



February 19, 2009

Memorandum

To: Members of the Board

From: Richard Fontenrose, Assistant Director

Through: Wendy M. Payne, Executive Director

Subj: TAB C2, Staff Analysis of Comment Letters on the Exposure Draft *Accounting for Social Insurance, Revised*¹

MEETING OBJECTIVES

To review the comments received in response to the exposure draft *Accounting for Social Insurance, Revised*, proposing amendments to SFFAS 17, *Accounting for Social Insurance*, and consider issues raised by respondents (see issues starting on page 3). Decisions made at the meeting will enable staff to resolve issues and prepare a pre-ballot draft standard for your consideration at the April meeting.

STAFF ANALYSIS

Overall Summary	2
Issues Raised -- Staff Analysis and Recommendations	3
Broad Issue 1:	3
Broad Issue 2:	7

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.

TAB C2

Broad Issue 3:.....	9
Other Pending Issues	10

Overall Summary

Table C – Overall Summary by Question (see Attachment 1 for tables of responses updated as of February 18. See Attachment 2 for comment letter #24, which was received after the initial distribution on February 13.)

Note: The denominator for each question is the number of respondents answering the related question with a yes or a no. The denominator excludes those not addressing the topic or whose response was not a clear yes or no. Staff exercised judgment in determining whether a clear yes or no answer was provided.

- Q1. A majority of respondents (15 of 21) **agree** that key measures should be presented in the MD&A as described in this exposure draft.
- Q2. A majority of respondents (16 of 21) **disagree** that the balance sheet should present a line item for the closed group measure as described in this exposure draft.
- Q3. A majority of respondents (12 of 20) **agree** that the SOSI should have a summary section as described in this exposure draft.
- Q4. A majority of respondents (16 of 19) **agree** that there should be a new basic financial statement explaining changes to the present value amount included in SOSI.
- Q5. A majority of respondents (11 of 20) **disagree** that an accrued benefit obligation should be disclosed as described in this exposure draft.
- Q6. A majority of respondents (17 of 20) **agree** that the SNC should not include a line item for the change during the period in the closed group measure, which would be presented below exchange revenue and expenses and not included in the totals for these classifications.
- Q7. A majority of respondents (14 of 19) **disagree** with the decision to feature the closed group measure in the financial reporting.
- Q8. A majority of respondents (11 of 17) **agree** with a general requirement that allows flexibility in the sensitivity analysis presented will produce better information regarding the sensitivity of social insurance programs.

Issues Raised -- Staff Analysis and Recommendations

The following discusses three “broad issues” from the comments received as of February 18, 2009. They are issues that constitute the respondents’ main areas of disagreement with the proposed standard, and with each other. They involve the appropriateness of (1) the closed group measure for social insurance, as a concept, and/or its display on the balance sheet or any basic financial statement or, indeed, anywhere in a financial report prepared on the basis of generally accepted accounting principles; and (2) the note disclosure of the accrued benefit obligation. These issues involve Questions for Respondents 2, 5, and 7 in the exposure draft.

There are other issues involving each of the other Questions for Respondents. For example, a large majority of respondents (15 of 21) agree that key measures should be presented in the MD&A as described in this exposure draft. However, some respondents disagree that the standard should specify exactly what measures should be discussed, and especially not specify the closed group measure. The objection to the closed group measure reflects their views on the main issues and is presented below in the “broad issues” discussion.

Similarly, a majority of respondents (12 of 20) agree that the statement of social insurance should have a summary section as described in this exposure draft. However, other respondents disagree with a summary and, again, especially with displaying the closed group measure in a summary, which, again, reflects their views regarding the closed group generally.

As the Board is well aware, the closing date for comments on the social insurance ED was very recent. The original, tentative target date for a hearing on social insurance and initial discussion of issues was April 2009. We decided to accelerate consideration of the social insurance in order to have a joint hearing for both EDs, after considering the significant advantages of doing so; but, a disadvantage of doing so is that a comprehensive staff analysis of all the social insurance issues is not possible at this time. However, I believe that the extensive basis of conclusion in the social insurance ED explores the main issues raised by the respondents, as presented below. Thus, the Board has considered many of the issues and may be ready to make some decisions at this time on that basis. I have listed “questions for the board” below for that purpose. I anticipate that the “broad issues” and other issues will need to be developed further for the April meeting. I plan to prepare a detailed staff analysis and staff recommendations, as needed, after the hearing on February 25 and the Board’s discussion on February 26.

