition, staff incorporated other changes most of which were editorial in nature, but some may be significant as they relate to important aspects of the Draft ED. Staff includes those here for your reference:

- Added a footnote to the first control indicator in paragraph 27 “establish or amend the fundamental purpose and mission of the organization, which may include authorizing the organization to exercise sovereign power of the federal government and requiring the organization to carry out federal missions and objectives” to address a concern noted by a Board member and shared by staff that Title 36 organizations like the Boy Scouts should not be automatically included based on the charter.

  The footnote states: “Congressionally chartered nonprofit organizations identified under Title 36, Subtitle II and III, should not be included solely because amendments to their federal charter must be enacted through legislation. Instead, such organizations should be included only if they meet the indicators in paragraph 28 or another indicator in this paragraph.”

  Staff consulted with counsel on the footnote. Although counsel did not object to the accuracy of the footnote and did not have issue with it being added, there was a question as to whether it was needed because counsel explained Congress can’t change these particular types of charters to be inconsistent with their state articles of incorporation. If they did and the organization performed, the organization would be in violation with its state articles of incorporation which may result in other consequences. The federal charter is more ceremonial. That is, the federal government has elected to recognize certain organizations that serve a patriotic or national purpose/mission.

  Staff believes the footnote may assist preparers in the analysis, while also noting the other indicators should be considered. Therefore, if an organization meets the other control indicators it would be included.

  Staff also notes the Congressional Research Service Report RL 30340 provides the following about federal charters which may be relevant:

  …because federal charters are laws of the US, they may only be amended by another law of the US. If an organization seeks to alter its primary purpose or change a provision in its charter, even a minor provision, it must return to Congress and subject its request to the full legislative process. While the process is generally routine, there are occasions when making even minor legislative changes in the charter may open the organizations to challenge from the outside.” (CRS RL30340, page 8)

The standards would include organizations where the federal government can establish or amend the fundamental purpose and mission of the organization. While Congress doesn't seem to initiate changes to charters, some may think the fact that once chartered a Title 36 corporation may not change its federal charter, including its primary purpose, without legislation makes it controlled. The footnote should prevent this conclusion.

- Added "Exemption by statute from laws or regulations dealing with the federal budget, funds, personnel, ethics, acquisition, property, or works" as a characteristic for governance to the Quasi Governmental and/or Financially Independent Entities to address how Congress often exempts certain organizations from certain laws or regulations thereby giving the organization operational authority.

- Developed the Executive Summary

- Ensured consistency with terminology throughout the document

Question 2 for the Board:

Does the Board have any questions or comments on the proposed changes referenced above or on any of the ones noted throughout the ED?

QUESTIONS FOR THE BOARD

1. Does the board agree:

- **a) with the proposed language for the component reporting entity section at paragraphs 51-60 of attachment 1?**
- **b) that the disclosure requirements should be the same at the component and government-wide levels (see paragraphs 61-74)?**
- **c) That an implementation period of 4 years is appropriate?**

2. Does the Board have any questions or comments on the proposed changes referenced above or on any of the ones noted throughout the ED?

Federal Accounting Standards Advisory Board

Identifying and Reporting upon Organizations to Include in General Purpose Federal Financial Reports

Statement of Federal Financial Accounting Standards

Exposure Draft

Written comments are requested by Date 90 days after issuance

Month Date, Year

Working Draft – Comments are Not Requested on This Draft

THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD

The Secretary of the Treasury, the Director of the Office of Management and Budget (OMB), and the Comptroller General, established the Federal Accounting Standards Advisory Board (FASAB or "the Board) in October 1990. FASAB is responsible for promulgating accounting standards for the United States Government. These standards are recognized as generally accepted accounting principles (GAAP) for the federal government.

An accounting standard is typically formulated initially as a proposal after considering the financial and budgetary information needs of citizens (including the news media, state and local legislators, analysts from private firms, academe, and elsewhere), Congress, federal executives, federal program managers, and other users of federal financial information. The proposed standards are published in an exposure draft for public comment. In some cases, a discussion memorandum, invitation for comment, or preliminary views document may be published before an exposure draft is published on a specific topic. A public hearing is sometimes held to receive oral comments in addition to written comments. The Board considers comments and decides whether to adopt the proposed standard with or without modification. After review by the three officials who sponsor FASAB, the Board publishes adopted standards in a Statement of Federal Financial Accounting Standards. The Board follows a similar process for Statements of Federal Financial Accounting Concepts, which guide the Board in developing accounting standards and formulating the framework for federal accounting and reporting.

Additional background information is available from the FASAB or its website:

- "Memorandum of Understanding among the Government Accountability Office, the Department of the Treasury, and the Office of Management and Budget, on Federal Government Accounting Standards and a Federal Accounting Standards Advisory Board."

- "Mission Statement: Federal Accounting Standards Advisory Board", exposure drafts, Statements of Federal Financial Accounting Standards and Concepts, FASAB newsletters, and other items of interest are posted on FASAB's website at: www.fasab.gov.

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Federal Accounting Standards Advisory Board

September 30, 2012

TO: ALL WHO USE, PREPARE, AND AUDIT FEDERAL FINANCIAL INFORMATION

The Federal Accounting Standards Advisory Board (FASAB or the Board) is requesting comments on the exposure draft of a proposed Statement of Federal Financial Accounting Standards entitled, Identifying and Reporting upon Organizations to Include in General Purpose Federal Financial Reports. Specific questions for your consideration appear on page 7 but you are welcome to comment on any aspect of this proposal. If you do not agree with the proposed approach, your response would be more helpful to the Board if you explain the reasons for your position and any alternative you propose. Responses are requested by January 25, 2012.

All comments received by the FASAB are considered public information. Those comments may be posted to the FASAB's website and will be included in the project's public record.

We have experienced delays in mail delivery due to increased screening procedures. Therefore, please provide your comments in electronic form. Responses in electronic form should be sent by e-mail to fasab@fasab.gov. If you are unable to provide electronic delivery, we urge you to fax the comments to (202) 512-7366. Please follow up by mailing your comments to:

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

The Board's rules of procedure provide that it may hold one or more public hearings on any exposure draft. A public hearing has been scheduled at 9:00 AM on February 27, 2013, in Room 7C13 at the GAO Building, 441 G Street, NW, Washington, D.C.

Tom L. Allen

Chairman

Executive Summary

What is the Board proposing?

The Board is proposing guidance to ensure that all organizations for which elected officials are accountable are included in general purpose federal financial reports (GPFFR). This exposure draft (ED) provides inclusion principles to guide preparers in determining what organizations are required to be included in their GPFFR. The government-wide GPFFR should include all organizations (1) for which elected officials establish the budget, (2) owned by the federal government, and (3) controlled by the federal government with the expectation of benefits or risk of loss. .

This ED also provides criteria for assessing whether such entities are core or non-core entities, what organizations are included in each component reporting entity GPFFR, and what information should be presented. The Board proposes each component reporting entity include all organizations for which it is accountable; that includes all core and non-core entities administratively assigned to it.

The Board proposes financial statements of core entities be consolidated and information about non-core entities be disclosed in the GPFFRs. The Statement allows flexibility in the disclosures as long as the disclosures meet the objectives described in ED. The objectives provide information about the relationship with the non-core entity, relevant activity during the reporting period, and future exposures to risks and rewards.

Related party-open issue TBD in June.

The proposed Statement would be effective for periods beginning after September 30, 20XX. Earlier implementation is encouraged.

How would this proposal improve federal financial reporting and contribute to meeting the federal financial reporting objectives?

This Statement would improve federal financial reporting by identifying organizations that should be included in the financial reports of the government-wide reporting entity and component reporting entities. This will ensure that users of GPFFR are provided with comprehensive financial information about federal reporting entities and their involvements so that federal financial reporting objectives are met.

In meeting the *Objectives of Federal Financial Reporting* identifying the organizations for inclusion in the government-wide reporting entity and component reporting entities are critical to creating transparent reports to support accountability. As a democracy, elected officials are to be held accountable to the public and financial statements

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provide them with a means of doing so.[1] In order to achieve accountability, the content and structure of the financial reports should be clear, complete and comprehensive to citizens.

[1] Par. 74, SFFAC 1, *Objectives of Federal Financial Reporting.*

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Questions for Respondents

The FASAB encourages you to become familiar with all proposals in the Statement before responding to the questions in this section. In addition to the questions below, the Board also would welcome your comments on other aspects of the proposed Statement.

The Board believes that this proposal would improve federal financial reporting and contribute to meeting the federal financial reporting objectives. The Board has considered the perceived costs associated with this proposal. In responding, please consider the expected benefits and perceived costs and communicate any concerns that you may have in regard to implementing this proposal.

Because the proposals may be modified before a final Statement is issued, it is important that you comment on proposals that you favor as well as any that you do not favor. Comments that include the reasons for your views will be especially appreciated.

The questions in this section are available in a Word file for your use at www.fasab.gov/exposure.html. Your responses should be sent by e-mail to fasab@fasab.gov. If you are unable to respond electronically, please fax your responses to (202) 512-7366 and follow up by mailing your responses to:

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

All responses are requested by January 25, 2012.

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Q1. The Board is proposing three inclusion principles for an organization to be included in the government-wide report:

- An organization with an account or accounts listed in the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account* unless the organization is a non-federal organization receiving federal financial assistance.
- When the federal government holds a majority ownership.
- An organization that is controlled by the federal government with the expectation of benefits or risk of loss.

In addition, the Board is proposing that an organization be included if it would be misleading to exclude it even though it does not meet one of the three inclusion principles.

Refer to paragraphs 18-33 of the proposed standards and paragraphs A14- A32 in Appendix A - Basis for Conclusions for a discussion and related explanation.

a. Do you agree or disagree with the inclusion principles? Please provide the rationale for your answer.

b. Do you believe the inclusion principles, and related definitions and indicators, are helpful and clear? Please provide the rationale for your answer.

c. Do you agree or disagree with the addition of a *Misleading to Exclude principle*? Please provide the rationale for your answer.

