FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD
Minutes
October 9-10, 2002
Room 7C13
441 G Street NW
Washington, DC 20548

Wednesday, October 9, 2002

Administrative Matters

- **Attendance**

The following members were present: Chairman Mosso, Messrs. Anania, Calder, Farrell, Kull, Patton, Reid, Schumacher, and Ms. Cohen

Agenda Hearing

The objective of the FASAB agenda hearing was to solicit input regarding the board's prioritization of future projects. Notice of the hearing was provided in the Federal Register and *FASAB News.* Staff provided brief project descriptions via the FASAB website and electronic delivery to the CFO Council, the President's Council on Integrity and Efficiency, the FASAB list serve, and to past respondents to exposure drafts.

The Board received input from:

1. Robert Bruce Holstein, Comptroller, Government Printing Office
2. Marilyn A. Kessinger, Director, and Neil J. Ryder, Assistant Director Department of Justice, Office of Inspector General, Financial Statement Audit Office
3. The American Institute of CPAs represented by Pat McNamee, Partner, PriceWaterhouse Coopers and Wendy Frederick, American Institute of CPAs

The meeting was called to order at 9:00 AM. Summaries of each presentation and the related discussion are presented below.

Mr. Robert Bruce Holstein, Comptroller, Government Printing Office on the issue of revolving funds' accounting for Federal Employee's Compensation Act (FECA) liabilities

Mr. Holstein thanked the board for taking time to hear his views. He summarized the views expressed in his September 12th letter to the executive director. He noted that recognition of the long-term liability for FECA has an undesirable impact on the Government Printing Office (GPO) specifically and revolving funds generally.

Each year, the Department of Labor (the entity responsible for making payments to eligible federal employees from all branches of the federal government) determines the actuarial liability attributable to departments and agencies. GPO has recognized this estimate of long-term FECA liability for several years. GPO has taken issue with the estimates provided by Labor and has or will have to expend resources to prepare an estimate specific to GPO.

Mr. Holstein noted that GPO would be hiring its own actuary to estimate a number [the actuarial estimate of the long-term FECA liability] that is creating an almost impossible situation for GPO. GPO must recognize the liability and related expense but cannot collect any revenue related to that long-term liability. He indicated that the statute creating GPO is clear -- GPO is to use accrual accounting and is expected to recover all costs. GPO recovers its costs by billing customers. He also indicated that guidance from Labor and Treasury on rate setting means GPO is not to include the cost accruing from the FECA liability in its rate structure. As he understands it, this guidance is intended to prevent revolving funds from funding this liability in advance. That advance funding would equate to an accumulation of funds at the revolving fund.

Mr. Holstein noted that this treatment is unfair to GPO. GPO rates are set to cover annual costs excluding such actuarial liabilities and the goal over time is to break even. With this liability recognized, GPO would never break even from a financial statement presentation standpoint. In fact, GPO will soon have a negative retained earnings balance as a result of the recognition of this liability. He doesn't know what the consequences of this will be. Attorneys at GPO have indicated that there is no consequence but Mr. Holstein is uncertain about the potential reactions from oversight committees on the Hill.

Mr. Holstein believes GPO is locked into a losing situation. He suggests that some modification of accounting standards could alleviate this. These modifications would take the form of modification of existing standards or creation of new standards for revolving funds. For example, it might be appropriate to accrue actuarial revenue to offset the annual costs. This would achieve revenue recognition at the time the cost is recognized. As an alternative, revolving funds should be able to capitalize the costs – similar to regulated entities to avoid the negative effect of showing these operating losses.

In response to questions from members, Mr. Holstein provided the following clarifying information:

1. GPO follows standards for non-governmental entities (i.e., Financial Accounting Standards Board (FASB) standards). However, GPO would consider switching if the federal standards help with the dilemma of actuarial liabilities. He noted that when the fund started in 1953 there was no federal accrual accounting system and the statute required an accrual system.

2. Other long-term liabilities for employee benefits (e.g., pensions) are recognized by the Office of Personnel Management (OPM) on behalf of all federal entities. GPO funds the annual cash contribution to OPM.

