FASAB

Federal Accounting Standards Advisory Board

July 12, 2007

Memorandum

To: Members of the Board

From: Richard Fontenrose, Assistant Director

Through: Wendy M. Comes, Executive Director

Subject: Social Insurance,[1] Tab A

This memorandum provides an overview of comments received on the *Preliminary Views* document, discusses areas where there appears to be consensus among members as well as areas where the members may differ, and explores alternatives for moving forward. The objective of this session is twofold: first, to present a plan for addressing social insurance; and, second, afford members an opportunity to provide tentative feedback regarding comments received and the work to date.

I. Discussion of Respondents' Comments

Preliminary Views Document

Sixty-seven respondents submitted comments to the *Preliminary Views* as follows:

1. 18 federal government representatives:

    A. 5 users, academics, other
    B. 6 auditors
    C. 7 preparers and managers

2. 49 non-federal representatives:

    D. 47 "users, academics, other"
    E. 2 "auditors"

[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.

Attachment 1 provides a record of the responses received to the *Preliminary Views* document. Attachment 1, Table 1 (pages 10-11) summarizes the responses on each question. (Also, see Attachment 5 for the detailed worksheet used for Table 1.)

The following is an overview of the comments received on each of the six questions asked in the *Preliminary Views* document. (See Box 1 below for a quick reference regarding the questions).

1. Question 1 asked respondents which obligating event they favored. **A slight majority of respondents** who commented on this question **favored either the Primary View** (22) **or "work in covered employment"** (11). **The Alternative View received the single most favorable responses among the four obligating event options** (30). No respondents commented on "threshold" eligibility.[2] Attachment 1 (pages 3-6) lists examples of the reasons given by respondents for their decision regarding Question 1; also, an abstract of comments by question number is provided in Attachment 1, Table 2 (pages 12-36). Generally, respondents supporting either the Primary or Alternative Views cite the rationale for each position in the *Preliminary Views* basis for conclusions. Those favoring the work-in-covered-employment obligating event often saw an exchange transaction occurring (payroll tax payments "in exchange" for future benefits), or saw no difference between SI and pensions. Some of those favoring work-in-covered-employment event stated that the government had created an expectation and reliance.

> Box 1 – PV Questions
>
> 1. Which obligating event creates a liability and expense for social insurance programs?
>   - A. All work in covered employment regardless of "vesting"
>   - B. "Substantially meeting eligibility requires," which for Social Security and Medicare occurs when workers become "fully insured" at 40 quarters of or equivalent work in covered employment and subsequently as workers become eligible for additional benefits due to work in covered employment
>   - C. "Threshold eligibility," which for Social Security and Medicare occurs at 62 or 65 years of age when workers become permanently fully insured
>   - D. "Due and payable"
> 2. Are Social Security and Medicare obligations measurable for the purposes of recording a liability after 40 quarters or equivalent work in covered employment?
> 3. Statement of Social Insurance (SOSI): Should line items be added to SOSI that tie to expense and liability amounts reported in the SNC and balance sheet per primary view (PV)? Should the reasons for changes in SOSI amounts be reported? If so, which approach is favored: PV? Alternative view (AV)?
> 4. Should a "statement of fiscal sustainability" be adopted?
> 5. Should "deferred revenue" be considered?
> 6. Other comments?

2. Question 2 asked if Social Security and Medicare obligations were measurable for the purpose of liability reporting at 40 quarters of work in covered employment as proposed in the Primary View. **A majority of respondents** who commented on this question **agreed with the Primary View** (21 of 38). Examples of the reasons given by respondents for their decision regarding Question 2 are listed in Attachment 1,

[2] Staff notes that its count of respondents' opinions is approximate and subject to interpretation. Some respondents were difficult to classify. For example, Dr. Prince (letter 51) stated that he concurred with the Primary View but would not report the 40-QC liability on the balance sheet; he suggests limited disclosure instead. Staff counted Dr. Prince as favoring the Primary View regarding Question 1 but not regarding Question 2. Thus, the tally is a starting point for discussion rather than conclusive evidence.

page 6; and an abstract of comments is provided in Attachment 1, Table 2 (pages 12-36).