Q2. The Board proposes that two types of entities are included in general purpose federal financial reports: core entities and non-core entities. Core entities are (1) generally taxpayer supported as evidenced by their inclusion in the budget, (2) being governed by the Congress and/or the President, (3) imposing or may impose risks and rewards on the taxpayer, and/or (4) providing core federal government goods and services on a non-market basis. In contrast, non-core entities are those that (1) receive limited or no taxpayer support, (2) have less direct involvement by the Congress and the President, (3) are more likely to provide market based goods and services, and/or (4) impose limited risks and rewards on the taxpayers.

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The Board proposes core entities be consolidated in the government-wide financial statements. The Board proposes that information about non-core entities be disclosed in the government-wide report. The Statement allows flexibility in the disclosures as long as the disclosures meet the objectives described in Disclosures for Non-core Entities after considering the Factors in Determining Non-Core Entity Disclosures.

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Refer to paragraphs 35- 50 and 61-62 of the proposed standards and paragraphs A35-A50 and A63-A74 in Appendix A - Basis for Conclusions for a discussion and related explanation.

a. Do you agree or disagree with the distinction between core and non-core entity attributes? Please provide the rationale for your answer.

b. Do you agree or disagree with the requirements for reporting on core and non-core entities? Please provide the rationale for your answer.

Q3. The Statement would require consolidation of FASAB and FASB based information without conversion for core entities.

Refer to paragraph 62 of the proposed standards and paragraphs A58-A62 A62 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree with the above referenced requirement? Please provide the rationale for your answers.

Q4. The Board proposes each component reporting entity include all organizations for which it is accountable; that includes all core and non-core entities administratively assigned to it, and non-core entities with which it has a comprehensive relationship. Administrative assignments can be identified by evaluating: the scope of the budget and budget approval process, whether accountability is established within a component entity, and other significant relationship considerations.

Refer to paragraphs 51-60 of the proposed standards and paragraphs A51-A54 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree with the above referenced requirement? Please provide the rationale for your answers.

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Q5. SFFAC 2 identified certain entities or types of entities (the Federal Reserve System, Government Sponsored Enterprises and Bailout Entities) that should not be considered part of the government-wide report entity. The Board is proposing new principles that can be applied to the entities previously excluded and conclusions reached to consider the entities as core or non-core entities, which would affect the manner in which they are included in the general purpose federal financial reports. Therefore, SFFAC 2 is being amended to remove those provisions.

Refer to paragraph A75 in Appendix A - Basis for Conclusions for a discussion and related explanation.

Do you agree or disagree? Please provide the rationale for your answer.

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Q6. Related Party Question-- open issue TBD in June.

Q7. Are there other unique situations that should be addressed within this Statement? Please explain fully and also how the situation is not addressed by this Statement when considered in its entirety.

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Introduction

Purpose

1. The federal government and its relationships with organizations have become increasingly complex. Notwithstanding these complexities, general purpose federal financial reports[2] (GPFFR) for the government-wide reporting entity should be broad enough to report the Congress and/or the President's accountability for those organizations. In addition, component reporting entity reports should allow the Congress and the President to hold management accountable for implementation of public policy decisions. Although Statement of Federal Financial Accounting Concepts (SFFAC) 2, *Entity and Display*, addresses identifying reporting entities and criteria for including components in a reporting entity, questions have continued in this area indicating the need for standards.[3] To meet federal financial reporting objectives, it is important to develop standards that can be used to identify organizations that should be included in the financial reports of the government-wide reporting entity and each component reporting entity.

2. This Statement guides preparers of GPFFRs in determining what organizations are required to be included in the financial reports, whether such entities are core or non-core, and what information should be presented. This guidance will ensure that users of GPFFRs are provided with comprehensive financial information about federal reporting entities and their involvements so that federal financial reporting objectives are met.

3. The guidance recognizes it is necessary to determine the substance of the relationship between the federal government and an organization as often that may not be reflected by an organization's legal form. As such, the legal form or designation of an organization does not always determine whether it should be included in the government-wide reporting entity. Even in cases where legislation indicates an organization is "not an agency or instrumentality" of the federal government, the organization should be assessed against the guidance contained in this Statement to determine whether it should be included in the reporting entity. Inclusion is not determined by the legal form of an organization;

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[2] The term "general purpose federal financial report" is used throughout this Statement as a generic term to refer to the report that contains the entity's financial statements that are prepared pursuant to generally accepted accounting principles. In the federal government, the report for the U.S. government-wide reporting entity is known as the Financial Report of the U.S. Government and for component reporting entities it is usually called the Performance and Accountability Report, the Agency Financial Report, or the Annual Management Report.

[3] SFFAC 2 is a Concepts Statement and is considered Other Accounting Literature. See SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles (GAAP) Including the Application of Standards Issued by FASB* for more information regarding the hierarchy.

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nor does inclusion change the legal form of an organization. Rather, inclusion is an indication of the need for accountability given the nature of the relationship between the federal government and the organization.

Materiality

4. The provisions of this Statement need not be applied to immaterial items. The determination of whether an item is material depends on the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement.

Proposed Standards

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<#>The proposed standards are effective for periods beginning after September 30, 20XX. Earlier implementation is encouraged.
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Scope and Applicability

5. This Statement applies to federal entities that prepare general purpose federal financial reports (GPFFR) in conformance with generally accepted accounting principles (GAAP) as defined by paragraphs 5 through 8 of Statement of Federal Financial Accounting Standards (SFFAS) 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

6. This Statement does not require any entity to prepare and issue GPFFRs. The purpose of this Statement is to enable entities preparing and issuing GPFFRs to determine:

   a. whether SFFAS 34 is applicable to an organization,

   b. what organizations should be included in the GPFFR of entities applying SFFAS 34,

   c. what information should be presented for organizations included in the GPFFR, and

   d. what, disclosures, if any, are needed regarding related parties.

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Definitions

Definitions in paragraphs 7 through 10 are presented first because of their importance in understanding the Statement. Other terms shown in boldface type the first time they appear in this document are presented in the Glossary at Appendix C. Respondents to this proposal may want to examine all definitions before reviewing the Statement and Basis for Conclusions.

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7. **Reporting Entity** The term "reporting entity" refers to both the government-wide reporting entity and component reporting entities (see definitions below) that issue a GPFFR because either there is a statutory or administrative requirement to prepare a GPFFR or they choose to prepare one.

   Statement of Federal Financial Accounting Concepts (SFFAC) 2 provides criteria for an entity to be a reporting entity.[4] The criteria focus on whether an entity should issue GPFFRs and include that a reporting entity's:

   a. management is responsible for controlling and deploying resources, producing outputs and outcomes, and executing the budget or a portion thereof (assuming that the entity is included in the budget), and is held accountable for the entity's performance.

   b. financial statements would provide a meaningful representation of operations and financial condition.

   c. financial information could be used by interested parties to help them make resource allocation and other decisions and hold the entity accountable.

   SFFAC 2 further provides that a GPFFR should provide "all the information that is relevant to the reporting entity, subject to cost and time constraints." Therefore, a reporting entity's GPFFR should include information regarding all organizations for which it is accountable.

8. **Government-wide Reporting Entity** The government-wide reporting entity's GPFFR includes all organizations for which the Congress and/or the President are accountable based on principles established in this Statement.

[4] SFFAC 2, par. 29-37, provides a discussion on Identifying the Reporting Entity for General Purpose Financial Reporting.

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9. **Component Reporting Entity** "Component reporting entity" is used broadly to refer to a reporting entity within a larger reporting entity.[5] Examples of component reporting entities include entities such as executive departments, independent agencies, government corporations, legislative agencies, and federal courts. Component reporting entities would also include sub-components (those components that are included in the GPFFR of a larger reporting entity) that may themselves prepare GPFFRs. One example is a bureau of a larger department that prepares stand alone GPFFR. Other examples include commercial functions, revolving funds, and/or other accounts for which GPFFRs are prepared.

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10. **Control with expected benefits or risk of loss** Control with expected benefits or risk of loss is the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to obtain financial resources or non-financial benefits[6] or be obligated to provide financial support or assume financial obligations.

Organizational Approach to Defining Boundaries

11. The federal government is unique because its constitutionally established powers, motivations, and functions are different from those of all other organizations. It is an extremely complex organization responsible for the common defense and general welfare of the Nation. Although there are other perspectives,[7] such as a program perspective, an organizational approach was established in SFFAC 2[8] as the most appropriate perspective for understanding the composition of the federal government. SFFAC 2 established GPFFRs should include the aggregation of organizations for which the federal government is financially accountable as well as other organizations for which the nature and significance of their relationship with the government are such that their exclusion would cause the federal government's financial statements to be misleading or incomplete.

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12. Accountability demands comprehensive reporting. To provide comprehensive reporting, the federal government must report on organizations that serve varied purposes and have complex governance structures and finances. Some differences in purposes and governance structures require differences in

[5] The larger reporting entity could be the government-wide reporting entity or another component reporting entity.

[6] For example, a non-financial benefit would be one where the federal government benefits from a service being provided to it or on its behalf.

[7] SFFAC 2, par. 13-28 discusses the budget and program perspectives of the federal government, as well as the intertwining of the perspectives.

[8] SFFAC 2, par. 31-38.

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presentation of financial information. For example, certain organizational distinctions must be maintained for financial reports to meet the reporting objectives established in SFFAC 1. In such cases, disclosures about the organization rather than financial information consolidated across all organizations may better meet these objectives.

13. Thus, decisions about reporting entities are taken in two steps – first, determining what organizations are to be included in the GPFFR and second, identifying the appropriate means to present relevant information about the organizations.