3. A solution under FASB GAAP is not available.

4. There does not seem to be a problem with the concept under which the liability is calculated.

5. While Mr. Holstein can explain the presentation of an ongoing loss but most people don't understand it unless they have an accounting background. GPO's Congressional affairs office spent considerable amount of time explaining it. He prefers an accounting solution that would end the portrayal of GPO as an entity operating at a loss each year.

Mr. Calder asked whether absent a law preventing GPO from including this FECA charge in rates would GPO include this cost in rates? Mr. Holstein indicated that GPO probably would not because he could not see why Congress would want to advance fund the liability. If GPO collected the money 30 years in advance and does not need to make payments on it then GPO would accumulate resources in some manner. Mr. Holstein indicated that GPO doesn't need the funding in advance since the annual cost [on a cash basis] is built into rates.

Mr. Schumacher asked if the change in liability from year to year is typically attributable to changes in the assumptions? Mr. Holstein said most of the dollar changes are due to actuarial assumptions. GPO typically does not have significant year-to-year changes in accidents and has a fairly level amount of payments. The annual cash payments run about $5-6 million per year for medical and injuries. The change in actuarial assumptions is due to the look out into the future with longer time horizon and interests rates.

Mr. Patton noted that the goal seems to be to more or less break-even annually. Is that break-even notion defined anywhere in legislation or operating doctrine in a way that would help GPO include appropriate costs in the rates? Mr. Holstein indicated that the law excludes buildings and land from rates. The law was written long before the accounting mechanism used for long-term personnel benefit liabilities was developed.

Mr. Holstein noted that GPO used to include FECA in the fundamental statements as part of personnel benefits but has pulled it out on a separate line item. This was to clarify for Congress since Congressional staff used to ask why personnel benefits kept going up. GPO has been criticized for having high wages and benefits.

Mr. Reid asked if the law restricting inclusion of land and buildings from the rates is the same law that requires use of accrual accounting. Mr. Holstein responded that it is. Mr. Reid noted that the same law that requires GPO to use accrual accounting prevents GPO from setting rates to recover accrued costs.

Mr. Farrell asked why GPO doesn't accrue pension liabilities but does accrue FECA liabilities? Mr. Holstein indicated that the expense for pensions is what we pay into the fund. He stated that these pension payments are built into rate structure. The FECA issue is a funding issue regarding what you want to put into the rates to break even on an annual basis.

Mr. Kull asked if Labor would pick up all of those costs in the future if GPO were shut down? Mr. Holstein indicated Labor would. Labor creates a total liability number for the legislative branch – not for GPO. GPO's portion is based upon a prorating of the total legislative branch liability. Ultimately, the GPO liability will be eliminated and the Consolidated Financial Report of the US Government would show the total number Labor has on its books.

Mr. Kull asked if GPO went out of business, how would anyone know what the cost to the government was for GPO's FECA liabilities? Mr. Holstein suggested that Labor would have to get an appropriation to fund GPO's portion of the liability recognized on Labor's books.

Mr. Anania asked if GPO has been permitted to explain the loss and the liability in its notes; do you have a robust explanation of this loss and why it exists? Mr. Holstein indicated that GPO did and even called attention to this item with a separate line.

Mr. Kull suggested that this is a scorekeeping issue. This goes back to the point that you are told to use accrual based accounting but then the law limits what you can recover. Maybe instead of changing the accounting we need to change the law. Mr. Holstein indicated he had thought about a legislative fix. GPO has not submitted a proposal to congress because Congress is not likely to allow this type of advanced funding.

Mr. Kull suggested that Congress could just acknowledge that this costs exists, explain why GPO may or may not need to recover it right now, and note that someone will have to pay this someday. If GPO did not have money from the ratepayers in the future – GPO or some other entity would have to appropriate it.

Mr. Anania commented that if you capitalize (one of the accounting standards modifications proposed by Mr. Holstein) the costs and then you go out of business, you have to ask yourself whether anyone would want to buy that asset -- the real test of an asset is what would someone pay for it. He did not think anyone would pay for this. Mr. Patton indicated that from GPO's point of view the asset would represent a future cash flow stream and therefore is an asset.