3. Question 3 involved several components. Examples of the reasons given by respondents for their decision regarding Question 3 are listed in Attachment 1, page 7; and an abstract of comments is provided in Attachment 1, Table 2 (pages 12-36).

    3.1 Question 3.1 asked the respondents whether the Board should adopt the Primary View proposal to add line items to the Statement of Social Insurance (SOSI) that tie to revised liability and expense amounts in the primary statements. About **two-thirds** of the respondents who commented on this question (23 of 36) **did not agree with the Primary View**.

    3.2 With respect to the question of reporting on SOSI changes (Question 3.2), almost everyone who commented **favored reporting on changes** (31 of 34).

    3.3 A subcomponent of Question 3.2 asked those who favored reporting changes whether they preferred the Primary or Alternative View approach, and a **majority** (22 of 31) **preferred the Alternative View** approach.

4. Question 4 asked respondents whether the Alternative View proposal to present a statement of fiscal sustainability in the Financial Report of the United States Government (FR) as required supplementary information (RSI). **A majority of respondents** who commented on this question **favored the Alternative View proposal** (29 of 41). Examples of the reasons given by respondents for their decision regarding Question 4 are listed in Attachment 1, page 7-8; and an abstract of comments is provided in Attachment 1, Table 2 (pages 12-36).

5. Question 5 asked respondents whether the Board should consider the Alternative View proposal regarding deferred revenue for earmarked revenues in excess of related program costs. **A majority of respondents** who commented on this question **did not agree with the Alternative View proposal** (20 of 33). Examples of the reasons given by respondents for their decision regarding Question 5 are listed in Attachment 1, page 8; and an abstract of comments is provided in Attachment 1, Table 2 (pages 12-36).

6. Question 6 asked respondents for any other comments they might have on the guidance provided for measurement, display, disclosure, and RSI. The respondents had various comments as shown in the Table 2 below. An abstract of comments is provided in Attachment 1, Table 2 (pages 12-36).

May 23 Hearing

Sixteen people testified on May 23 as follows (the minutes are present at Attachment 2):

1. 5 from federal government:

    - Steven Schaeffer, SSA IG office
    - CG Walker
    - Steve Robinson from Senator Grassley’s office
    - Stephan Goss, SSA chief actuary

  - Representative James Cooper

2. 11 from private sector:

  - Institutes/organizations:

    - Bob Bixby, Concord Coalition
    - Sheila Weinberg, Institute for Truth in Accounting
    - John Rother, AARP
    - Jagadeesh Gokhale, Cato Institute
    - Bob Childree, AGA FMSB
    - Alison Fraser, Heritage Foundation

  - Other:

    - Thomas Prince, NW University
    - Martha Zeilger, municipal government financial director, NC
    - Howell Jackson, Harvard Law School
    - Mike Shannon
    - Terry Menzel, KPMG

3. The following are staff notes regarding comments made at the hearing, organized by topic:

A. <u>Obligating events</u>:

1. Work in covered employment (WICE):

   - Recognize a commitment to provide benefits for all beneficiaries, not just the very young, but he is indifferent as to what you call the commitment. (Gokhale)
   - Supports PV but believes beginning WICE is the point at which measurement should commence. There is an implicit exchange transaction when payroll taxes are paid. (Menzel)

2. "Threshold" event:

   - Congress would be reluctant to change <u>retiree</u> benefits and, generally, retirees would need certainty. (Rother)
   - A reasonable period could be looked at. (Schaeffer)

3. Due and payable:

   - Due and payable is appropriate and consistent with the liability definition in the *Elements* ED. The proposed Primary View (PV) cost would dwarf other costs. (Schaeffer)
   - The AV is more consistent with current law, Government SI communications, and international accounting. (Walker)
   - Current standard is consistent with current law.

