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Mr. Tom L. Allen
Chairman
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street NW, Suite 6814
Washington, DC 20548

Dear Mr. Allen:

**Ref: Comments on an Exposure Draft— *Reporting Long-Term Fiscal Projections for the U.S. Government***

We welcome the initiative of the Federal Accounting Standards Advisory Board (FASAB) to improve public reporting of information that is helpful in assessing the long-term fiscal sustainability of the U.S. Government. We note that the Exposure Draft (ED) proposes that the government should produce a *basic financial statement* of all projected receipts and payments of the government, relate such amounts to GDP, and show how such projections have changed from the previous year. The ED also proposes that the basic financial statement should be supplemented by narrative that highlights the major factors contributing to any trends, and explains the projections and their inherent uncertainty and also any alternative projections. Finally, the ED proposes that information about the implications of political or legislative inaction be also included.

In principle, it is desirable that governments be encouraged to provide routine public information on long-term fiscal sustainability, as an increasing number of governments around the world are doing. As the ED observes, information on the current financial position can never be adequate for this purpose, as it is necessary to consider the future implications of current expenditure and tax policies. We also agree with the approach proposed by the ED to employ the fiscal gap methodology to analyze fiscal sustainability, and use "current policy without change" as the basis for projecting future receipts and payments. Thus, for economists, the case for the reporting is completely clear, and Appendix B provides important information in a neutral way. Hence, the comments that follow mainly reflect the specific concern of our accountants—to ensure that the proposal is appropriate to an accounting standard.

**The ED could provide clearer explanation of why such forward-looking information should be included in a financial statement or be the subject of accounting standards.** In other words, the leap from having the standard refer to financial position to financial condition could be justified more in Appendix A. From a pure accounting perspective, it could be argued that the unavoidable uncertainty associated with such projections—reflecting the high degree of sensitivity to the assumptions made, and the great difficulty in many cases of avoiding arbitrary assumptions—make such information unsuitable for inclusion in financial statements. The provision of guidance on the assumptions, along the lines provided in the ED, is helpful but does not fully address this issue. It remains unavoidable that, as the Board acknowledges, the "details of the assumptions for projecting current policy without change should be left to the judgment of the preparer, subject to review by the auditor." For many programs, the projections will end up being based on essentially arbitrary assumptions, such as that expenditure grows at the same rate as GDP. The ED explicitly acknowledges this uncertainty, and recommends that it be highlighted in conjunction with the proposed financial statement. The paper also rightly recommends the presentation of alternative scenarios. Notwithstanding these disclosures, it could be argued that the act of designating fiscal gap estimates as a "financial statement" may tend to endow the specific numbers with an authority which they do not deserve.

**The ED therefore could more clearly explain the proposed requirement to report long-term fiscal projections in the context of the underlying conceptual framework of federal financial reporting.** In particular, the ED could expand on the stewardship objective of financial reporting and how the reporting proposed by the ED satisfies this objective. Among other things, the stewardship objective requires that financial reports should provide information to facilitate the assessment of whether future budgetary resources will be sufficient to sustain public services and to meet the obligations as they become due. The reporting proposed by the ED is directly relevant to this objective. While the ED does refer to the stewardship objective, some further explanation of this objective may be necessary to clarify that the financial reporting is not concerned solely with *ex post* information, but also with relevant forward looking information.

**The ED could also explain any limitations of the traditional financial statements that the proposed reporting is designed to overcome.** For example, under existing accounting standards, the government's ability to impose taxes or its commitments for various social insurance payments such as social security and Medicare are not recognized as assets or liabilities on the government's balance sheet. The ED could explain that the proposed reporting of fiscal projections is one way to address the resulting lack of information about the sustainability of government operations required by the *Statement of Federal Financial Accounting Concepts* (SFFAC) 1.

**Finally, the ED could more clearly address the concerns about the reliability of the proposed reports.** For example, the ED could explain that information in the proposed reports on long-term projections would have to satisfy the qualitative characteristic of reliability, as set out in SFFAC 1. The ED could usefully discuss the reliability of projections in the context of the requirements of SFFAC 1 that the information presented should be verifiable, comprehensive, free from bias, and a faithful representation of what it purports to be. It may also be helpful to explain the implications for the long-term reports proposed by the ED of the concept that while reliability does not imply precision or certainty, it is affected by the degree of estimation in the measurement process and by uncertainties inherent in what is being measured.

Our other comments are as follows:

- On Question 5, we support showing both finite and infinite horizon analysis. They reassure different audiences: accountants are probably more comfortable with the first, and economists with the latter.

- On Question 7 on the level of disaggregation, the proposal that all expenditures other than Medicare, Medicaid and Social Security, should be presented as one amount, could be reconsidered. This residual amount, referred to as “the rest”, includes significant items such as education and defense spending that are also sensitive to demographic, productivity, and macroeconomic assumptions and may therefore be a source of "unsustainablilty." A table could be provided showing the composition of this item, e.g., on a classification of functions of government (COFOG) basis, which would enable readers to compare U.S. trends with those in other countries, such as the U.K. and EU members, that produce similar projections. This comparative information is, in many ways, the most useful as it gives a sense of scale to what can look like unfathomably large numbers.

- On Question 9, if the financial statement requirement were introduced, our view is that alternative scenarios should be provided.

- On Question 14, we agree with the majority view that it would be inappropriate to require analysis of policy options for addressing any fiscal gap. The subjectivity of the selection of options would appear to make this an inappropriate subject for mandatory provisions.

Sincerely yours,

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