Mr. Reid noted that from Labor's point of view the FECA liability represents un-recovered costs. It represents GPO's (through Congress' direction) shifting the cost to tomorrow's printing job and if GPO goes out of business we are just shifting the cost to every other federal agency.

Ms. Cohen asked if this was the equivalent of an un-funded pension plan. If you were to recover for the future costs – you would be collecting excess costs in advance for yourself because there is no concept of an invested fund anywhere.

Mr. Kull said that if you were to charge these costs in your rates – you could loan the excess funds to Treasury and the monies would be available to cover the liability if you went out of business. The problem seems to be explaining the loss. The truth is that you are losing money.

Mr. Reid noted that it seems there is a portion of the law that you have to violate no matter what you did. Mr. Calder indicated he doesn't think GPO would have to violate the law. The law says you have to set rates on one basis and report on another basis - a GAAP basis. The effect is that GPO shows a loss. They don't want to show a loss but he does not think GPO violates the law. GPO has an accrual loss – and the problem is the reality of a loss.

Chairman Mosso indicated that the board did not seem inclined to take this up since the accounting seems to be correct. Some members believe the legislative solution presents a chance of solving this. Mr. Holstein asked if the board could notify him of that decision. If he received such a notification, he would be inclined to explore legislative alternatives. Chairman Mosso indicated that we would communicate the board's decision.

Ms. Marilyn A. Kessinger, Director, and Mr. Neil J. Ryder, Assistant Director, Financial Statement Audit Office, Office of the Inspector General, Department of Justice, on the issue of accounting for leases and leasehold improvements

Ms. Kessinger and Mr. Ryder summarized the paper presented to the board in preparation for the hearing. They noted that they had encountered issues with leasehold improvements and believe the board could resolve this by addressing leases in general. The issues relate to:

1. How cancellation clauses affect classification of leases

2. Whether occupancy agreements with the General Services Administration (GSA) constitute leases (GSA explicitly states that these agreements are not leases)

3. Whether funding arrangements should result in differing treatment for leasehold improvements (When an agency leases or enters into an occupancy agreement, the agency may pay for improvements or finance the improvements through increased rent. Improvements where costs are paid up front tend to be capitalized. Improvements where costs are financed thru increased rent tend not to be capitalized. Auditors don't always agree that accounting for the improvement should be the same in either case.)

In preparing for this discussion, Ms. Kessinger and Mr. Ryder reviewed all the guidance including FASB guidance. Under FASB Ms. Kessinger and Mr. Ryder believe improvements should be capitalized regardless of the funding mechanism. However, there is disagreement and Ms. Kessinger and Mr. Ryder are living with a hybrid. Department of Justice capitalizes improvements paid up front but those paid for through increased lease payments are expensed.

Mr. Kull noted that this is prevailing practice throughout government. Most real estate is controlled by GSA. The funding for improvements is governed by appropriations. Many times agencies don't have the funds necessary to fund improvements up front. However, GSA can fund improvements and recover the cost through lease payments over time.

Mr. Ryder noted that there are some costs that agencies are required to pay but most costs are negotiable relative to the timing of payment. Also, tenants can break the lease with four months notice but the tenant must then reimburse GSA for the improvements that went unpaid. He indicated that obviously there is a liability to GSA for these improvements.

Mr. Anania asked for confirmation that the FASB guidance leads to capitalizing the improvement. Mr. Ryder noted that FASB's Technical Bulletin 79-10 discusses the fiscal funding clauses in leases. If there is a fiscal funding clause then management must consider the likelihood of that clause being exercised – if the likelihood is remote then you should consider the lease a non-cancelable lease. That then gets you back to applying the capital lease criteria and guidance. Getting to the guidance on non-cancelable leases is difficult in the federal sector. The differences in terminology tend to permit avoidance of the requirements.

Mr. Kull asked who the leased property belongs to? Mr. Ryder noted that it can be owned by either GSA or private commercial entities. Mr. Kull noted that moveable walls can be an asset because you can take them with you – he asked who owns these types of assets?

Mr. Ryder noted that agencies are prohibited by law from negotiating their own leases – they must go through GSA. Agencies get a tenant allowance to install furniture and fixtures to bring the space to a basic operating level. It is the customization level of improvement that brings up these funding and accounting issues.