B. <u>Current law</u>:

- As long as the policy is in place, there is a liability. (Gokhale)
- The AV is consistent with current law. (Walker)

C. <u>Congress' ability to change the law</u>:

- Some commented that the key difference between the private sector and the government is Congress' ability to raise taxes and change benefits and the AV is a more accurate representation of this. (Rother, Walker)
- Current law expressly reserves the right to change or repeal SI programs, which is one of the two unique characteristics of Social Security and Medicare that make PV inappropriate. The other is the statutory limit on Trust Fund payments. (Robinson)
- Congress can change a great many things in addition to SI programs, including repudiating debt. Consideration of Congress' ability to change law is not very helpful in deciding whether something is recognized. (H. Jackson)
- Accounting measures liabilities based on the circumstances at the balance sheet date. The notion is embedded in the literature. (Menzel)

D. <u>The meaning of "liability"</u>: Views differ regarding what constitutes "liability."

- "Liability" is equivalent to a "legal liability." (Bixby)
- Reporting a liability does not change legal status. (Zeigler)
- Liabilities are implicitly linked to funding and information in that context is not useful for evaluating SI, which is not (or cannot be) advance-funded. (Bixby, Robinson) This is appropriate for private companies that can go out of business but not for the Government, which is perpetual, nor for SI, for which the deficit is too large to pre-fund in any case. (Robinson)
- The Government's commitment to the Social Security Trust Fund (and other holders of US Treasury securities) is irrevocable and the Board should consider recognizing a deferred revenue liability. (Walker, Goss)
- A liability is something that must be paid yet we know Social Security benefits can be changed at any time and therefore classifying them as liabilities would be misleading. (Fraser)
- Language is important. The liability label makes benefits intractable. (Fraser)

E. <u>The affect of reporting a long-term liability on efforts to reform Social Security and Medicare</u>:

- Calling the SI commitment a "liability" may preclude reform due to the political perception of a repudiation of a debt. (Bixby)
- Reporting an accrued liability would make reform harder. (Weinberg)
- Reporting an accrued liability would be more likely to stimulate reform than impede it. (Zeilger, H. Jackson)

- The outcome of the Board's work is not expected to lead to the resolution of issues regarding the sustainability of programs. (Walker)
- It are not just what you do but how you do it. It will be either a net plus or a net minus in improving public understanding, and the possible narrowing of options for reform. (Walker)
- The acting of sending SSA individual statements has not "locked-in" benefits, and it is not plausible that reporting a gross number will accomplish that. (H.Jackson)
- Citizens comprehend that a benefit is being accrued as they work. From a technical legal perspective, the PV would not "lock in" benefits. (Cooper)

F. <u>The difference between SI and other federal programs</u>:

- Prefers to start measuring fiscal condition from a governmentwide perspective and therefore Medicaid and other programs should be included. Start with a complete picture of the overall projection and then explain components of the continuum. (Gokhale)
- SI programs are not different from other entitlement programs. SI commitments are similar to defense spending. How the government manages such spending to similar how individuals manage the family budget: child-rearing costs are not prefunded when the child is born. (Schaefer)
- SI programs are more defined than other programs that might appear similar. (Walker)
- There are many factors (trust funds, payroll tax, accumulation of benefits from being in the work force, open-ended appropriations) that distinguish SI programs from others. (H. Jackson)
- Entitlement programs are the gray area on the "continuum." Programs with mandatory spending fall on the liability side. It is easier to block changes than to put through changes. Permanent appropriations are hard to change and are somehow locked in. They are on "autopilot." Yes, this makes funding key criteria but only in the sense that permanent appropriations are very hard to change. (H. Jackson)
- SI is not welfare. SI gives the appearance that participants are paying for benefits. (Cooper)