Broad Issue 1:

A majority of respondents (16 of 21) disagree that the balance sheet should present a line item for the closed group measure as described in this exposure draft, which is Question for Respondents 2.

This issue also encompasses Question for Respondents 7, where a majority of respondents (14 of 19) disagree with the decision to feature the closed group measure in

the financial reporting, additional points regarding which are presented below as “Broad Issue 3.”

Key points raised by respondents regarding Broad Issue 1 centered around 4 main arguments:

1. *The closed group measure for social insurance is inappropriate for the balance sheet or any basic financial statement.*
 - a. *The closed group measure is a liability measure and is not meaningful for social insurance programs since they are not liabilities.*
 - i. *No exchange has occurred and no such irrevocable commitment exists.*
 - ii. *Including such information on the face of the balance sheet would, at a minimum, result in confusion among financial statement users, and could even be viewed as misleading.*
 - iii. *A social insurance commitment is a future event.*
 - b. *The balance sheet, which by definition presents assets and liabilities at a single point in time, is not the appropriate place to display social insurance commitments or obligations on either an open or a closed group basis.*
 - c. *The SOSI is the appropriate vehicle for presenting the open group line item. Its purpose is to “illustrate the extent to which future revenues will be sufficient to pay future benefits.” It does not seem appropriate to “crosswalk” between items presented on the balance sheet and on the SOSI, since the statements are trying to convey information over different points in time.*
 - d. *If deferred revenues of future taxes are not recorded, it is misleading to have future liabilities recorded on the balance sheet ... based on the matching principle of accounting.*
 - e. *The balance sheet is a historical measure as of a certain date.*
2. *The closed group measure for social insurance is inappropriate anywhere in the financial report – the financial statements, notes, or RSI.*
 - a. *We agree with the alternative view put forth by Mr. Werfel in paragraph A144.*
 - b. *The closed group measure is not at all relevant to the financial status of programs financed on a current-cost, pay-as-you-go basis.*
 - i. *It is misleading and would encourage a fundamental misunderstanding of the financing basis for the programs.*
 - ii. *Any program with future obligations that are intended to be and will be financed on a current-cost, pay-as-you-go basis as obligations come due will have a substantial closed group shortfall, even when financing is expected to be perfectly adequate on a current-cost basis.*

- iii. *While the closed group measure is presented in the Social Security Trustees Report, it is displayed along with the net present value for future participants, solely as an illustrative decomposition of the open group measure.*
 - *The decomposition represents a generational perspective that may be of interest from a relatively academic analytical perspective, but it has no relevance at all to the financial status of a current-cost-financed or a pay-as-you-go system.*
 - *The closed group measure is also currently included in the [SOSI] where it is described and explained in more detail in the supporting disclosures.*
 - iv. *The FASAB should encourage further disclosure and emphasis on measures that illustrate the timing and trend in annual government obligations and cash-flow balances that are critical to an understanding of sustainability of the various government programs.*
 - c. *The open group measure is the appropriate measure for pay-as-you-go programs because it includes all future cash flows over the projection period and therefore addresses the sustainability of the program.*
 - d. *The argument that more measures and illustrations are necessarily better is appealing but false. Readers of any document, including the governmentwide entity financial statements, have limited time and attention that can be devoted to that particular document.*
3. *The balance sheet should not display “commitments.”*
- a. *Including a commitment line item on the balance sheet would be misleading to the reader because no clear definition of a commitment exists in accounting literature issued by FASAB or OMB.*
 - b. *The ED seems inconsistent in not proposing to add other significant long-term commitments, such as those for defense and education.*
 - c. *The balance sheet shows the government’s financial position at a certain point in time and this includes showing only liabilities that are present obligations. By including this new line item, it would appear to be including future benefits as a liability. A liability can only occur when the entity does not have the ability to single-handedly alter the liability. In the case of the Social Security program, the federal government retains the right to alter the benefit up until the point when the benefit is due.*
 - d. *The Board bases its proposal for adding a line for the closed group measure to the balance sheet ... on what the Board describes as a liability-commitment-expectation continuum. ... In fact no such continuum exists. Rather, federal programs fall onto a multi-dimensional array of combinations regarding the source, degree of certainty and timing of funding and expenditures. ... The variety of funding mechanisms for federal programs is*

too broad to place on a single continuum. The ED fails to provide any compelling argument that the five covered programs are both so similar to each other yet so distinct from other government programs as to require special treatment on the balance sheet.