Several questions were raised regarding whether GSA or the operating entity capitalizes leasehold improvements. Some factors that might impact this are (1) GSA's capitalization threshold and policies for bulk purchases and (2) the funding mechanism used by the operating entity. It was noted that there are not currently any eliminations associated with leasehold improvements or property. In addition, the President's Management Agenda may include asset management issues in the near future and leases are an issue.

Mr. Ryder noted that he does not believe these lease issues are being resolved consistently throughout government. An additional question is whether the GSA leases should be included in the lease disclosures. CPA firms don't always agree on this issue.

It was suggested that if FASAB codified the private sector (FASB) literature the issues might be resolved.

Chairman Mosso thanked Ms. Kessinger and Mr. Ryder for their time and asked if they were willing to help sort out the problem if FASAB took it on. They responded that they would.

Mr. Pat McNamee, PriceWaterhouseCoopers, and Ms. Wendy Frederick, American Institute of CPAs (AICPA), representing the Federal Liaison Task Force of the AICPA

Mr. McNamee thanked the board for the opportunity to discuss board priorities. He noted that he and Ms. Frederick were representing the AICPA's federal liaison task force which generally provides feedback on FASAB active projects. The task force believes all fourteen of the identified projects are good projects. FASAB – like all organizations - has to allocate scarce resources to receive the optimal benefit for its constituents. The task force – which is comprised of people who audit in the federal environment – has a different perspective than FASAB and its other constituents. Therefore, the task force hopes that FASAB is reaching out to users of FASAB products because these are the real beneficiaries of what FASAB does.

The task force did not come forward with a ranking of the proposed projects. Instead they offer thoughts on what should drive the decisions. Going back to the key federal financial reporting objectives (stewardship, budgetary integrity and operating performance) and the overall federal financial management environment (the key driver in that environment is the President's Management Agenda), a number of the proposed projects (notably improve integration of budget and performance data) may allow FASAB to make an impact on the broader objective of improving performance.

The task force suggests that the board look at projects within a framework of decision criteria. The task force offers four criteria:

1 – Program significance may influence selection. (Social Insurance programs are the largest programs the government has; so clearly social insurance programs would meet the test of program significance since all citizens are impacted by the programs.)

2 – The board also might consider which types of information have the most utility and value for decision making at the policy and operating level. A lot of work at the Financial Accounting Standards Board and the Governmental Accounting Standards Board goes into improving the quality of information for decision-making. Managerial cost accounting standards are important in the federal government because managerial cost accounting strives to get good information to decision-makers. One might consider whether the processes underlying managerial accounting provide information for day-to-day decision-making. Accelerated deadlines and quarterly reporting and other administration initiatives are intended to force the improvement of the quality of information. Auditors must look beyond compliance with generally accepted accounting principles (GAAP) in the federal sector. Since auditors have to report under the Federal Financial Management Improvement Act, auditors have to look at information for management decision-making. So that would be an important consideration – which of these projects can best improve information for management decision-making.

3 – The board might also consider the adverse impacts of diverse accounting in the federal government. For example, the board just heard that there may be diversity of accounting for leases - a number of the other projects have elements of diversity of practices – this should be considered in selecting projects.

4 – The board might also consider the credibility of federal financial reporting. For example, the idea that defense assets weren't really assets was difficult to explain to the general public. The board has been open to revisiting these types of issues based on these types of reactions from the public and may have other areas that warrant revisiting.

The task force has also commented on earlier issues such as deferred maintenance and asset impairment that are important. The notion of stewardship of federal assets means just reporting on the historical cost of the assets may not be sufficient. This area of reporting seems key to achieving stewardship objectives. The task force has also commented on tax revenues and collection efforts. They are also emerging issues.

If observers of the board go back to review the concepts, they will see that FASAB views itself as a thought leader in accounting. FASAB has not necessarily focused on just traditional accounting but what's important in the federal government. Performance reporting might be a way to further that through leadership and to tie into what the government as a whole is working toward. Integration of budget and performance information is one area for future work. The task force view is the more that there is in the general purpose external financial reports that can be of value to budget decision making, the more that will increase the value of the financial reporting and the audits that go behind them.