G. <u>What a "liability" on the balance sheet would communicate</u>:

- People may be confused if a liability amount differs from estimates, for example, the unfunded obligation, reported in the Trustees' Report. (Bixby)
- A liability is a snapshot of where the program is. (Zeilger)
- A liability is a different number than the "closed group" or "open group" number. These numbers measure different things. (Bixby)
- A liability is only a part of the SI commitment and reporting it on the balance sheet could mislead users. (Gokhale)

- "Liability" and "balance sheet" may be accounting constraints that work well in the private sector but not in the public sector; for example, the use of shutdown measures when the program will not be shut down. (Gokhale)
- The AV liability position is consistent with other Government communications (benefit statements). (Walker)
- Some line must be drawn between what you call a liability and what you do not. We should not represent SI – and perhaps not OPEB or other uncertain future benefits either – as promises because of the misunderstanding that it can create. (Goss)
- A liability should convey the magnitude of the commitment and the change in fiscal burdens. (H. Jackson)
- It makes a difference whether you recognize an element on the balance sheet or other statements or disclose it in notes. (Menzel)
- If you have a statement of financial position that does not include all aspects of position then you are misleading people. (Menzel)
- The balance sheet is the only way to communicate with citizens on this issue. Citizens consider the balance sheet a "real" financial statement. For example, it would be meaningful to Rotarians. Accounting must mesh with the people's understanding. (Cooper)
- The financial statements should provide information for policy decisions. With liability recognition, the immediate reaction is tax increases. (Fraser)

H. <u>The significance of payroll tax "contributions"</u>:

- Earmarked funds create a distinction among entitlement programs. (Bixby, Weinberg)
- The public probably perceives payroll tax contributions as an indication of an exchange transaction. (Bixby, Cooper)
- Payroll tax contributions are not directly tied to benefits. (Bixby)
- The payroll tax has little significance other than political. Parts of Medicare are funded differently but have the same substance. (Robinson)

I. <u>Public perception of the commitment</u>:

- Look at the legality of the program not how the public perceives it. (Bixby)
- What the public thinks based on what the politicians say is what really matters. The public refers to SI as social contracts. (Weinberg)

J. <u>The statement of fiscal sustainability and/or non-traditional financial statements</u>:

- The Board may decide to call the balance sheet number something other than "liability" but the number should be on the balance sheet, and the change should be reported as a cost. The bottom line on the SNC equates to the budget deficit and that is the number that should be the focus. (Weinberg)

- The key issue is to capture the full governmentwide and component effect of policy changes. (Gokhale)
- The balance sheet is a snapshot in time and a statement of fiscal sustainability would help evaluate that point-in-time picture. (Zeilger)
- Disclosure of the PV information is useful in the right context. (Schaeffer, Walker)
- The fiscal sustainability report should be developed first to communicate the totality of the issue, followed by the liability standard. (Childree, Robinson) Something is needed that helps us understand what this really means in the grand scheme of things, and to decide whether a $40-trillion number is appropriate. The standard needs to be generally accepted. (Childree)
- A broad look at sustainability is needed, including all programs and sources of revenue. (Walker)
- We need to think about whether a traditional balance sheet is meaningful for a national government. Important items are not on the balance sheet. The current deeply red condition of the federal balance sheet has not motivated anyone to do anything. Out-of-the-box thinking is needed. Perhaps combine traditional balance sheet with items from fiscal sustainability. (Walker)
- FASAB should focus on improving SOSI and on sustainability reporting. (Robinson)
- “Sustainability” is not well defined. Social Security is sustainable, for example, within the statutory limits. (Goss)
- Integrating the amounts with current statements is very important. He referred to two models for linking amounts. Staying within the structure of traditional financial statements is helpful. Non-experts need a bottom line. There must be a single number to be understandable. He supports sustainability reporting but it addresses a different question. (H. Jackson)
- Table 1 in the FR Executive Summary is excellent. (H. Jackson, Fraser)
- The federal government is unique and it is worth considering whether the traditional balance sheet is helpful. (Menzel)