- e. As noted in par. A98, the below-the-line item is not an element and, therefore, should not be included on the balance sheet as proposed. However, if the line was, instead, changed to a note to the balance sheet appearing both on the bottom of the balance sheet and as a note to the liability section of the balance sheet, then what the ED seeks to accomplish “might” be achievable (emphasis in original).
4. A liability greater than “due and payable” should be shown as such on the balance sheet.
- a. I agree with Mr. Patton that ALL liabilities should be shown as such on the balance sheet (emphasis in original).
 - b. The Board should continue to deliberate on the possibility of recognizing some form of liability and/or obligation associated with social insurance within the balance sheet and statement of net cost.
 - i. It is difficult to appreciate how either the compromise position or the alternative view expressed by Mr. Werfel serves the information needs of the citizens, the Congress, or the Administration.
 - ii. The compromise position on balance sheet disclosure and Mr. Werfel’s view does not acknowledge that non-exchange transactions can impose a “liability” on the government in selected instances.
 - iii. The alternative view of Mr. Werfel appears to rely on notions presented in the Preliminary Views document—which are not otherwise found in accounting theory.
 - iv. The alternative view of Mr. Patton opens the door to possibly recognizing some portion of social insurance on the balance sheet and in the statement of net cost. Such options for recognition that could be tied to FASAB concepts and accounting theory.
 - v. The points made within the ED that are supportive of the above approach to recognition and disclosure, by way of illustration, include:
 - a. Conditions for receiving a future benefit are substantially met when the participants become fully insured, and the omission of the effects of these events results in an incomplete reporting of costs and liabilities.
 - b. An expense may be incurred and a liability may arise equally for exchange, nonexchange, or quasi-exchange transactions so long as a present obligation exists. “ and “...the use of “trust funds” and the “investment” of excess payroll taxes in special Treasury securities, arguably creates a constructive

obligation at a point much earlier in time than when the payments are due and payable.”

- c. *The “accrued benefit obligation” is the most truthful amount of the Social Security and Medicare “obligation”. This amount should be presented on the face of the balance sheet as a liability.*

Questions for the Board (QfB) Regarding Broad Issue 1:

- 1. Should the balance sheet present a line item for the closed group measure as described in this exposure draft?

Broad Issue 2:

A majority of respondents (11 of 20) disagree that an accrued benefit obligation should be disclosed as described in the exposure draft, which is Question for Respondents 5.

Key issues raised by respondents centered around 4 main arguments:

- 1. *One respondent commented that he found the accrued benefit obligation irrelevant.*
- 2. *The accrued benefit obligation does not reflect the realities of a social insurance program.*
 - a. *The accrued benefit obligation is calculated based on current participants only (closed group), not considering the current cost financing principle of Social Security.*
 - b. *Projected shortfalls in expected financing for social insurance programs should only be presented on a basis that properly accounts for the intended financing of the program. For a current-cost-financed program like Social Security, only the open group measure is appropriate. The closed group measure, and the even more specific “accrued benefit obligation” are inappropriate and misleading and do not contribute to the understanding of the financial challenges presented by the program.*
- 3. *The accrued benefit obligation would not provide meaningful information to the readers of the financial statements.*
 - a. *The term “obligation” may be misleading to users in this context since it implies that the government has an “obligation” or liability to participants.*
 - b. *The accrued benefit obligation is a measure of the future benefit obligation based on past earnings and past work in covered employment as of the*

valuation date. The accrued benefits obligation is simply not a meaningful number for an ongoing pay-as-you-go social insurance program.