14. This Statement first establishes the principles for including organizations in the government-wide GPFFR (see Principles for Inclusion in the Government-wide GPFFR) then a distinction will be made between core entities and non-core entities (see section 'Organizations - Core Entities and Non-core Entities' which describes these types of entities).

15. This statement also establishes that component reporting entities must identify and include in their GPFFRs all core and non-core entities for which they are accountable so that both the component reporting entity and government-wide GPFFRs are complete.

16. Lastly, the presentation of financial information based on those decisions is addressed (see Reporting Entity Consolidation and Disclosure).

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Principles for Inclusion in the Government-wide GPFFR

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17. To determine which organizations should be included[9] in the government-wide GPFFR, this Statement provides three principles for inclusion and also requires inclusion of organizations if it would be misleading to exclude them (see par.33).

18. An organization meeting any of the three principles below is included in the government-wide GPFFR:

    a. In the Budget

    b. Majority Ownership Interest

    c. Control with Expected Benefits or Risk of Loss

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[9] 'Included' means an organization's information is either consolidated or disclosed.

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In the Budget

19. An organization with an account or accounts listed in the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account* should be included in the government-wide GPFFR unless it is a non-federal organization receiving federal financial assistance.[10] Any listed non-federal organizations receiving federal financial assistance should be assessed against the next two principles (*Majority Ownership Interest* and *Control with Expected Benefits or Risk of Loss*) to determine if they should be included in the government-wide GPFFR.

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Majority Ownership Interest

20. The federal government (directly or through its components) may have an ownership interest[11] in an organization. An ownership interest is a legal claim on the net residual assets of an organization such as holding shares or other formal equity instruments. The holding of an ownership interest often entitles the holder to an interest in voting rights, but not always.

21. Majority ownership interest exists with over 50% of the voting rights or net residual assets[12] of an organization. When the federal government holds a majority ownership in an organization it should be included in the government-wide GPFFR.[13]

Control with Expected Benefits or Risk of Loss

22. An organization that is controlled by the federal government with the expectation of benefits or risk of loss should be included in the government-wide GPFFR. For these purposes, such control is defined as follows:

Control with expected benefits or risk of loss is the power to impose will on and/or govern the financial and/or operating policies of another organization with

[10] As defined by the Single Audit Act Amendments of 1996, federal financial assistance is assistance that non-federal organizations receive or administer in the form of grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, or other assistance.

[11] 'Ownership interest' is the possession of substantially all of the benefits and risks incident to ownership. *FASAB Glossary FASAB Pronouncements as Amended as of June 30, 2011.*

[12] For example, the federal government may hold more equity in preferred stock than all other stockholders but the preferred stock may be non-voting.

[13] Ownership interests 50% or less should be accounted for in accordance with the appropriate accounting standards per the GAAP hierarchy. However, the entity should still be assessed against the control inclusion principle and the misleading to exclude principle.

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the potential to obtain financial resources or non-financial[14] benefits or be obligated to provide financial support or assume financial obligations. Both the power and either the expected benefit or risk of loss aspects of the definition should be met to justify inclusion of an organization. Hereafter, control with expected benefits or risk of loss is referred to as "control."

23. Control refers to the ability to control and should be assessed at the reporting date regardless of the federal government's ability to change it in the future. In determining if control exists, it is necessary to determine the substance of the relationship between the federal government and the organization as it may not be completely reflected by the legal form of the relationship.

24. Control does not necessarily mean the federal government has responsibility for the management of the day-to-day operations of an organization. Rather, it is the federal government's authority to determine or influence the policies governing those activities that indicates control.

25. Determining whether control exists requires the application of professional judgment. The federal government achieves its objectives through a wide range of organizations which individually will fall on a continuum. At one end of the continuum, it will be clear that an organization does not have the power to act independently and is controlled by the federal government—such as an executive department. At the other end, the organization will have the power to act independently and, while the federal government may have a level of influence, it will be clear that it does not have control—such as a state government.

Indicators of Control

26. As discussed in the following paragraphs, there are indicators that should be considered in determining whether the federal government controls an organization. As noted above, consideration needs to be given to the nature of the relationship between the federal government and the organization and judgment applied to determine whether control exists.

27. Certain indicators provide persuasive evidence that control exists. These indicators provide strong evidence of control, so meeting any one would typically mean control is present. However; the absence of any does not lead to a

[14] For example, a non-financial benefit would arise when the federal government receives a service or a service is provided to others on its behalf.

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presumption that control is not present. These indicators are when the federal government has the authority to:

a. establish or amend the fundamental purpose and mission of the organization,[15] which may include authorizing the organization to exercise sovereign power of the federal government and requiring the organization to carry out federal missions and objectives;

b. unilaterally appoint or remove a majority of the governing board members;

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c. direct the governing body on the financial and operating policies of the organization; or

d. unilaterally dissolve the organization thereby having access to the assets and responsibility for the obligations.

28. Other indicators provide evidence that control exists, but must be considered in the aggregate and often require the application of professional judgment in assessing. These indicators are when the federal government has the ability to:

a. provide significant input into the appointment of members of the governing body of the organization or being involved in the appointment or removal of a significant number of members;

b. direct the ongoing use of the organization's assets;

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c. appoint or remove key executives or personnel;

d. approve the budgets or business plans for the organization;

e. require audits;

f. veto, overrule, or modify governing board decisions or otherwise significantly influence normal operations;

g. finance the deficits of, provide financial support to, or settle liabilities of the organization;

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[15] Congressionally chartered nonprofit organizations identified under Title 36, Subtitle II and III, should not be included solely because amendments to their federal charter must be enacted through legislation. Instead, such organizations should be included only if they meet the indicators in paragraph 28 or another indicator in this paragraph.

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h. direct the organization to work with the government to provide services to taxpayers which may include determining the outcome or disposition of matters affecting the recipients of services;

i. establish, rescind, or amend the organization's management policies;

j. establish limits or restrictions on borrowing and investments of the organization; or

k. restrict the capacity to generate revenue of the organization, especially the sources of revenue.

Situations Where Control Does Not Exist

29. Because of the uniqueness of the federal government, control would not be inferred from either:

    a. authority to exercise regulatory powers over an organization; or

    b. economic dependency of the organization on the federal government.

30. The federal government has the power to regulate many organizations by use of its sovereign and legislative powers. For example, the federal government has the power to regulate the behavior of organizations by imposing conditions or sanctions on their operations. However, the governing bodies of the regulated organizations make decisions within the regulatory framework. Regulatory powers do not constitute control for purposes of this Statement because the federal government's interest in these organizations extends only to the regulatory aspects of the operations.

31. Certain organizations may be economically dependent on the federal government but ultimately retain discretion as to whether to accept funding or do business with the federal government. For example, many nonprofit organizations rely on federal government funding but that does not mean they are controlled by the federal government. Although the federal government may be able to influence organizations dependent on federal funding or business through purchasing power, the federal government typically does not govern their financial and operating policies.

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Misleading to Exclude Principle

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32. There may be instances when an organization does not meet the inclusion principles in paragraphs 18 through 28 yet the government-wide GPFFR would be misleading or incomplete if the organization were excluded.[16]

33. Organizations should be included in the government-wide GPFFR if it would be misleading to exclude them.

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Organizations--Core Entities and Non-core Entities

34. The principles above would be used to assess what organizations to include in GPFFRs. To assist in making decisions about presentation, a distinction is then made between core entities and non-core entities. This assessment is based on the degree to which the following characteristics are met: the organization is taxpayer supported, is governed by the Congress and/or the President, imposes or may impose risks and rewards on the taxpayer, and/or provides core federal government goods and services on a non-market basis. However, not all characteristics are required to be met to the same degree; classification is based on the assessment as a whole.

Core entities

35. Core entities generally provide federal goods and services on a non-market basis.[17] Such entities are financed primarily through taxes, fees, and other non-exchange revenues as evidenced by inclusion in the budget. Significant risks and rewards fall to the taxpayer for core entities.

36. Accountability for core entities rests with the President and/or the Congress. Their governance structure is vertically integrated, such that the chain of command and manner of decision making leads directly to elected officials. Vertical integration may include the establishment of organizational authorities, development and approval of budgets, and the appointment of organizational leaders by the President and/or the Congress.

37. Entities listed in the budget, except for non-federal organizations receiving federal assistance (see par 19), are presumed to qualify as core entities while greater judgment will be needed to classify other organizations.

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Non-core entities

[16] Although such situations would be rare, this Statement provides for situations that may arise.
[17] Goods and services are provided on a non-market basis when they are provided free of charge or at charges that bear little relationship to the cost of goods or services.

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38. In order to fulfill public policy objectives, the federal government may have relationships with organizations that have a greater degree of autonomy than core entities. Such entities are included for accountability purposes but are considered "non-core entities."

39. Non-core entities may maintain a separate legal identity, have a governance structure that vests greater decision making authorities in a governing body to insulate the organization from political influence, and/or have relative financial independence.

40. Non-core entities may provide the same or similar goods and services that core entities do, but are more likely to provide them on a market basis.[18] Non-core entities receive limited or no taxpayer support. Accountability rests with the Congress and/or the President, but they have less direct involvement in decision making than is true in core entities. Limited risks and rewards fall to the taxpayers.

41. Non-core entities include but are not limited to: quasi governmental and/or financially independent entities, receiverships and conservatorships, and federal government intervention actions. In some cases, the relationship with the federal government is not expected to be permanent. The following non-core entity types are presented to assist in identifying entities that are non-core entities.

Quasi Governmental and/or Financially Independent Entities

42. Quasi Governmental and/or Financially Independent Entities are hybrid organizations that differ from core entities with regard to governance and/or financial arrangements.