Finally, there is one project worthy of mention that is not on the staff prepared list. Improper payments are an important element of the President's Management Agenda. In terms of accountability to the public – we think it is important to include information on improper payments in the general purpose external reports and have the information audited. This is a measure of the cost of doing business. It is not practical to get improper payments to zero but having some reliability around what the number for improper payments would be a positive thing for people making policy decisions in the federal government.

Chairman Mosso noted that the criteria would be useful and that we would need to consider criteria we have used in the past and codify a set for the board's purposes.

Mr. Kull requested a recap of the criteria and Mr. McNamee listed them succinctly as (1) program significance, (2) decision utility – policy and operating, (3) adverse impact of diversity in practice, and (4) credibility of the federal financial reporting model.

Mr. Anania asked for clarification of the phrase "improper payments" because that phrase has different meaning to different people. He asked whether that phrase refers simply to bribes or is it broader.

Mr. Kull clarified that there are multiple components of improper payments . We have a responsibility to look at fraud such as that occurring as a result of contractual arrangements and at payments based on eligibility requirements. With eligibility requirements circumstances change rapidly. Recipients may be disabled and then not disabled or unemployed then employed. There may also be a mismatch in terms of what kinds of assistance people should receive versus what they do receive – some is due to simple errors. Some are also underpayments. A lot of agencies don't do a good job mitigating the risk – making sure the right people get the right money. Some agencies are prohibited from using information in certain systems – new hires databases, IRS data, etc. Improper payments are a complex and pervasive problem.

Mr. Anania noted that in the private sector the accounting standard setters do not get into improper payments. The audit addresses these types of payments. The AICPA has a project to strengthen the audit standards that deal with fraud. Through our broader mission – FASAB may have to look at this area.

Chairman Mosso noted that the AICPA's last criterion– credibility of federal financial reporting -- may be relevant here. This is a highly visible financial issue and how it is dealt with reflects on the accounting. FASAB was asked by a Senate oversight committee to look at this but because OMB took it on and acted quickly FASAB decided not to address the issue at that time. Staff was asked to present the history of the Senate request, FASAB's response and OMB guidance for the next board meeting.

Mr. Patton noted that one impediment to clear GAAP standards is an unclear or incomplete conceptual foundation. He believes that solving some of the more pervasive issues here in a way that would survive more than a couple of years would require some agreement to a conceptual foundation. Thus, answering questions such as "what is the reporting model" and "what are the elements" would be important. He asked whether the task force believes the current development of the FASAB model is sufficient to support a stable answer to the questions such as the social insurance liability issue?

Mr. McNamee noted that the task force had not discussed at length the merits of the proposed conceptual framework project. However, the task force has gone back to the concepts to see if see one could discern how consistent the proposals were with the framework. Some members have said the conceptual framework is like the bible – you can read concepts statements and what the statements mean is dependent on what's in your heart. Mr. McNamee expressed his agreement that a framework helps set the boundaries. The role of FASAB under the current conceptual framework is unbounded. For example, improper payment disclosures would address stewardship and ultimately improve systems and controls. So, the conceptual framework now is very broad based. He suggested that a conceptual framework project might focus the work of the board.

Mr. Patton recalled that the board has discussed criteria for ranking projects in April 2002. He asked that staff provide those for review in addition to the AICPA proposed criteria.

The Chairman thanked Mr. McNamee and Ms. Frederick for sharing the views of the AICPA liaison task force.

The board adjourned for a short break.

For the remainder of agenda hearing, the board members offered their thoughts on potential projects. Mr. Calder shared some history of the board's consideration of a liability for Social Insurance. (This history referred to work by FASAB in developing SFFAS Nos. 5 – liabilities - and 8 – stewardship reporting.) The board at that time considered four numbers that might be considered a "liability." (During the discussion it was noted that the term liability was being used in a manner unconstrained by definitions. Thus "liability" appears in quotes throughout to indicate that it does not equate to the FASAB, FASB or GASB liability definitions but to some general idea of liability.)