4. *The financial statements already include extensive information on social insurance programs.
 - a. *There is a limit as to how much information can be reasonably absorbed.*
 - b. *Another measure of social insurance commitments would likely confuse and mislead users of the financial statements.**
5. *Absent any realistic possibility of the federal government terminating these programs in a manner similar to an employer sponsored pension plan, which is what this measure implies, including accrued benefit obligation information would be both inappropriate and a step in the wrong direction.*
6. *Several respondents said the difficulty in defining the basis for computation of this measure is enormous.*
7. *The Board claims this new disclosure comes at the request of users, but does not attempt to explain how it would be used other than “to provide information for the many users who are interested in knowing what such an amount might be and in evaluating the obligation in this way.” He found this rationale is simply too vague to be compelling.*
8. *Social insurance programs are appropriately characterized as statements of intent for future benefits of a general nature, but do not make commitments to any level of benefits that may be scheduled in current law. The historical record makes this clear. Projected shortfalls in expected financing for social insurance programs should only be presented on a basis that properly accounts for the intended financing of the program. For a current-cost-financed program like Social Security, only the open group measure is appropriate.*

Question for the Board Regarding Broad Issue 2:

2. Should an accrued benefit obligation be disclosed as described in this exposure draft?

Broad Issue 3:

A majority of respondents (14 of 19) disagree with the decision to feature the closed group measure in the financial reporting, which is Question for Respondents 7.

Key issues raised by respondents centered around 4 main arguments:

1. *The use of an open group measure is essential in performing an accurate sustainability analysis.*
 - a. *An open group measure projects all future cash flows over a given period.*
 - b. *The closed group measure fails to reflect the financing principle of the Social Security program, where working individuals pay the benefits of retired or disabled individuals. Ignoring this concept makes it appear that benefits to current participants would not be payable to a far greater degree than is appropriate.*
 - c. *Social insurance sustainability, policy, and other related changes are more accurately illustrated in changes to the open group measure for all participants.*
2. *The Social Security and Medicare Trustees Reports emphasize almost exclusively the open group.*
 - a. *The closed group is only presented as an illustrative component of the theoretical decomposition of the open group from a generational perspective. This kind of academic analysis has no relevance in a financial statement. Focusing on the closed group measure would inappropriately magnify the difference between projected obligations and projected taxes and would be misleading and confusing for readers of the financial statements.*
3. *The closed-group measure is not a good estimate of the net responsibility of future taxpayers.*
 - a. *Under current law, some of the scheduled benefits to the closed-group participants would not be payable even with the receipt of all scheduled taxes from future participants over the next 75 years.*
 - b. *The closed-group measure reflects only current program beneficiaries and participants and assumes that the program is closed to future participants, which contradicts the pay-as-you-go financing principle on which the social security program was designed.*
4. *Closed-group measures are typically used for private sector pension plans and retiree health programs where individuals perform services in exchange for such benefits as part of their compensation. However, social insurance transactions are nonexchange transactions. That is, payments of social insurance taxes by an individual (which do not entitle the individual to a benefit in a legal or contractual*

TAB C2

sense), and the subsequent receipt of social insurance benefits by that individual are not directly based upon taxes paid or employment services rendered, and are separate nonexchange transactions.

Question for the Board Regarding Broad Issue 3:

QfB3. Should the standard feature the closed group measure in the financial reporting?

NEXT STEPS

Other Pending Issues

Questions for the Board (from the questions for respondents in the ED):

QfB4. Should key measures be presented in the MD&A as described in this exposure draft?

QfB5. Should the SOSI have a summary section as described in this exposure draft?

QfB6. Should there be a new basic financial statement explaining changes to the present value amount included in SOSI?

QfB7. Should SNC not include a line item for the change during the period in the closed group measure?

QfB8. Should there be a general requirement that allows flexibility in the sensitivity analysis of social insurance programs?

The issues immediately above will be discussed in subsequent staff memoranda. I will prepare a more detailed staff analysis and staff recommendations, as needed, after the hearing on February 25 and the Board's discussion on February 26.