K. <u>The difference between the cost of federal employees and other administrative costs and SI costs:</u>

- If the government enacted a policy that everyone gets $50 then the cost of the policy is that amount. (Gokhale)
- SI costs can be likened to insurance contracts where premiums are paid and policyholders expect a benefit there from; both should be recognized by the company. (Zeilger)

L. <u>Uncertainty</u>:

- The amount of benefits is uncertain and estimates are unreliable. (Schaeffer)

M. Measurement:

- The amount should be net of future payroll taxes. (XXXX)
- If the PV were adopted all flows should be considered. (Schaeffer)
- Payroll taxes are used for other government expense they should not be subtracted. (Weinberg)
- A comprehensive measure for all beneficiaries and for past and future events is preferable. (Gokhale)
- The closed group obligation may be a useful compromise. It addresses the generation imbalance, increases over time due to implicit interest, and picks up statutory and demographic changes. Economists and actuaries are familiar with it. The closed group vested measure would be similar to how swaps are accounting for and could be useful. The fact that amounts are large should not be a deterrent. (H. Jackson)
- There are no measurement issues with the PV proposal. (Menzel)
- The PV would not offset future benefits with future payroll taxes, which would be misleading. (Fraser)

Several respondents suggested alternative approaches. Mr. Jackson's proposal is at Attachment 3. Several people testified that Table 1 from the Financial Report of the United States' Executive Summary is good starting point for discussion of possible new reporting or new financial statements, and it is provided at Attachment 4.

II. Majority of Respondents Favored Certain Positions

Although the respondents split on the obligating event and other issues, the tally of respondents' comment letters indicates that a majority of respondents may favor the following positions:

1. Social Security and Medicare obligations are measurable for the purposes of recording a liability after 40 quarters or equivalent work in covered employment.
2. Line items should not be added to SOSI. The current format is preferred.
3. The reasons for changes in SOSI amounts should be reported, and there should be a new basic statement for this purpose.
4. A sustainability reporting should be developed either in the SI project or separately.
5. Reporting "excess" payroll taxes as deferred revenue either is not favored or should not be a part of the SI project.

III. FASAB Consensus

When the Board issued the *Preliminary Views* document there appeared to be a consensus among members regarding several points. The members agreed that the Statement of Social Insurance (SOSI) was a useful financial statement, and that changes in SOSI amounts should be reported. However, views appeared to differ regarding the display format of the SOSI and for changes in SOSI. In addition, the members agreed that sustainability reporting is necessary and a separate project commenced. Finally, they agreed that the supplementary information required in SFFAS 17 should be continued.

On the other hand, views differed in other areas. The discussion of differing views may benefit from the following summary of the Primary View (PV) and Alternative View (AV) rationales from the bases for conclusions, focusing on the liability and associated issues.

Primary View

The PV is that the attainment of fully insured status (e.g., 40 QC) constitutes substantially meeting of eligibility requirements for Social Security and Medicare, and therefore is an obligating event and a present obligation. The PV basis for this conclusion notes that there is dissatisfaction with the SFFAS 17, "due and payable" liability and cites AICPA letters to this effect (PV par. A2). It also refers to economists and others expressing concern regarding the completeness of information. It cites Alan Greenspan on the benefits of accrual accounting (PV par. A4), and there are references to Fisher, Diamond, Orszag (PV par. A5) and Howell Jackson (PV par. A6).

The PV is that decision-makers will benefit from PV information. The balance sheet would be closer to presenting total liabilities and the SNC much closer to presenting the cost of transactions and events occurring during the period. Citizens and intermediaries would gain access to information used by experts (PV par. A7).