43. Governance differences typically lead to greater independence. Characteristics may include the following:

   a. Longer appointments of key executives or governing boards to allow these appointees a degree of independence from the Congress and the President

   b. Delegated operational authority to provide a service or execute a program in a manner similar to private business enterprises

   c. Private sector legal characteristics, such as nonprofit status under the Internal Revenue Code

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[18] Goods and services are provided on a market basis when prices are based on the prices charged in a competitive marketplace between willing buyers and sellers.

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d. Exemption by statute from laws or regulations dealing with the federal budget, funds, personnel, ethics, acquisition, property, or works

e. Voluntary association with the federal government and shared purposes to implement government policies

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44. Financial differences typically lead to greater fiscal autonomy. Characteristics may include the following:

a. Primarily funded from a source other than appropriations

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b. Delegated financial authority to provide a service or execute a program in a manner similar to private business enterprises

c. Principally engaged in selling goods and/or services to organizations outside of the federal government

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d. Intended to, in the normal course of its operations, maintain its operations and meet its liabilities from revenues received from sources outside of the federal government

45. While not all entities of a given type will meet the characteristics above, examples of the types of entities that may be quasi governmental and/or financially independent entities are provided below. Each entity should be assessed objectively since there are likely to be differences among the entities within these example types such that some are core and others are non-core entities. Examples may include certain Federally Funded Research and Development Centers, museums, performing arts organizations, universities, and venture capital funds. The accompanying Illustrative Guide offers examples that may be useful in application.

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Receiverships and Conservatorships[19]

46. There are certain federal entities whose mission may include taking control or ownership of failed financial institutions, such as banks, with no goal to maintain control or ownership. To accomplish that mission, certain federally-created entities may act as receivers to liquidate failing financial institutions or as conservators to guide such institutions back to safe and sound conditions.[20]

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[19] This differs slightly from federal interventions because receivership and conservatorship activities are considered part of the mission of the federal reporting entities that perform them and the duration is typically shorter.

[20] For example, the Federal Deposit Insurance Corporation (FDIC) is an independent agency created by the Congress with the mission "to maintain stability and public confidence in the nation's financial system

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Organizations controlled or owned by such federal entities would be non-core entities.

Federal Government Intervention Actions

47. The federal government may intervene in exceptional circumstances, such as an economic crisis or military occupation, due to its broad responsibility for the well being of the country. However, intervention actions are not expected to be permanent and may not include a specific time limit.

48. Typically federal government intervention actions in these instances are not routine activities. Strategic planning documents are unlikely to include objectives to routinely initiate such interventions or to permanently operate organizations acquired through past interventions.

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49. Examples of intervention actions include:

    a. Temporary control-- the federal government seizes control of an established organization but expects to relinquish or cede control.

    b. Temporary ownership--the federal government acquires an ownership interest of an organization but expects to end its interest as soon as practicable.

50. Intervention actions that exist at fiscal year-end must be assessed to confirm the resulting control or ownership is not expected to be permanent. If not expected to be permanent, organizations controlled or owned through intervention actions would be non-core entities.

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Component Reporting Entities

51. The government-wide reporting entity is the only federal reporting entity that is an independent economic entity[21] and the inclusion principles are expressed from the perspective of the federal government. However, GPFFRs for the government-wide reporting entity represent a consolidation of component reporting entity GPFFRs. Therefore, component reporting entities must identify and include in their GPFFRs all core and non-core entities for which they are

by: insuring deposits; examining and supervising financial institutions for safety and soundness and consumer protection; and, managing receiverships."

[21] SFFAC 2, par. 38.

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accountable so that both the component reporting entity and government-wide GPFFRs are complete.

52. A component reporting entity's GPFFR should include all organizations that would allow Congress and the President to hold its management (appointed officials or other agency heads) accountable for implementation of public policy decisions, show the risks inherent in component reporting entity operations, and enhance accountability to the public. Each component reporting entity is accountable for all core and non-core entities administratively assigned to it.

53. Administrative assignments to component entities are typically made in policy documents such as budget documents, laws, regulations, or strategic plans. Administrative assignments can be identified by evaluating one or more of the following areas[22]:

a. Scope of the Budget and Budget Approval Process

b. Accountability Established Within a Component Entity

c. Other Significant Relationship Considerations (Misleading to Exclude and/or Misleading to Include)

Scope of the Budget & Budget Approval Process

54. Core and non-core entities subject to the budget approval and oversight process of the component reporting entity head should be included in the component reporting entity GPFFR. Each component reporting entity should include all core and non-core reporting entities:

a. listed within its section of the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account* unless they are non-federal organizations receiving federal financial assistance[23] or

b. included within its Congressional Budget Justification.

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Identifying Entities Administratively Assigned to

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[22] Component reporting entities should develop processes to ensure organizations in each of these areas have been considered and assessed. Central agencies are anticipated to determine if there is a need for coordinated guidance to be developed to ensure government-wide consistency.

[23] See par. 19.

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Accountability Established Within a Component Entity

55. Core and non-core entities for which a component reporting entity has been assigned accountability responsibilities should be included in its GPFFR. Determining whether accountability was established or assigned to a component reporting entity can be determined based on the consideration of certain indicators, but it also requires the application of professional judgment. Indicators[24] that accountability was established in the component reporting entity include:

a. Statutes or regulations establishing an organization state that it is assigned to or part of a larger federal organization.[25]

b. An organization is included in the component reporting entity's official organization chart.

c. The component reporting entity acquires and/or monitors[26] ownership[27] interests in organizations where there are ongoing responsibilities such as:

   (1) monitoring activities and/or reporting on outcomes,

   (2) monitoring the value of the ownership interest,

   (3) coordinating and/or conveying input on strategic plans,

   (4) providing appropriated funds to the organization and requesting funding for future years, or

   (5) administering any federal grants or contracts awarded to the organization.

d. A controlled organization[28] was established by the component reporting entity or to support the mission of the component reporting entity, and a continuing relationship exists. Examples of continuing relationships include:

   (1) approving bylaws including any amendments,

   (2) being represented on the governing board (e.g., as an ex-officio member),

[24] These indicators provide evidence that accountability was established or was assigned to a component reporting entity. Meeting any one would typically mean accountability was established.

[25] For example, the United States Census Bureau (officially the Bureau of the Census, as defined in Title 13 U.S.C. § 11) is part of the US Department of Commerce.

[26] Such responsibilities may be assigned to a program office or the office of inspector general.

[27] An owned organization may be a component reporting entity itself but also must be reported by another component reporting entity if management responsibilities are assigned to that entity.

[28] Where control exists at the government-wide level based on paragraphs 22-31.

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(3) appointing members of the governing board,

(4) coordinating and/or conveying input on strategic plans,

(5) monitoring organizational performance,

(6) approving budgets, operating plans, or contracts with others,

(7) establishing and executing cooperative agreements with the organization,

(8) administering federal grants to or contracts with the organization, or

(9) testifying before Congress regarding entity performance and objectives.

56. If more than one component reporting entity is assigned responsibilities related to a non-core entity as described above, the non-core entity should be included in the GPFFR of each component reporting entity assigned such responsibilities.

57. In the unexpected case where a non-core entity has not been administratively assigned to a core entity, the non-core entity should be reported by the component reporting entity (a) assigned responsibility for transferring funds to the non-core entity or (b) with which its mission most closely aligns.

Other Significant Relationships /Considerations (Misleading to Exclude and / or Misleading to Include)

58. There may be instances where an organization is not administratively assigned to the component reporting entity based on the principles in paragraphs 54-57, yet the component reporting entity GPFFR would be misleading or incomplete if the organization were excluded. For example, two organizations with the same mission may establish joint strategic plans and cooperate in executing programs to the extent that it would be misleading to separately report on their activities. Organizations should be included in the component reporting entities' GPFFR if it would be misleading to exclude them.[29]

[29] Although such situations would be rare, this Statement provides for situations that may arise.

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59. There may be instances where administrative assignments based on the principles in paragraphs 54-57, would result in misleading presentation. For example, an organization may have been legally established within a larger entity while being authorized to operate independently. While such conditions are expected to be rare, if the component reporting entity GPFFR would be misleading if the organization were included, the organization may be excluded so long as it prepares its own GPFFR and is included in the government-wide GPFFR.

60. Determining whether it would be misleading to include a core entity administratively assigned to a component reporting entity requires the application of professional judgment. Indicators that it may be misleading to include an organization include:

a. The budget submission is combined for administrative purposes as indicated by the
   - o Budget request not being coordinated with component reporting entity management
   - o absence of involvement by component reporting entity management regarding budget execution, investments, or strategic planning

b. The component reporting entity provides no direct oversight of the organization.

c. The organization's funding is separate from the component reporting entity's funding.

d. Inclusion of the organization's financial information in the component reporting entity's financial statement could be misleading as to the component's entity's responsibilities for the organization's liabilities and other obligations.

e. The organization has established itself as a stand-alone organization since its inception and has routinely prepared audited financial statements since that time. Further, the organization includes a statement in its own GPFFR that the organization is excluded from the component reporting entity's consolidated financial statement.

f. The organization provides financial data directly to the Department of the Treasury for the government-wide GPFFR.

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GPFFR Consolidation and Disclosure

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Core entities

61. The Statement provides for consolidation[30] of core entities' financial statements to facilitate an assessment of the financial position of the federal government and the cost of operations financed by taxpayers. Consolidation aggregates the individual financial statements of entities comprising a reporting entity and results in presentation of information for a single economic entity representing core taxpayer supported activities, resources, and obligations where accountability rests with the Congress and/or the President.

62. Core entities as defined herein are considered federal entities and should apply GAAP as defined in SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

63. SFFAS 34 recognizes that a limited number of federal entities prepare and publish financial reports pursuant to the accounting and reporting standards issued by the Financial Accounting Standards Board (FASB). SFFAS 34 provides that GPFFRs prepared in conformity with accounting standards issued by the FASB also may be regarded as in conformity with GAAP. Consolidated reporting entities (i.e. the consolidated government-wide entity or a consolidated component reporting entity) should consolidate component reporting entity or sub-component financial statements for core entities prepared in accordance with SFFAS 34 without conversion for any differences in accounting policies among the entities.