Mr. Calder described the "**Ives Number**" and noted that it was named for Marty Ives who was a member of the board during these discussions. Mr. Ives had suggested that we should have a "liability" of at least the amount expected to be paid to those in the Social Security program who have attained retirement age or are fully qualified for future benefits. This would be the present value of Social Security obligations to those presently receiving benefits or eligible to receive benefits but not having applied for benefits yet. This is a gross liability since if a person receives benefits but continues to pay in there was no reduction of the future benefits for the additional contributions.

Mr. Calder described the **closed group estimate** as the present value of the excess of future benefit payments over future contributions by or on behalf of covered workers – that is everybody who is a Social Security participant. Social Security includes all persons fifteen years old or older and who eventually will be covered workers. The closed group estimate looks at the entire population over 14 years of age and estimates what we will pay over their lifetime and what they will pay in – we then take the present values of each and the net of these two numbers is the closed group estimate. This would be a "liability" type number. It is the number we have discussed that is most like a pension liability. It covers a different population than the Ives Number. Chairman Mosso noted that this has been considered the generational gap.

Mr. Calder described the **open group estimate** and noted it is not a liability-type number – it is a flow type number because it is the net present value of all flows during a period. (In considering the description of this as a flow number it was noted that this number represented flows during a specified time period rather than flows associated with a defined population. This was viewed as a critical difference because the estimate includes contributions from some in the population while excluding their benefits because they fall beyond the 75th year.) It was suggested that Social Security Administration (SSA) has supported reporting the open group estimate in the past because they manage the program on an open group basis. For example, SSA discusses actuarial balance as when net present value of flows over 75 years approximate zero.

Mr. Anania noted that the element of including new participants makes the open group estimate different than a pension concept. Mr. Farrell noted that at the end of year 75 the calculation does not include what we still owe the then 20-year old participants - it simply cuts off the calculation. Thus it is just cash flows for a defined period and not a defined group.

Mr. Patton pointed out that with any positive discount rate the present value of dollars in the 75th and later years doesn't much matter. Mr. Reid noted that some are beginning to think of "in perpetuity" calculations. In undiscounted dollars there is a fairly significant increase in the liability if you go beyond 75 years.

Mr. Reid noted that the point seems to be that there is no agreement on what population to consider if we wanted to determine a social security "liability."

Mr. Calder then presented the board with pie charts showing the relative size of each potential slice of the open group population (note that the population presented was the open group estimate as constrained by the 75-year time horizon). [The slides used will be appended to the minutes.]

Mr. Calder presented a timeline that showed what the time horizon would be for each "liability" approach. For the Ives Number, the "liability" is the PV of benefit payments made from the valuation date to the date the last person in the population receives benefits. The timeline is equivalent to the longest lifetime of those eligible to receive benefits on the measurement date.

For the closed group estimate, to obtain the present value of benefits less contributions from those people or on their behalf the timeline runs the longest lifetime of anyone in that group and could go more than 75 years.

For the open group estimate, to obtain the net present value of benefit payments and contributions you use a timeline of 75 years. However, members of that population are going to live longer than 75 years. Some won't be entering the population until the 75th year. Thus the population does not fall within the constraint of the 75-year set of flows.

Looking at the Statement of Social Insurance presented in the consolidated financial report (page 58 of the FY2001 CFR), Mr. Calder highlighted the amounts that correspond to the various "liability" numbers considered. The Ives Number was $3,946,000,000,000. The closed group estimate is approximately $10,541,000,000,000. Mr. Reid commented that this represents the unfunded past service cost. Mr. Anania noted that a piece of the Ives Number seemed to be missing – those eligible for Social Security but not yet collecting benefits. Mr. Reid also noted that the figure referenced is net of Social Security taxes the group pays while still working.

Mr. Calder noted that the open group estimate was $4,207,000,000,000.

Mr. Anania noted that the reason the future participants line shows excess contributions over benefits is because we cut the cash flows off before this population gets benefits. Mr. Kull noted that it seems confusing to deduct the future participants' contributions without reducing it for the benefits SSA would owe them. The net present value related to the future participants is not calculated like a liability because we cut off at 75 years and leave off what we would owe them.

Chairman Mosso noted that the discussion was helpful but that we would come back to the issue of project priorities at the next meeting. He asked that members submit input to staff if they believe they need more information or if staff missed any potential projects. Staff will also present criteria and their own assessment of projects against the criteria for the next meeting.