TAB C2, Attachment 1 – Updated Tables of Comment Letters

RESULT: Summary of Respondents

As of February 19, 2009, we have received 24 responses from the following sources:

	FEDERAL (Internal)	NON-FEDERAL (External)
Users, academics, others	2	14
Auditors	2	
Preparers and financial managers	6	

Table A – Tally of Responses by Question

QUESTION	YES/AGREE	NO/DISAGREE	NO COMMENT
<p>Q1. The Board proposes to require social insurance component entities and the governmentwide entity to discuss and analyze key measures from the basic financial statements in their management’s discussion and analysis (“MD&A”). See paragraphs 26-30 in the proposed standard and paragraphs A75-A79 in the basis for conclusions. Do you believe that key measures should be presented in the MD&A as described in this exposure draft?</p>	15	6	3
<p>Q2. The Board is proposing to add a line for the closed group measure to the balance sheet below assets, liabilities, and net position and not included in the totals for these classifications.² See paragraphs 31-32 in the proposed standard and paragraphs A81-A100 in the basis for conclusions. Two members have submitted alternative views on this issue. See paragraphs A139-A142 in the basis for conclusions for Mr. Patton’s view. Mr. Patton and other members believe that a liability greater than the due and payable amount should be recognized on the balance sheet. See paragraph A144 in the basis for conclusions for Mr. Werfel’s view. Mr. Werfel and other members believe that the closed group measure should not be presented on the balance sheet. Do you believe that the balance sheet should present a line item</p>	5	16	3

² Definitions of certain terms are provided in the Definitions section and Appendix F: Glossary of this proposed standard.

TAB C2, Attachment 1 – Updated Tables of Comment Letters

QUESTION	YES/AGREE	NO/DISAGREE	NO COMMENT
<p>for the closed group measure as described in this exposure draft?</p>			
<p>Q3. The Board proposes to add a new summary section of the statement of social insurance (“SOSI”) to present the closed and open group measures. See paragraphs 34-35 in the proposed standard and paragraphs A114-A116 in the basis for conclusions. Do you believe that the SOSI should have a summary section as described in this exposure draft?</p>	12	8	4
<p>Q4. The Board proposes a new basic financial statement entitled “statement of changes in social insurance amounts.” The new statement would explain the changes during the reporting period in the present value amounts for the closed group measure included in the statement of social insurance. See paragraphs 36-37 in the proposed standard and paragraph A116 in the basis for conclusions. Mr. Werfel and other members have an alternative view. They believe the new statement should focus on changes in the open group measure and not the closed group measure. The question of the use of the appropriate measure is addressed in question 7 below. See paragraph A145 in the basis for conclusions. Do you believe there should be a new basic financial statement explaining changes to the present value amount included in SOSI?</p>	16	3	5
<p>Q5. The Board proposes to disclose an accrued benefit obligation in notes to the financial statements. This information would include a five year trend when the standard is fully implemented. See paragraph 38 in the proposed standard and paragraphs 117-123 in the basis for conclusions. Mr. Werfel and other members have an alternative view expressing opposition to this disclosure. See paragraph A146 in the basis for conclusions. Do you believe that an accrued benefit obligation should be disclosed as described in this exposure draft?</p>	9	11	4
<p>Q6. The Board considered but decided not to propose adding a line item to the statement of net cost (“SNC”) for the change during the reporting period in the closed group measure that would be presented below exchange revenue and expenses and not included in the totals for these classifications. Some argue that this measure should not be presented on the SNC because it is a fundamentally different measure.</p>	17	3	4

TAB C2, Attachment 1 – Updated Tables of Comment Letters

QUESTION	YES/AGREE	NO/DISAGREE	NO COMMENT
<p>Others believe the change is an economic cost that belongs on the SNC, and that including this number at the bottom of the SNC appropriately links all basic financial statements. See paragraphs A101-A113 in the basis for conclusions.</p> <p>Do you believe that the SNC should not include a line item for the change during the period in the closed group measure, which would be presented below exchange revenue and expenses and not included in the totals for these classifications?</p>			
<p>Q7. The Board decided to present the closed group measure (CGM) (defined in paragraph 19) as a common thread among the proposed new reporting. The proposal requires that the CGM and other key measures from the financial statements be discussed in management’s discussion and analysis; that the CGM be presented on the balance sheet below assets, liabilities and net position (without being included in the totals for those categories); and that the changes in the CGM during the reporting period be presented and explained in the new summary section of the statement of social insurance and the new statement of changes in social insurance. The Board considered the open group measure (defined in paragraph 24) instead of the closed group measure as the focus for the disclosure. This exposure draft discusses both the closed group measure and the open group measure throughout. Paragraphs A69-A74 provide the basic rationale for the Board’s selection of the closed group measure. Mr. Werfel and other members have an alternative view regarding the presentation of the closed group measure. They oppose the addition of the closed group measure to the balance sheet. Further, they believe the open group measure is the appropriate measure to use in the new statement of changes in social insurance and not the closed group measure. See paragraph A145 in the basis for conclusions.</p> <p>Do you agree with the Board’s decision to feature the closed group measure?</p>	5	14	5
<p>Q8. The Board is proposing to change the requirement currently in SFFAS 17 for specific sensitivity analysis. The standard will require the entity to provide sensitivity analysis of the closed and open group measures appropriate for its particular social insurance program but will</p>	11	6	7