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Non-core entities

64. Maintaining a distinction between the finances of core entities and non-core entities will more effectively meet federal financial reporting objectives. However, federal financial reporting objectives cannot be fully met without information regarding non-core entities.

[30] Consolidation is a method of accounting that combines the accounts of those entities line by line on a uniform basis of accounting and eliminates balances and transactions among the entities. For selected financial statements such as the statement of budgetary resources, a combined financial statement which does not eliminate balances and transactions among the entities is acceptable.

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65. For those organizations classified as non-core entities, this Statement provides for judgment by the preparer in determining the appropriate disclosures based on the factors and principles provided herein.

66. Non-core entities need not be grouped by type and no distinction is made by type for purposes of determining the appropriate presentation or disclosure. Disclosures regarding these types of entities and any other types of entities identified as non-core should be provided in accordance with Disclosures for Non-core Entities as detailed in par. 68 to 71 below after considering the factors listed in par. 67.

Factors in Determining Non-Core Entity Disclosures

67. Materiality is an overarching consideration in financial reporting. Preparers should consider both qualitative and quantitative materiality in determining non-core entity disclosures. Beyond materiality, the following factors[31] should be considered in making judgments about the extent of appropriate non-core entity disclosures:

   a. ***Relevance to reporting objectives*** - Significance of the non-core entity to meeting the reporting objectives established in SFFAC 1, *Objectives of Federal Financial Reporting*, with regard to the core entity. This would include the significance of the information regarding results of operations and financial position to meeting the operating performance and stewardship reporting objectives.

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   b. ***Nature and magnitude of the potential benefits or risks/exposures associated with the relationship***- Information is needed to provide an understanding of the potential operational or financial impact, including financial-related exposures to potential gain and risk of loss, to the core entity resulting from the non-core entity's operations.

   c. ***Non-core entity views/perspective***- How the non-core entity itself accounts for or reports on its relationship with the federal government. For example, whether the non-core entity views itself as an extension of the federal government or operationally independent of the President and the Congress may influence the type and amount of information that is disclosed.

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[31] The factors are presented in a list for consideration in the aggregate; no individual weights should be assigned or interpreted.

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d. ***Complexity of the relationship***- More complex relationships would involve more detailed disclosures to ensure the relationship is understood by the readers.

e. ***Extent to which the information interests, or may be expected to interest, a wide audience*** - Due to the sensitivity of the relationship, materiality of the transactions, media attention, or other reasons, interested parties may expect some disclosure regarding the non-core entity or its relationship with the federal government.

f. ***Extent to which there are no alternative sources of reliable information***- An objective of GPFFRs is to meet the needs of users who may have limited access to information or statements and lack the ability to demand the desired information.

Disclosures for Non-core Entities

68. In addition to the factors presented in par. 67 regarding the extent of disclosures, both qualitative and quantitative factors should be considered in determining whether the disclosures for a non-core entity should be presented separately due to its significance or aggregated with other non-core entities. If disclosures are aggregated, aggregation may be based on non-core entity type, or class, investment type, or a particular type of event deemed significant to the reporting entity.

69. Disclosures should be integrated, concise, meaningful and transparent. Integration is accomplished by incorporating references to relevant disclosures elsewhere in the GPFFR with the required non-core entity disclosures or by providing a single comprehensive disclosure regarding the non-core entity and related balances. For example, reference may be made to a disclosure regarding investments in the non-core entity.

70. For each significant non-core entity and aggregation of non-core entities, disclose information to meet the following objectives[34]:

a. ***Relationship:*** The nature of the federal government's relationship with the non-core entity or entities

[34] The objectives are not listed in any order of preference.

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b. ***Relevant Activity:*** Nature and magnitude of relevant activity during the period and balances at the end of the period

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c. ***Future exposures:*** A description of financial and non-financial risks and potential benefits and, if possible, the amount of the federal government's exposure to gains and losses from the past or future operations of the non-core entity

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71. Examples of information[35] that may meet the above objectives and provide the necessary understanding of the non-core entity's relationship, activities, and future exposures specific to the federal government include but are not limited to:

a. The name and description of the non-core entity, including information about its mission and organization

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b. The nature of the relationship between the federal government and the non-core entity including any control or influence over the non-core entity and/or the percentage of ownership interest and voting rights

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c. For intervention actions, the primary reasons for the intervention and a brief description of the federal government's plan relative to operating or disposing of the non-core entity (including timeframes) and/or a statement that the intervention is not expected to be permanent

d. A description and summary of assets, liabilities, revenues, expenses, gains, and losses recognized in the financial statements of the reporting entity as a consequence of transactions with or interests in the non-core entity and the basis for determining the amounts reported (or a reference to other disclosures where such information is provided)

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e. A discussion of key indicators of financial health and changes in financial health including as appropriate summary financial statements, condensed financial information for the non-core entity (e.g. assets, liabilities, fund balances, total expenditures and sources of revenues) or key indicators.

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f. A general reference to non-core entity financial statements and how they can be obtained

35 No individual example is itself a required disclosure nor are the examples required in the aggregate. Therefore, the examples are not alternatives or substitutes one for another. Rather, a disclosure that meets the objectives in paragraph 70 should be provided.

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g. Key terms of contractual agreements, statues or other legal authorities regarding potential financial impacts (including those terms of the arrangements to provide financial support and liquidity, including events or circumstances that could expose the federal government to a loss)

h. The nature of, and changes in, the risks associated with the control of or other involvement with the entity during the period

i. The amount that best represents the federal government's maximum exposure to gain or loss from its involvement with the non-core entity, including how the maximum exposure to gain or loss is determined. If this cannot be quantified, a narrative discussion could be offered.

j. Other information that would provide an understanding of the potential financial impact, including financial-related exposures to potential gain and risk of loss to the reporting entity, resulting from the non-core entity's operations including important existing, currently-known demands, risks, uncertainties, events, conditions and trends—both favorable and unfavorable.

72. Non-core entity information disclosed in the GPFFR should be based on accrual based standards provided in generally accepted accounting principles for its specific type of entity. [36] This includes generally accepted accounting principles for the relevant domain (FASAB, Governmental Accounting Standards Board, or Financial Accounting Standards Board).

73. Although information for the same reporting period as the government-wide reporting entity is preferable, it is not mandatory; particularly if deemed not preferable from a cost-benefit perspective. If a non-core entity's reporting period differs from the government-wide reporting entity's and it is not cost-beneficial to align the reporting periods, financial information disclosed for the non-core entity should be for a reporting period ending within the government-wide reporting entity's reporting period.

74. Any significant changes in information occurring from the end of the non-core entity's reporting period should be reported consistent with the requirements of

[36] Core government entities should apply the GAAP hierarchy established in SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

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SFFAS 39, *Subsequent Events: Codification of Accounting and Financial Reporting Standards Contained in the AICPA Statements on Auditing Standards*.

Related Party

75. In addition, the federal government may be able to exercise influence over certain organizations that were not included in the GPFFR but the relationship should also be disclosed. NOTE: The issue of related parties will be addressed at the June meeting.

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Effect on Existing Concepts

Effective Date

77. These standards are effective for periods beginning after September 30, year. Earlier implementation is encouraged.

The provisions of this Statement need not be applied to immaterial items.

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Appendix A: Basis for Conclusions

This appendix discusses some factors considered significant by Board members in reaching the conclusions in this Statement. It includes the reasons for accepting certain approaches and rejecting others. Individual members gave greater weight to some factors than to others. The standards enunciated in this Statement–not the material in this appendix–should govern the accounting for specific transactions, events, or conditions.

Introduction

A1. The federal government and its relationships with other organizations have become increasingly complex. These complex relationships make it difficult to identify federal entities. In addition, some organizations may be viewed as "non-federal" and yet be owned or controlled by the federal government. Identifying the organizations to be included in the government-wide general purpose federal financial reports (GPFFR) is necessary to ensure their completeness.

A2. The GPFFR should include the varied organizations for which the President and/or Congress are accountable regardless of their form. Therefore, the primary reason for developing standards for the government-wide GPFFR is to ensure that users will be provided with complete financial information about the federal government and its involvements. While SFFAC 2 provides criteria for determining if an organization should be included, questions have continued in this area that resulted in the need for standards.

Project History /Task Force

A3. In 2008, the Board formed a task force to support the project. The objective of the task force was "to assist in developing the proposed standards on the boundaries of the reporting entity and specific criteria for determining whether an organization should be included."

A4. The task force met several times over the course of the project and also exchanged numerous ideas and recommendations electronically. The task force views and recommendations were presented to the Board for their consideration during the development of these proposed standards. Their assistance was essential and their views carefully considered by members during deliberations. (See Appendix X for a list of task force members.)

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Organizational Approach to Defining Boundaries

Underlying Concepts

A5. The federal government is complex and therefore defining the boundary of the GPFFR may be difficult. Its constitutionally established powers and often its motivations and functions are different from other organizations. Despite these complexities, difficulties, and differences, accountability is a fundamental goal of financial reporting. As noted in SFFAC 1:

> The federal government derives its just powers from the consent of the governed. It therefore has a special responsibility to report on its actions and the results of those actions. These reports must accurately reflect the distinctive nature of the federal government and must provide information useful to the citizens, their elected representatives, federal executives, and program managers. Providing this information to the public, the news media, and elected officials is an essential part of accountability in government.[37]

A6. SFFAC 1 discusses accountability and users' information needs as the foundation of governmental financial reporting. Specifically, par. 71 states "It may be said that 'accountability' and its corollary, 'decision usefulness,' comprise the two fundamental values of governmental accounting and financial reporting. They provide the foundation for the objectives of federal financial reporting. …The assertion of accountability therefore leads to identifying, first, those to whom government is accountable and, second, the information needed to maintain and demonstrate that accountability."