Pursuant to the liability definition in the *Elements* ED, a liability of the Government has two essential characteristics: (1) it constitutes a present obligation and (2) the Government and the other entity have an agreement or understanding as to when settlement is to occur. Present obligations require past obligating transactions or events; such events are critical for liability determination (PV pars. A12-A13). The existence of an obligation is determined with reference to current law (PV par. A14).

Expenses include increases in liabilities (PV pars. A9-A11). The expense to be recognized is consistent with the SI benefit formula. (PV par. 55).

The PV is that obligating events for Social Security, Medicare and RRB occur when participants substantially meet eligibility conditions and attain fully insured status by completing sufficient work in covered employment. Obligating events also occur when subsequent work increases their future benefit (PV pars. A16, A39). The Government and the participant have an agreement or understanding concerning settlement at that point (PV par. A39). Thus, the definition is satisfied. At this point economic cost is incurred the omission of which results in incomplete reporting (PV par. A17).

Distinction between "exchange" and "nonexchange" transactions is not determinative. Expenses may be incurred and liabilities arise equally for exchange, nonexchange, and quasi-exchange transactions (PV par. A18).

Work in covered employment before "fully insured" status is not an obligating event because participants are not <u>eligible</u> for benefits at that point (PV par. A40).

Uncertainty is addressed through measurement (PV par. A39). Measurement uncertainty can be tolerated if clearly explained (PV par. A67).

The PV rationale concludes by noting that the balance sheet and SNC are primary means of communication (PV par. A100).

Alternative View

The AV is that social insurance reporting should be designed to meet its unique nature. Additional reporting proposed (AV par. 115). Financial reporting should help users understand and evaluate the:

- current status and longer-term fiscal sustainability of SI and other programs, as well as the inter-generational effects and potential effect on individuals' long-term planning (AV par. A116);
- impact of the Government's operations on the financial condition of the Government and the nation, as per SFFAC 1 (AV par. A117);
- long-term sustainability of federal programs (AV par. A118).

Such reporting should consider indicators of fiscal sustainability, factors affecting federal costs, sensitivity of the estimates, and many other factors (AV par. A119).

The AV is that the complex nature of the Government requires an expanded model. FASAB has provided a model with additional statements that can be articulated, bridged, or aligned into an integrated framework (AV par. A120).

SI is a category of program unique to government, usually at the national level, designed to protect against hazards that might produce large dependency problems (AV par. A122). SI is compulsory. Participants do not select the kind or amount of protection or the price (AV par. A123). SI is a pay-as-you-go program (AV par. A125). SI is a deliberate inter-generational transfer. Little correlation exists between taxes and benefits (AV par. A126). Nor is SI like private insurance where there is a direct relationship between risk and premiums paid (AV par. A127); nor like employee benefits that feature exchange transactions (AV par. A128).

The AV is that the liability and related expense for SI benefits should continue to be recognized when benefits become "due and payable" for several reasons, including

1. future scheduled benefits are not present obligations,
2. recognizing future benefits would result in a mismatch of costs and transfers or services, and
3. amounts are not reasonably estimable given the government's ability to change the SI laws and the unsustainability of current benefits (AV pars. A133-A137).

SFFAS 5 notes that the distinction between exchange and nonexchange transactions is important in determining the point of liability recognition (AV par. A135-A136). The Supreme Court has affirmed the right of Congress to modify law. The Government is not bound in its policy decision by previous actions (AV par. A137). Nor would it be a liability under the *Elements* ED because the Government is not committed or bound to make SI or other benefit payments until all eligibility criteria are met (AV par. A139-A141). Government costs should be matched year by year with the delivery of services (AV par. A142).

SI is like defense and public education: costs that are highly likely to continue but are not recognized as costs of the current period. They will be financed by future taxes. There is not present obligation to provide them (AV par. A143).

In addition, the enormity of the SI "liability" would distort the amounts related to other activities and render them insignificant (AV par. A144).

Given the ability of the government to change the laws and the unsustainability of current benefits under current financing, amounts are uncertain and not reliably estimable (AV pars. A133, A145).