TAB C2, Attachment 1 – Updated Tables of Comment Letters

QUESTION	YES/AGREE	NO/DISAGREE	NO COMMENT
<p>not specify a particular approach for the analysis. See paragraphs 42-43 of the standard and paragraphs A125-A137 of the basis for conclusions.</p> <p>Do you believe that a general requirement that allows flexibility in the sensitivity analysis presented will produce better information regarding the sensitivity of social insurance programs?</p>			

Table B – Quick Table of Responses by Question

Key to Respondents

	Name	Organization	Category
1	Douglas Jackson	Individual	Non-federal, Other
2	Dick Young	Individual	Non-federal, Other
3	Juan Kelly	Mahoney and Associates	Non-federal, Other
4	Kenneth Winter	Individual	Non-federal, Other
5	David M. Walker	Peter G. Peterson Foundation	Non-federal, Other
6	Mary Glenn-Croft	Social Security Administration, Office of Chief Financial Officer	Federal Preparer
7	Daniel L. Fletcher	CFOC Standardization Committee, FASAB Response Group Representative	Federal Preparer
8	Steven Schaeffer	Assistant Inspector General for Audit, Social Security Administration	Federal Auditor
9	Eric Klieber	Buck Consultants	Non-federal, Other
10	Dr. Joseph Maresca	Individual	Non-federal, Other
11	Denial Kovlak	Greater Washington Society of CPAs and GWSCPA Educational Foundation	Non-federal, Other
12	Andrew Rettenmaier	Texas A & M University	Non-federal, Other
13	Stephan Goss	Chief Actuary, Social Security Administration	Federal Preparer
14	Cynthia Simpson	Labor Department	Federal Preparer
15	Richard G. Schreitmueller	American Academy of Actuaries	Non-federal, Other
16	Jagadeesh Gokhale	Cato Institute	Non-federal, Other
17	Terry Bowie	NASA	Federal Preparer
18	Sheila Weinberg	Institute for Truth in Accounting	Non-federal, Other
19	Robert Childree	AGA – Financial Management Standards Board	Non-federal, Other

TAB C2, Attachment 1 – Updated Tables of Comment Letters

	Name	Organization	Category
20	Alvin K. Winters	Individual	Non-federal, Other
21	The Honorable Jim Cooper	House of Representatives	Federal, Other
22	Frank Murphy	Department of Housing and Urban Development	Federal Preparer
23	Jeanette Franzel	Government Accountability Office	Federal Auditor
24	Douglas W. Elmendorf	Congressional Budget Office	Federal, Other

Table B – Quick Table of Responses by Question

Respondent ▼	1 Do you Agree?	2 Do you Agree?	3 Do you Agree?	4 Do you Agree?	5 Do you Agree?	6 Do you Agree?	7 Do you Agree?	8 Do you Agree?
1	Yes	No	Yes	N/C	Yes	No	N/C	N/C
2	N/C							
3	Yes	No	Yes	No	No	Yes	No	No
4	N/C							
5	Yes	No	No	Yes	No	Yes	No	Yes
6	No	No	No	Yes	No	Yes	No	Yes
7	No	No	No	Yes	No	Yes	No	Yes
8	No	No	Yes	No	No	Yes	No	Yes
9	Yes	No	No	Yes	No	Yes	No	Yes
10	N/C							
11	Yes	Yes	Yes	Yes	Yes	Yes	No	No
12	Yes							
13	No	No	No	Yes	No	Yes	No	No
14	No	No	Yes	Yes	Yes	Yes	N/C	Yes