A7. SFFAC 1 explains that the federal government has a special responsibility to report on its actions and the results of those actions. SFFAC 1 discusses the information needs of both internal and external users including the citizens, their elected representatives, federal executives, and program managers because meeting user information needs is an essential part of accountability in government.

A8. An organizationally based approach to defining boundaries supports accountability to all users but particularly to external users who may be unaware of the nature of organizational relationships. Focusing on organizations helps to identify who is accountable for what. In addition, an

Deleted: <#>An organizationally based approach to defining boundaries supports accountability. Focusing on organizations helps to identify who is accountable for what. In addition, an organizational approach provides meaningful financial statements by aligning boundaries with defined organizations for which there would likely be users of GPFFR.[38] However, as the federal government must report on many different types of relationships with varied purposes due to complex governance structures and finances, there must be differences in presentation of financial information for different relationships. ¶

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[37] SFFAC 1, paragraph 8.
[39] See SFFAC 2, paragraphs 29-38, for a discussion of the organizational approach.

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organizational approach provides meaningful financial statements by aligning boundaries with defined organizations for which there would likely be users of GPFFRs.[39] However, as the federal government must report on many different types of relationships with varied purposes due to complex governance structures and finances, there must be differences in presentation of financial information for different organizations based on the nature of the relationship.

A9. SFFAC 1 is very clear that the objectives were designed to help ensure the accountability of the federal government and to better inform decisions influenced by financial information about the government. There is a focus on the needs of current and potential users of federal financial information. In each of the four federal financial reporting objectives articulated in SFFAC 1 there are several references to user information needs and accountability. Clearly, the notion of accountability is important when considering the boundaries of GPFFR.

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Identifying and Classifying Organizations

A10. This Statement provides that decisions about reporting boundaries be taken in two steps – first, determine what organizations are to be included[40] in the reports and second, identify the means to present relevant information about organizations.

A11. Three principles for including organizations in the government-wide GPFFR are established: *In the Budget*, *Majority Ownership Interest*, and *Control with Expected Benefits or Risk of Loss*. The Statement also includes a provision requiring inclusion of an organization if it would be misleading to exclude it. Next, for those organizations to be included, a distinction is made between core entities and non-core entities. The distinction between core and non-core entities will determine how financial information is presented in the GPFFR. Core entity financial information is to be consolidated and non-core entity financial information is to be disclosed.

A12. Professional judgment is required in the application of the standards proposed in this Statement. This Statement presents a principles-based approach to determining which organizations should be included[41] in the government-wide GPFFR because of the wide and varying relationships of the federal government. General purpose federal financial reports for the government-

[40] 'Included' means an organization's information is either consolidated or disclosed.
[41] Note that this Statement does not specify which organizations must prepare and issue financial statements.

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wide reporting entity should be broad enough to report the Congress and the President's accountability for organizations. This ensures that the financial reports contain all the information essential for fair presentation of the government's financial position and results of operations.

A13. The Board considered several alternative approaches to identifying organizations for which elected officials – the Congress and/or the President – were accountable. The principles for inclusion proposed herein establish accountability for organizations (1) funded through the budgetary process, (2) where a majority ownership interest is held, or (3) controlled with an expectation of benefits or risk of loss. Each of these principles for inclusion is discussed below.

Principles for Inclusion in the Government-wide GPFFR

In the Budget

A14. Identification of an organization in the President's Budget is the clearest evidence that an entity should be included in the government-wide report. Absent budgetary actions – originating with the President's Budget and leading to appropriations – federal organizations would be unable to continue operations. Financial reporting objectives – budgetary integrity, operating performance, stewardship, and systems and controls – could not be met if organizations identified in the budget were not included in the financial reports. Therefore, the most efficient means to identify organizations for inclusion is by their participation in the budget process as evidenced by the *Budget of the United States Government: Analytical Perspectives- Supplemental Materials* schedule *Federal Programs by Agency and Account*.

A15. Although the legislative and judicial branches (and most organizations within those branches) are not currently required to prepare financial statements, based on this principle (*In the Budget)* those organizations would be included in the government-wide report.[42]

A16. Organizations should include any financing accounts associated with the organization although such accounts may not be specifically identified in the schedule. For example, the *Federal Programs by Agency and Account* may

[42] As the source of GAAP for federal reporting entities, FASAB GAAP would be the appropriate accounting standards for these entities to adopt to the extent they prepare GAAP-based financial statements.

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not identify federal credit reform financing accounts, but those accounts should be included in GPFFR for the organization. In addition, other GAAP principles would apply, such as SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* and SFFAS 5, *Accounting for Liabilities of the Federal Government,* and help identify the elements and required disclosures for each organization.

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Organizations receiving federal financial assistance

A17. The *Federal Programs by Agency and Account* schedule also sometimes names specific recipients of federal financial assistance. SFFAC 2, *Entity and Display*, acknowledged that the *Federal Programs by Agency and Account* schedule sometimes names an organization to receive a "subsidy" and states "This does not mean, however, that an appropriation that finances a subsidy to a non-Federal entity would, by itself, require the recipient to be included in the financial statements of the organization or program that expends the appropriation." Thus, "subsidy" is the term used in SFFAC 2 to distinguish such "non-federal" organizations from the organizations intended to be included in the GPFFR.

A18. While the provision in SFFAC 2 was correct, the Board is proposing standards, and believes terms used in this Statement should be defined. The Board considered ways to define "subsidy" but concluded it was more appropriate to rely on the existing definition of "federal financial assistance."

A19. The proposed language ensures organizations that receive assistance as defined by the Single Audit Act Amendments of 1996[43] but listed under an appropriation in the *Federal Programs by Agency and Account* aren't automatically included in the GPFFR. Often grants are received through programs and recipient organizations are not necessarily listed in the budget, but an organization may be listed in some cases. The Board believes a means to confirm whether specifically identified recipient organizations are "non-federal organizations receiving federal financial assistance" is needed. When such organizations are listed in the budget they should be assessed against the Majority Ownership Interest and Control with Expected Benefits or Risk of Loss principles before being excluded from the government-wide GPFFR.

[43]'Federal financial assistance' is assistance that non-federal entities receive or administer in the form of grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, or other assistance.

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A20. Generally, the Board believes preparers can identify organizations that are in fact receiving ‘subsidies’ as described by SFFAC 2. The Statement provides that although these may be listed in the budget they are neither automatically included based on the first inclusion principle nor automatically excluded based on perceptions. The Board does not believe it would be appropriate to articulate how subsidies are presented in the *Federal Programs by Agency and Account* schedule or refer to other budget documents because such treatments may change.

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Organizations partially in the budget

A21. The Board deliberated the issue of certain organizations being partially in the budget (i.e., some of their operations or accounts are not in the President’s Budget), such as a museum receiving substantial donor support. The Board determined the organization should be included in the government-wide GPFFR based on the *in the budget* principle. The Board further decided that how such organizations should be presented would be based on whether the organization was a core or non-core entity, as discussed later in the Statement. Therefore, the language in the principle (*in the budget*) is silent regarding organizations partially funded by non-budgetary sources.

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Need for Additional Principles

A22. While the principle *in the Budget* is the most efficient means to identify organizations for inclusion, there are additional principles to be considered to identify other organizations that should be included in the government-wide GPFFR. The budget principle represents a starting point in analysis but does not necessarily mean that accountability goals would be met solely through that principle. Because the budget’s purposes differ from financial reporting objectives in many respects (such as the focus on the allocation of budgetary resource flows), it is possible that organizations or activities might be excluded from the budget for reasons that do not justify exclusion from financial reports. For example, some organizations may be established to operate in a manner similar to businesses and excluded from the budgetary process. Therefore, additional inclusion principles are necessary to ensure completeness in the context of the federal financial reporting objectives.

Majority Ownership Interest

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A23. Ownership interests typically provide owners access to resources and exposure to risks while supporting their desired goals. Federal financial reporting objectives require that information about the service efforts, costs, and accomplishments be made available. To ensure such information is included, when the federal government holds a majority ownership in an organization it should be included in the GPFFR. As described in the Statement, majority ownership interest exists with over 50% of the voting rights or the net residual assets of an organization.

A24. The Board noted that some may question how minority ownership interests (less than 50%) should be accounted for. The Board agreed attempting to address minority interests through the project may be less effective than allowing the GAAP hierarchy to fill any void. To address the potential question, the Board included within the Statement a footnote stating ownership interests 50% or less should be accounted for in accordance with the appropriate accounting standards per the GAAP hierarchy.

Control with Expected Benefits or Risk of Loss

A25. When the federal government controls an organization with the expectation of benefit or risk of loss, the organization should be included in the government-wide GPFFR to provide accountability. As detailed in the Statement, control involves the power to impose will on and/or govern the financial and/or operating policies of another organization with the potential to obtain financial resources or non-financial benefits or be obligated to provide financial support or assume financial obligations as a result of those actions. Both the power and benefit or risk of loss aspects of the control definition should be present to justify inclusion of the organization in the GPFFR.

A26. For example, the Statement provides for situations where the expectation of benefit or risk of loss does not exist—in the instance of the federal government exercising regulatory powers over an organization. In these cases, the federal government is unable to exercise that power for its own benefit and rarely explicitly assumes risk of loss. Therefore, including such an organization in the GPFFR would misrepresent the financial position and results of operation of the government. This would not support achievement of the objectives of financial reporting.

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A27. For financial reporting purposes, assessment of control is made at the reporting date and based on current legislation, rather than legislation that may or may not be enacted in the future.

A28. Determining control requires judgment, and the Statement provides indicators to assist in making determinations. The first set of indicators is “persuasive” as

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the federal government has the authority to control and any one of the listed items would mean control is present. The second set of indicators requires more judgment because the set of indicators is considered in the aggregate to assess whether the federal government has the ability to control the organization.