The Alternative View is that the PV is inconsistent with public sector accounting standard setters' opinions (AV par. A110 -A114).

IV. IPSASB Update

Staff notes that at its meeting on July 3-6, 2007, the IPSASB decided to issue three documents following review at the November 2006 meeting. The documents are:

(1) an exposure draft ("Social Benefits: Disclosure: Cash Transfers") requiring disclosure of the present value of cash transfers to those attaining threshold eligibility,
(2) a consultation paper ("Social Benefits: Issues in Recognition and Measurement") seeking input on some key issues in recognition and measurement of expenses and liabilities related to social benefits, specifically, when a present obligation arises for cash transfers and the impact of contributions and earmarked taxes, present obligations for individual goods and services, and revalidation of eligibility criteria as a recognition criterion or measurement attribute; and,
(3) a project brief regarding fiscal sustainability.

V. Areas Where Board Members' Views Differ and/or in which Members (or Respondents) Have Expressed Interest

Based on the *Preliminary Views* document and the discussion at the May 23 hearing, the following are areas where members' views differ:

1. The event within social insurance programs that would satisfy the "present obligation" requirement of the liability definition

2. The effect of current law and Congress' ability to change current law

   A key issue regarding "legal enforceability" is the differing views on the effect of Congress's ability to change the law. The *Elements* ED, paragraph 44, states that:

   > To meet the definition of a liability, the federal government's contract or other agreement to provide assets or services … must be based on *existing* conditions, including current law, because an essential characteristic of a liability is that the government has a *present* obligation, even if conditions may change before settlement is due. … [L]iabilities and all other elements of accrual-basis financial statements are based on transactions or events that already have occurred. The government's power to change existing conditions does not preclude what otherwise would be a present obligation and recognized as a liability.

3. The meaning of "legally enforceable" and/or "legal liability"

   Some argue that SI benefits are not "legally enforceable" and/or a "legal liability." The Board has not defined these terms. Some may view them narrowly to denote a claim enforceable via judicial process immediately or soon. Others may view "legal enforceability" more broadly; for example, a claim eventually enforceable when or if it matures. For example, interest on Treasury debt is payable when it matures. Some claims are contingently enforceable and/or potentially enforceable via judicial process, e.g., insurance claims. SI benefits are payable if the participant lives to be 62 or older, dies with survivors, or is disabled. Other contingent claims include lawsuits and environmental responsibilities.

4. What a "liability" on the balance sheet would or should communicate

5. The appropriate SI cost, e.g., the conceptual difference between (1) the cost of federal employees and other administrative costs and (2) SI costs, if any

6. What other national governments are reporting on accrual financial statements comparable to the FR

7. The effect of reporting a long-term liability on efforts to reform Social Security and Medicare [Note: Members seem to agree that this point is not relevant to the discussion of GAAP.]

8. SOSI format:

   A. PV – SOSI line item links to balance sheet; add section for SOSI changes
   B. AV – retain current SOSI and add a new basic statement analyzing SOSI changes

9. Other:

   A. ?

Staff requests member feedback on the above issues, which it plans to develop along with others to be identified in the future. For example, are these issues of interest to the members? What other issues should the staff develop?

VI. <u>Possible Alternative Approaches</u>

There appears to be a consensus on certain components of a draft social insurance standard. The staff wishes to confirm that there is agreement on these components.

First, the future exposure draft on social insurance accounting should require the current Statement of Social Insurance (SOSI) as well as a statement of changes in SOSI amounts. The exact format for the statement of changes is to be determined.

In addition, sustainability reporting is necessary. There is a separate project on that subject, and the staff assumes that that project will address the subject. However, the members may wish to ensure that the proposal resulting from the separate project precedes the SI exposure draft.

Finally, members agreed that the supplementary information required in SFFAS 17 should be continued.