TAB C2, Attachment 1 – Updated Tables of Comment Letters

Respondent ▼	1 Do you Agree?			2 Do you Agree?			3 Do you Agree?			4 Do you Agree?			5 Do you Agree?			6 Do you Agree?			7 Do you Agree?			8 Do you Agree?		
	15	No			No			No			Yes			No			Yes			No			No	
16	Yes			Yes			N/C			N/C			N/C			N/C			No			N/C		
17	Yes			No			No			Yes			No			Yes			No			Yes		
18	Yes			Yes			Yes			No			Yes			No			Yes			N/C		
19	Yes			No			Yes			Yes			Yes			Yes			Yes			Yes		
20	Yes			No			No			Yes			No			Yes			No			No		
21	Yes			Yes			Yes			Yes			Yes			No			Yes			N/C		
22	Yes			No			Yes			Yes			Yes			Yes			No			Yes		
23	Yes			No			Yes			Yes			No			Yes			No			No		
24	Yes			No			Yes			Yes			Yes			Yes			Yes			Yes		
Totals	15	6	3	5	16	3	12	8	4	16	3	5	9	11	4	17	3	4	5	14	5	11	6	7
Legend – N/C – no comment																								

CBO Comments on FASAB Statement of Social Insurance Exposure Draft
Draft: February 13, 2009

CBO believes that on net, the proposal would improve the Statement of Social Insurance. However, there are two shortcomings in the current proposal that would considerably limit its use to policymakers and might even present a misleading message about the state of federal finances. Moderately expanding the presentation in two ways would make the SOSI substantially more useful to readers and relevant to the policymaking process.

First, the draft requires that Social Security and Medicare cash flows be presented as a share of GDP and taxable payroll. However, all present value figures are shown in dollars only. The standard should require that present value measures be shown as a share of the present value of GDP and taxable payroll over the same period.

The current SFFAS 17 requires that cash-flow measures be shown in both nominal dollars and relative to GDP and, if applicable, taxable payroll. The proposed amendment would no longer require the values to be shown in nominal dollars, a great improvement.³ (For example, the Social Insurance Supplemental Information in the 2008 Financial Report presents the confusing and misleading fact that in nominal dollars, OASDI outlays will grow to over \$20 trillion by 2080 (Chart 2, p.123).)

Similarly, in the discussion of Fiscal Sustainability Reporting, the board notes that presenting present values “in a meaningful base such as GDP is required to assist readers in understanding large dollar amounts.” (A49a)

In the SOSI currently, that requirement applies only to the cash flow measures. But nothing in the current or proposed standard *prohibits* other values from being presented relative to a meaningful base. Yet in the current SOSI and in the appendices of the draft, every value other than the cash flows is given in dollars only. As a result, readers will have great difficulty interpreting the policy implications of the report.

CBO strongly recommends that the Board require all values in the SOSI to be presented as a share of a relevant base, such as GDP, taxable payroll or both. Preferably, that presentation would come before the tables that show dollar values.

Current values (e.g., the Table of Key Measures and the Balance Sheet): Even for expert readers who know the current value of GDP (about \$14 trillion in 2008), not presenting current values as a share of GDP makes interpreting the data difficult. Simply showing these values as a share of GDP would make the policy implications of the data much clearer for all readers.

³ Instead, the draft says: “For the OASDI and HI programs, the actuarial projections should be expressed as a percentage of taxable payroll and gross domestic product (GDP). For the SMI program, the actuarial projections should be expressed as a percentage of GDP. For the RRB program, the actuarial projections should be expressed as a percentage of taxable payroll. For the Black Lung and UI programs, the actuarial projections should be expressed in constant (or inflation-adjusted) dollars.”

Present values (e.g., Statement of Social Insurance and Statement of Changes in Social Insurance Amounts): Presenting present value measures in dollar values places an even greater burden on the reader. Virtually no one knows the present value of GDP or taxable payroll over the next 75 years. The Social Security trustees project the present value of GDP over the next 75 years to be \$768.4 trillion.⁴ As a result, the economic meaning of the numbers is obscure. Most readers are likely to react to “\$1 trillion” differently than to “0.13 percent of GDP,” though the values are equal.

Second, the current structure of the Statement of Changes in Social Insurance Amounts (SCSIA) only analyzes changes to the closed group measure and does not distinguish between the portion of the increase that is due to the addition of new participants and the growth that occurs simply because the reference date has shifted forward by a year.