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A29. Because the government does not usually seek only financial benefits, the expected *benefit* associated with control does not have to be a financial benefit. Instead, it may be non-financial. For example, it may be in the form of a service provided on the federal government's behalf or the ability to direct the work of the other entity to deliver goods and services.

Misleading to Exclude Principle

A30. The Statement includes a general provision requiring inclusion of an organization if it would be misleading to exclude it. Certain members believed this may be problematic because no criteria are offered. However the Board ultimately agreed the principle would help ensure that the proposed Statement could accommodate rare situations that may arise in the future. This is consistent with provisions of SFFAC 2.

A31. The Board also believes the principle is consistent with the Governmental Accounting Standards Board Statement 14, *The Financial Reporting Entity.* It provides for those unique situations where the preparer and auditor agree something should be included that was not otherwise incorporated.

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A32. The Board also believes this principle would be used in situations agreed to by the preparer and auditor; judgment would be required in this area. Therefore, the Board believes these types of situations would be difficult to anticipate and developing criteria challenging.

Organizations--Core Entities and Non-core Entities

A33. Differences in purposes and governance structures require differences in presentation of financial information. To facilitate this, decisions about federal financial reports for an organization are taken in two steps – first, determining what organizations are to be included in the reports and second, identifying the appropriate means to present relevant information about the organizations.

A34. Different means of presenting relevant information are provided for core and non-core entities. The distinction between core entities and non-core entities is

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based on the degree to which the following characteristics are met: the entity is taxpayer supported, is governed by the Congress and/or the President, imposes or may impose risks and rewards on the taxpayer, and/or provides core federal government goods and services on a non-market basis.

Core entities

A35. Core entities generally provide federal goods and services on a non-market basis. That is, prices are not established solely through market transactions where supply and demand determine price. Goods and services provided on a non-market basis may be free of charge or provided at prices that are either not economically significant or bear little relationship to the cost of the good or services.

A36. Core entities are financed through taxes, fees and other non-exchange revenue as evidenced by inclusion in the budget. Significant risks and rewards fall to the taxpayer for core entities. Inclusion in the budget is the clearest evidence that an entity is relying on the taxpayer and that elected officials are key decision makers.

A37. The budget is a political document serving many purposes. The 1967 *Report of the President's Commission on Budget Concepts* indicates that "the budget must serve simultaneously as an aid in decisions about both the efficient allocation of resources among competing claims and economic stabilization and growth." On the topic of coverage of the budget, the Commission recommended that "the budget should, as a general rule, be comprehensive of the full range of Federal activities." Because the budget includes "federal activities," entities listed in the budget that are not receiving federal financial assistance are presumed to qualify as core entities. For such entities, allocation of resources to its activities is determined through federal legislation – making the entity itself financially accountable to Congress and/or the President. Accountability for core entities rests with the President and/or the Congress, and their approved appointed organizational leaders.

A38. The assessment of whether an entity meets the attributes for a core entity is based on the assessment of all the attributes and the degree to which each is met. As such, not all attributes are required to be met; classification is based on the assessment as a whole. For example, the post office may compete against other organizations; therefore it may be viewed as providing goods and services on a market basis. However, if it primarily meets the remaining characteristics then it is a core entity.

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Non-core entities

A39. On the opposite end of the spectrum and with varying degrees in between are non-core entities. The use of professional judgment will be required when assessing the non-core entities as there is a much broader spectrum of entities having varying degrees of relationships with the federal government.

A40. Non-core entities receive limited or no taxpayer support. Non-core entities, in contrast to core entities, are often structured so there is a clear barrier or limit on taxpayer financing of the entity. This is an effort to shield the taxpayer from risk.

A41. In addition, another contrast with core entities is that with non-core entities, accountability ultimately rests with the President and/or Congress, but there is much less direct involvement in decision making. Greater decision making may rest with a governing board or there may be situations where non-core entities may have a separate legal identity.

A42. The Statement provides categories of non-core entities primarily as a way to help identify non-core entities. However, the Statement does not require presentation by any specific class or category and allows flexibility in presenting information about non-core entities. The categories of non-core entities include quasi governmental and/or financially independent entities, receiverships and conservatorships, and federal government intervention actions.

Quasi Governmental and/or Financially Independent Entities

A43. The Statement describes quasi governmental and/or financially independent entities as those non-core entities where governance and/or financial differences lead to greater independence. The Statement provides both governance and financial characteristics that would be found in this type of non-core entity.

A44. Quasi governmental and/or financially independent entities may include certain Federally Funded Research and Development Centers (FFRDC), museums, performing arts organizations and universities, and venture capital funds. Since details may differ among organizations in each example type an objective assessment may classify some individual organizations as core entities rather than non-core. The accompanying Illustrative Guide offers examples that may be useful in application.

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Receiverships and Conservatorships

A45. The Statement describes receiverships and conservatorships as non-core entities. This includes those failed financial institutions and banks the federal government may take control or ownership of with no goal to maintain the relationship. Absent a decision to make control permanent, such entities would be non-core entities.

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Federal Government Intervention Actions

A46. The Statement describes federal government intervention actions as non-core entity involvements resulting from exceptional circumstances where the involvements are not expected to be permanent. SFFAC 1 acknowledges the unique nature of federal government activity and its broad responsibilities. Par. 50 explains "The federal government is unique, when compared with any other entity in the country, because it is the vehicle through which the citizens of the United States exercise their sovereign power. The federal government has the power through law, regulation, and taxation to exercise ultimate control over many facets of the national economy and society…" SFFAC 1 describes the federal government's responsibility for the general welfare of the nation in par. 53-54 as "a broad responsibility that involves multiple goals."

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A47. With these broad responsibilities, the federal government may be required to take certain actions or intervene in certain situations. Examples may include actions to provide stability to the financial markets or military occupation of another country.[44] These types of federal government interventions are considered rare.[45]

A48. Currently SFFAC 2 provides an exception for situations where the indicative criteria are met temporarily. Specifically, par. 45 of SFFAC 2 states "The entity or any of the above criteria are likely to remain in existence for a time, i.e., the interest in the entity and its governmental characteristics are more than fleeting." 'Fleeting' may imply periods of one year or less to some and the Board considered how to clarify the term 'fleeting.' Ultimately, the Board decided terms such as 'fleeting' and 'temporary' implied a time limit.

A49. However, there may be instances where an intervention is longer than one year due to the extreme factors of the national crisis. In most instances, it is

[44] After the signing of the Japanese Instrument of Surrender in 1945, Japan was supervised for 6 years by the Allied (primarily American) forces and subject to military control, with General MacArthur at the head of the Occupation administration. (Takemae, Eiji 2002 p. xxvi and Wikipedia http://en.wikipedia.org.wiki/Occupation_of_Japan)

[45] The current financial crisis is considered to be the most severe since the Great Depression. (White Paper on Changes to Financial Regulations)

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difficult to establish and meet a timeline for ending an intervention. In these instances, the focus continues to be on governance and protection, rather than maximizing profits or establishing new federal government lines of business. Although the actions may be longer than one year, the interventions are 'not expected to be permanent.' The Board established this 'non-permanent' expectation as a characteristic of non-core entities rather than relying on 'temporary' or 'fleeting' to avoid the implication that a time limit could be established.

A50. Historically the federal government has been involved in few commercial enterprises on an equity basis or shared ownership basis.[46] As a sovereign entity, the federal government does not act to maximize profits. However, there may be instances when the federal government may act in these capacities for the general well-being of the nation. Challenges may force the federal government to take extraordinary measures, such as actions to provide stability to financial markets or to revive the financial system. In doing so, the federal government may intervene and act in capacities to protect taxpayers which may ultimately lead to taking control of organizations or acquiring some form of ownership.

Component Reporting Entities

A51. The Board believes there should be consistency in treatment of organizations at the government-wide and the component reporting entity levels. The reasons for including entities in the government-wide entity GPFFR should be consistent with the reasons at the component reporting entity level. Further, classification as core or non-core entities would be the consistent in government-wide and component reporting entity GPFFR. The Board believes a single set of principles for inclusion and classification presented from the government-wide perspective provides for the desired consistency. This is appropriate and necessary because the government-wide reporting entity is the only federal reporting entity that is an independent economic entity. However, implementation of these principles will involve the component reporting entities because the government-wide report is a consolidation of the reports provided by component reporting entities. Therefore, component reporting entities must identify and include in their GPFFR all core and non-core entities for which they are accountable so that both the component reporting entity and government-wide GPFFR are complete.

[46] CRS Report for Congress RL30533, *The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics*

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A52. The Board believes that component reporting entities should identify core and non-core entities based on organizations that are administratively assigned to the component reporting entity. Standards that are based on organization and accountability provide a more realistic view of how component reporting entities become accountable for organizations and how component entity boundaries are likely to be determined. The result will be component reporting entity GPFFR that include all organizations the component reporting entity management (appointed officials) are expected to be accountable for.

A53. Administrative assignments to component entities are typically made in policy documents such as budget documents, laws, regulations, or strategic plans. Ultimately, component reporting entities would identify and include in their GPFFR all core and non-core entities for which they are accountable so that both the component reporting entity and government-wide GPFFR would be complete.

A54. Although there may be a one-time review to ensure completeness and consistency, the Board believed this method is reasonably consistent with current practice. Further, a coordinated effort from the central agencies could promote a process to ensure the component reporting entities are performing the necessary procedures to capture the material organizations from their perspectives and also for consideration at the government-wide level.

Reporting Entity Consolidation and Disclosure

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A55. As noted above, decisions about the government-wide GPFFR are taken in two steps – first, determining what organizations are to be included in the reports and second, identifying appropriate means to present relevant information about organizations. The final determination of the presentation of financial information through consolidation or disclosure is based upon the results of two assessments—first if the organization is included and second, if those included organizations are classified as core or non-core entities.