Mr. Reid indicated a desire to give thought to what is currently disclosed in the statements versus what is recorded. He explained that many things represent some sort of commitment by the government. For example, some portions of the national debt that are eliminated in consolidation, but which are full faith and credit obligations of the government, don't appear in the balance sheet. He would like to consider a more holistic view of the commitments of the government. While many commitments that the USA economy will have to bear in the future do not yet rise to a liability, there should be some presentation to assist people in assessing the level of these commitments. Further, it seems when companies get in trouble – the difficulty results from liabilities that did not make the balance sheet. The reaction is that the information was shielded in some way – users did not get the whole picture. We need to ask what represents fair presentation.

Mr. Anania noted he would find a listing of the commitments that raise concern helpful to decideing if this is a specific project or a concept issue. Mr. Reid indicated that Treasury is working on that list.

Mr. Kull noted that there might be merit in reevaluating the conceptual framework.

Agenda Topics

- **Target Audience and Qualitative Characteristics of the CFR**

Lucy Lomax explained to the Board that there were two actions to be taken on the document: 1) complete the vote (2 members had not yet voted) on how to handle paragraph 30 in the draft concepts document, and 2) vote on whether the concepts document should be issued.

Ms. Lomax reiterated the background on paragraph 30. In mid-September the draft concepts document had been forwarded to the Board for a vote. Jim Patton had disagreed with paragraph 30, believing that it provided a conclusion about a Board action that was not addressed in the concepts. Further, he believed that paragraph 30's suggestion that the CFR should specifically direct users to other information sources was outside of the scope of the concepts statement, which addressed intended audience and qualitative characteristics. To address Mr. Patton's concerns, Ms. Lomax had forwarded three proposals for Board consideration:

1) Proposal 1 – Eliminate paragraph 30 since paragraph 29 addresses the reporting limitations issue without being prescriptive for the CFR.

2) Proposal 2 – Retain paragraph 30 and add the suggested CFR action to the concepts by adding to the end of paragraph 6:

   Moreover, since the CFR is a general purpose report that is, by design, an aggregated report summarized from agency reports, the CFR should provide users with information on where they would find information presented in other formats, both aggregated and disaggregated.

3) Proposal 3 – Merge paragraph 30 onto the end of paragraph 29 and modify it, as follows:

> For example, the reader of the general purpose CFR might benefit from having access to a list of information presented in other formats, both aggregated and disaggregated, such as individual agency reports, agency websites, and the President's Budget.

The Board completed the initial vote on the paragraph 30 issue: 5 votes for proposal 1, and 3 votes for proposal 2Joe Anania explained that he voted for retaining the essence of paragraph 30. He believed that the paragraph provided information that would support the Board's goal of making the CFR more understandable to users and thus would be appropriate for the concepts document. Joe Kull agreed and suggested that the guidance could be reworded to be less prescriptive yet still clear . In a real-time mode, using input from Mr. Anania and Mr. Kull, Wendy Comes made changes on the screen version of the document to reword the language of proposal 2. Most of the Board members agreed with the wording changes. However, Mr. Patton reiterated his points that he did not believe prescriptive language was appropriate in the Basis for Conclusions, nor was this particular prescriptive language appropriate for the scope of concepts in this document. However, the Board voted to accept the modified language of proposal 2. It also voted to eliminate paragraph 30 since the essence of the paragraph was captured in the wording to be added to paragraph 6. The following sentence will be added to the end of paragraph 6:

> Moreover, the CFR is a general purpose report that is aggregated from agency reports and tells users where to find information in other formats, both aggregated and disaggregated, such as individual agency reports, agency websites, and the President's Budget.

The Board then unanimously voted to issue the concepts document. Statement of Federal Financial Concepts 4, *Intended Audience for the Consolidated Financial Statement of the United States Government*, will be put in final format for transmittal to the Board's principals within the next two weeks. Mr. Anania also suggested that a future topic for Board consideration should be to discuss the difference between statements of concepts and standards.

- **Natural Resources**

Staff opened the discussion by referring to the staff paper provided to the Board on the natural resources project. Staff indicated that the objectives for today's discussion was to get the Board's approval on the following items:

- project objective
- project scope
- project plan and
- some initial project issues.