An explanation of changes in the financial statement from the previous year is essential for readers to understand the government’s financial position, and the additional Statement of Changes in Social Insurance Amounts (SCSIA) is an important step in that direction. However, it has several shortcomings.

First, the proposed SCSIA would apply only to the closed group measure. It should instead focus on changes in the open group measure. It is inconsistent to include the open group measure in the SOSI balance sheet and the closed group measure as a supplement, and then address only the closed group measure in the SCSIA. (CBO does not object to explaining changes in the closed group measure or other values as supplementary information in the SCSIA.)

Second, it does not allow readers to distinguish between the portion of the change in the measures that are due to ongoing real transactions with economic significance and those that are simply due to the change in the reference date.

As the Board notes, “A present obligation requires a past transaction or some other event.” (A102). Readers may believe that an increase in the closed group balance results from an actual economic transaction. In fact, the balance can change for four general reasons, only the first two of which result from a real transaction or event:

1. Legislative change
2. Implementation of existing law (e.g., a group of participants enters the program)
3. Change in data, assumptions, or methods
4. Change of the reference date. (Present value projections are discounted to a different year. Therefore, even absent any real economic change, the value increases by the *nominal* value of the discount rate. Part of that growth is due to inflation, which has no economic or policy meaning. The other part of the growth is equal to the real interest rate. Note that this change does not include any real information, since it could have been computed the previous year.)

⁴ Table IV.B6, Note 2 (p.62) of the OASDI Trustees Report.

The proposed statement (Appendix E) has three lines with the effect of new data and assumptions (on demographics, economics, and health costs) and a line on the effect of methodological changes. It also has a line that shows the effect of legislative changes. However, the effects of implementing existing law and changing the reference date are not separated.

Finally, it is particularly important that the analyses of changes be shown as a share of GDP and/or taxable payroll. Some of the same factors that change the closed group measure (or other value of interest) can change GDP. For example, an increase in the assumed rate of inflation would increase the dollar value of a measure but would have little to no effect on that measure as a share of GDP. Similarly, a higher real interest rate would lower the present value of outlays but would also lower the present value of GDP. When only dollar values are presented, readers cannot tell how much of the difference between projected outlays under different assumptions is due directly to changes in the size of the economy and how much reflects a change in outlays as a share of the economy.

Responses to specific questions:

Q1. Do you believe that key measures should be presented in the MD&A as described in this exposure draft?

Yes.

Q2. Do you believe that the balance sheet should present a line item for the closed group measure as described in this exposure draft?

The closed group measure should not be a central part of the SOSI. As the members of the board who oppose including the closed group measure accurately observe, “the closed group measure ... contradicts the pay-as-you-go financing principle on which the social security program was designed.” (A145). However, as long as that point is made clearly and conspicuously, we see no reason to exclude the closed group measure from being shown as a supplementary measure.

Q3. Do you believe that the SOSI should have a summary section as described in this exposure draft?

Yes; a summary will be useful to many readers.

Q4. Do you believe there should be a new basic financial statement explaining changes to the present value amount included in SOSI?

Yes, but it should be greatly expanded. See discussion above.

Q5. Do you believe that an accrued benefit obligation should be disclosed as described in this exposure draft?

As for the closed group measure, we do not believe that the accrued benefit obligation should be part of the balance sheet, but we do not object to including it as

supplementary information. However, if it is included, its meaning should be clearly described so readers understand that like the closed group measure, the accrued benefit obligation is not consistent with the pay-as-you-go design of social insurance programs.

Q6. Do you believe that the Statement of Net Cost (SNC) should not include a line item for the change during the period in the closed group measure, which would be presented below exchange revenue and expenses and not included in the totals for these classifications?

We agree with the proposal to continue to exclude the change in the closed group measure. This is consistent with the presentation of the closed group measure only as a supplement to the SOSI, not in the balance sheet

Q7. Do you agree with the Board's decision to feature the closed group measure?

As explained above, we do not oppose inclusion of the closed group measure, but we believe it should be only a supplemental measure and should not be featured. Rather, the SOSI should focus on the open group measure. The SOSI should also explain that the open group measure is consistent with the pay-as-you-go design of social insurance programs, while the closed group measure is not consistent with that principle.

Q8. Do you believe that a general requirement that allows flexibility in the sensitivity analysis presented will produce better information regarding the sensitivity of social insurance programs?

Yes.