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A56. The **High Level Flowchart** at Appendix B to this ED is a useful tool in applying the principles established as it steps through this process. It is helpful in the assessment and applying the standards in order, including paragraph references to the ED and major decision points.

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Core entities

A57. The Statement provides that core entities apply SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*. In addition, it provides for the consolidation of core entities so taxpayers and citizens may assess the financial position and the cost of operations of the federal government. Consolidation of the taxpayer supported activities, resources, and obligations where accountability rests with the Congress and/or the President ensures that the reporting objectives of SFFAC 1 are met.

Consolidation of FASB-based and FASAB-based Information

A58. The Board has considered the potential ramifications when some federal entities follow GAAP for nongovernmental entities promulgated by the private sector Financial Accounting Standards Board (FASB GAAP) and their information is consolidated with information based on FASAB standards. For example, federal government corporations, the U.S. Postal Service, certain component entities of the U.S. Department of the Treasury, and some smaller entities in the executive and legislative branches have historically applied FASB GAAP and continue to do so. SFFAS 34 recognizes that "general purpose financial reports prepared in conformity with accounting standards issued by the FASB also may be regarded as in conformity with GAAP for those entities that have in the past issued such reports." SFFAS 34 also provides that a federal entity preparing audited financial statements for the first time may adopt FASB standards in the rare case that the needs of its primary users would be best met through the application of FASB standards. The acceptance of these practices raises the question of whether the information prepared under FASB standards may be consolidated with information prepared under FASAB standards in consolidated reports prepared by other component entities and in the consolidated government-wide entity.

A59. The Board has considered such issues on several occasions and provided concepts as follows:

> The reporting entities of which the components [preparing reports under FASB or regulatory accounting standards] are a part can issue consolidated, consolidating, or combining statements that include the components' financial information prepared in accordance with the other accounting standards. They need to be sensitive, however, to differences resulting from applying different accounting standards that could be material to the users of the reporting entity's financial statements. If these differences are material, the standards recommended by FASAB and issued by OMB and GAO should be applied. The components would need

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to provide any additional disclosures recommended by FASAB and included in the OMB issued standards that would not be required by the other standards.[47] (SFFAC 2, Entity and Display, par. 78 (excerpt from section on "Financial Reporting For An Organizational Entity"))

A60. The Board determined in SFFAS 34 that FASB-based statements are acceptable in certain circumstances. While there are significant differences between FASB and FASAB standards, both standards result in accrual basis information and disclosures that aid users in understanding the information. Given the decisions made in SFFAS 34, members do not believe requiring a conversion of FASB-based information to FASAB-based information for consolidated financial reports of larger entities is justifiable.

A61. Users may be confused by the presentation of different amounts for a component in its own financial report and in the consolidated financial reports of larger entities; particularly when both amounts would be in accordance with GAAP for federal entities per SFFAS 34. In addition, conversion imposes a cost and it is not clear that the cost is justifiable based on benefits to the user. Therefore, this Statement proposes that amounts derived for component entities in compliance with SFFAS 34 be consolidated without adjustment.

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A62. However, if this leads to consolidation in a single line item of amounts measured differently due to differences between FASB and FASAB principles, then one would anticipate disclosures of the different accounting policies and the related amounts to aid the reader in understanding the information provided. The Board considered adopting requirements for such disclosures but believes that existing requirements and long-standing professional practices are sufficient.

Non-core entities

A63. The Board believes consolidation of non-core entities would not result in information meeting the basic qualitative characteristics of information in financial reports because it would not provide the most relevant, understandable, or consistent information. For example, for non-core entities the Board believes consolidation may obscure the boundaries of the risks and rewards intended to be assumed or gained. Further, assets that are not available for purposes other than the specific business operation of the non-

[47] In October 1999, FASAB was recognized as the Rule 203 standards-setting body for the federal government. As such, FASAB now issues the standards, rather than issuing recommendations to OMB and GAO for issuance of the standards.

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core entity might be commingled with federal assets and liabilities not fully guaranteed by the federal government might be added to federal liabilities.

A64. SFFAC 1 par. 49 states "…Federal accounting and financial reporting are shaped by, and need to respond to, the unique characteristics and environment of the federal government." SFFAC 1 par. 105 further explains "reports must accurately reflect the distinctive nature of the federal government and must provide information useful to the people, their elected representatives, and federal executives…" SFFAC 1 also provides the qualitative characteristics of information in financial reports, by identifying these basic characteristics: understandability, reliability, relevance, timeliness, consistency, and comparability.[48]

A65. Flexibility in disclosures for non-core entities is provided because the range of non-core entities is broad and may require different disclosures to meet the reporting objectives. Providing this flexibility allows the preparer to present information judged most necessary to meet reporting objectives while also providing an understanding of the potential effect of the relationship on the core entity's financial statements.

A66. One approach is to consider how to ensure that basic financial statements measure and communicate the risks and rewards assumed by the citizens.[49] Citizens have a clear interest in the risks and rewards assumed, but it is less clear that full consolidation provides the most relevant, understandable, or consistent measures of risks and rewards.

A67. Par. 161 of SFFAC 1 discusses relevance as "…To be relevant, a logical relationship must exist between the information provided and the purpose for which it is needed. Information is relevant if it is capable of making a difference in a user's assessment of a problem, condition, or event. Relevance depends on the types of financial information needed by the various users to make decisions and to assess accountability." SFFAC 1 also provides that the concept of consistency in financial reporting extends to the determination of the financial reporting entity.[50]

Factors in Determining Non-Core Entity Disclosures

[48] SFFAC 1, par. 156

[49] SFFAC 1, par. 99-102 describes the users need information to assess the effect of the government's activities on its financial condition and that of the nation, which includes information on the federal government's exposures and risks.

[50] SFFAC 1, par. 163

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A68. Because of the flexibility needed regarding disclosures, preparers are provided a list of factors or guidance to assist in determining what disclosures to include. Materiality is an overarching consideration in financial reporting. Preparers should consider both qualitative and quantitative materiality in determining non-core entity presentation and disclosure. Beyond materiality, the factors provided in the Statement assist in determining the nature and extent of appropriate non-core entity disclosures to be provided.

A69. The factors are to be considered in the aggregate; no individual weight should be assigned or interpreted. Therefore, the assessment of the appropriate disclosures should be made after considering all the factors.

Disclosures for Non-Core Entities

A70. The Board recognizes that although the Statement provides flexibility with non-core entity disclosures, there is a wide variety of information listed as examples that may be disclosed to meet the intended objectives. Care should be taken to ensure the objectives are met, without producing unintended consequences. Preparers should keep in mind there are associated costs and potential audit implications with any information included in GPFFR. Incorporating by reference or including summary financial statements or summary financial information generally would result in an auditor being required to gain audit assurance on that information and thereby may result in additional audit costs.

A71. The Board believes non-core entity disclosures in the government-wide GPFFR should be based on accrual basis standards specific to the type of entity while minimizing additional costs on the non-core entity. Therefore, there will be instances where non-core entities disclosures are based on different reporting periods. The Board agreed that if non-core entities have a different reporting period than the government-wide GPFFR, disclosure of information from a reporting period ending within the government-wide reporting entity's reporting period is acceptable. The Board performed outreach on this issue to the audit community and to the federal entity task force. Generally, the feedback supported this approach.

A72. However, due to the fact there could be a large time lag, there should be a provision for disclosing significant changes in the financial position and other information occurring from the audited financial statements to the reporting

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entity's fiscal year end. The Board notes this would only be necessary if a non-core entity summarized financial statements or summarized financial information were presented. Otherwise normal transactions would be captured throughout the year so this would be a somewhat narrowed focus.

A73. The Board was especially concerned with the interpretation by the users and preparers regarding the proposed ED requirements for non-core entity and ultimately how they would affect the display and disclosures. The Board believed this would be an important consideration during deliberations of the ED and invited the assistance of the Department of the Treasury and a potential included organization in preparing a draft Illustration of a disclosure based on the draft requirements.

A74. Although the Board believed some enhancement of the draft standards was in order to encourage concise and transparent disclosures, the Board agreed the inclusion principles were appropriate. Further, the flexibility provided within the disclosure requirements, along the factors to consider, were preferable to prescribing information required regarding specific entities. After the draft disclosure was provided, the Board noted the need to emphasize the aggregation of information, referencing other disclosures when possible, additional focus on risk and other enhancements to the non-core entity disclosure section. This need arose because of the complexity of the relationships being described, transactions affecting multiple assets and liabilities being reported, and the desirability of an integrated set of disclosures. The Board modified the draft disclosure requirements to emphasize integration of disclosures.

Federal Reserve System and Other Entities Identified in SFFAC 2

A75. SFFAC 2 identified certain entities or types of entities (the Federal Reserve System, Government Sponsored Enterprises and Bailout Entities) that could be included in the government-wide reporting entity based on the established concepts but that should not be included.[51] This Statement establishes principles to ensure users of GPFFR are provided comprehensive financial information while recognizing the complexity of the federal government and its relationships with varied organizations. The new principles can be applied to the entities previously excluded and conclusions reached to include the entities—either as core or non-core entities—or to continue to exclude the entities. SFFAC 2 is being amended to ensure that concepts provide a

[51] SFFAC 2, *Entity and Display,* par. 47-50.

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framework for standards-setting but do not themselves establish standards by listing specific exclusions.

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Appendix C: Abbreviations

CFR	Consolidated Financial Report
DOL	U.S. Department of Labor
ED	Exposure Draft
FASAB	Federal Accounting Standards Advisory Board
FASB	Financial Accounting Standards Board
GAAP	Generally Accepted Accounting Principles
GPFFR	General Purpose Federal Financial Reports
OAI	Other Accompanying Information
OMB	Office of Management and Budget
RSI	Required Supplementary Information
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards
U.S.	United States

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