Regarding the basic areas where the members' views differ, the staff suggests the following alternative approaches for the Board's consideration. They are based on ideas presented in the *Preliminary Views* document and/or expressed by respondents or Board members. The staff could develop any of these as the Board wishes:

1. Primary or Alternative View – One approach, of course, is to adopt either the PV or AV as presented in the *Preliminary Views* document.

2. Modify the Primary or Alternative View – Another approach would be to adopt a modified version of either the PV or the AV. One option associated with the PV is to conclude that, although the liability definition (in *Elements* concept statement) is satisfied when participants substantially meet the eligibility requirements for fully insured status (e.g., 40QC), the second recognition requirement (in the *Elements* statement) regarding measurability leads to a "threshold liability" for the balance sheet. The "threshold" obligating event occurs when a participant is eligible for immediate annuity or survivor or disability benefits, e.g., at 62 or 65 years of age. The *Elements* statement states that measurement may require the use of estimates or approximations and an assessment of the probability that future inflows or outflows … will result from them (*Elements*, par. 7). The uncertainty and order of magnitude associated with Social Security and Medicare at 40 QC or equivalent may be considered outside relevant range of the current balance sheet model. Although the SOSI present values are audited now, they are presented in financial statement developed for that specific purpose. Advantages of recognizing the threshold amount include that it is consistent with the amount that the IPSASB's current exposure draft regarding accounting for social benefits requires to be disclosed as the liability in the notes. In addition, this amount ties to current SOSI line items.

3. Expansion of the Current Reporting Model – The current reporting model can be expanded, either by adding a new section to the existing balance sheet or develop a new statement. See Attachment 4 for Table 1 from the executive summary of the 2006 FR about which respondents have spoken favorably.

   Reporting different levels of information is similar to the Financial Accounting Standards Board (FASB) approach regarding "other comprehensive income." FASB issued FAS 130, *Reporting Comprehensive Income*, in June 1997. FAS 130 establishes a standard for disaggregated reporting and display of comprehensive income and its components (revenue, expense, gains, and losses). In addition, other FASB statements require segregation of comprehensive income components, for example FAS 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)*.

   The FASB and International Accounting Standards Board (IASB) are currently working on a financial statement presentation project the objective of which is to explore ways of presenting information in individual financial statements (and among the financial statements) that improve the ability of investors, creditors, and other financial statement users to:

- Understand an entity's present and past financial position
- Understand the past operating, financing, and other activities that caused an entity's financial position to change and the components of those changes
- Use that financial statement information (along with information from other sources) to assess the amounts, timing, and uncertainty of an entity's future cash flows.

Developing additional levels for the federal balance sheet and/of statement of net cost may be appropriate for the SI project at this time. Additional levels may be useful in communicating the nature of federal liabilities. For example, liabilities arising from what have been referred to as "social contracts" by some might be distinguished from those arising from exchange-related contracts. [Note that this might be characterized as a "continuum" of liabilities and align with the "continuum" discussed in item 4 below.]

4. <u>New Element for the Existing Reporting Model</u> – A new element could be considered that would be part of net position but not a "liability," e.g., "obligations," "commitments," "responsibilities." This approach would develop the notion of a continuum[3] that some members introduced at the May 23 hearing. The continuum could be characterized not as a "liability continuum" but as "responsibility" or other continuum containing all types of federal commitments, e.g., social welfare, disaster relief, social insurance, other federal insurance, federal employee benefits, Treasury and other "full faith and credit" federal securities, and contract obligations.

<u>Attachments</u>

Attachment 1 – Staff Summary of Responses **(**updated from May 2007 edition**)**
Attachment 2 – Summary/"minutes" of May 23 hearing
Attachment 3 – Howell Jackson's Proposal
Attachment 4 – Table 1, FR Executive Summary
Attachment 5 – Worksheet re Tabulation of Respondents Comments

[3] Webster's defines continuum as 1: a coherent whole characterized as a collection, sequence, or progression of values or elements varying by minute degrees ….