During the discussion of the project objective, Mr. Calder noted that he could not conceive what the outcome of the project could be because of the uncertainties intrinsic in the topic. He believes that the most that would come out of the project is a footnote that states that "the Federal government has several types of natural resources somewhere throughout the United States and we cannot value them." Mr. Farrell asked if there was currently a footnote that recognized the fact that the Government does own natural resources and that they cannot currently be valued. Mr. Mosso noted that the Federal government does know where these natural resources are located (i.e., the Outer Continental Shelf), however they may not be measurable. Mr. Anania noted that the key point in the primary objective is "under what conditions will a value be reported". He further noted that if we establish specific conditions in which a value would be reported and some resources do not meet those conditions and then we would find alternative reporting for them, such as quantity reporting in the footnotes.

Mr. Kull noted that the task force recommended that the natural resources information be reported as RSSI, but since the Board is revising the RSSI reporting, the natural resources disclosures could be reported as RSI. Mr. Schumacher noted that as we review "the conditions under which a value should be reported" we should also review how those natural resource values should be measured; Mr. Mosso asked that this measurement of values concept be added to the project objective.

Staff recommended reviewing each of the natural resource categories against the project objectives one at a time and to determine the amount and type of data available to meet those objectives. Staff specifically talked about reviewing the available data at each of the "stages" for each category to determine what is measurable and what is recognizable. Mr. Mosso stated that all of the resources included in the scope of the project are currently resources that are sold and producing revenues.

Staff recommended to the Board that the term "extractable" be removed from the project scope because it would exclude those resources that are taken off the top of the land surface. The Board briefly discussed water rights because it is noted as one of the natural resources that have been excluded from the project because the authority of the rights to water is owned by the states. Staff also recommended that the electromagnetic spectrum be included in the scope of the project. Mr. Patton asked that the difference between natural resources "owned by the Federal government" and those "under the stewardship of the Federal government" be clarified so that the project domain is clearly defined.

Staff discussed the project plan timeline with the Board. The sense of the Board was that the timing of the project would depend on how controversial the issues are and the extent of the Board deliberations. Ms. Comes asked that the Board members comment back to the Staff on the issues listed in the document as well as any comments on those recommendations made by the task force in the June 2000 discussion paper.

Mr. Patton commented that FASAB has only a "working definition" of assets from SFFAS 6 so it may be difficult to answer the question about natural resources being assets. Mr. Mosso noted that staff had a list of asset definitions from FASB, IASC, and other nations' standard setters that may be useful as we deal with the asset issue. The list of asset definitions was then distributed by Staff to the Board members.

- **Department of Defense – Progress Briefing**

Mr. Steve Tabone, Deputy Director for PP&E Policy, OUSD (AT&L), Department of Defense (DoD) and Ms. JoAnn Boutelle, Deputy CFO, OUSD, DoD presented a DoD progress briefing to the Board. Mr. Tabone provided a status on DoD's early implementation of the property, plant, and equipment accounting standard for three "pilot" acquisition programs. Ms. Boutelle provided an update on DoD's financial management enterprise architecture project.

Early Implementation of Accounting Standard

Mr. Tabone commented that Mr. Dov Zakheim, the Under Secretary of Defense (Comptroller)

and Mr. E. C. Aldridge, the Under Secretary of Defense (Acquisition, Technology and Logistics) asked him to express their appreciation to be given the opportunity to give a progress briefing to the Board.

The areas Mr. Tabone addressed during his briefing were:

- **Review Accounting and Reporting Requirements for Military Equipment.** Mr. Tabone explained what the effects the amending standards would have on SFFAS Nos. 6, 8 and 11. He noted that: SFFAS No. 11 would be rescinded, thus eliminating the term national defense property, plant, and equipment (ND PP&E); military equipment would be accounted for and reported on in accordance with the accounting and reporting requirements of general PP&E, which would include the capitalization and depreciation of existing assets and future acquisitions; use of composite and group depreciation is permitted; and, the effective date for the amending standards is effective for fiscal year (FY) 2003.

  He added that the amending standards also provided implementation guidance that: recognizes the imprecision of developing historical costs for existing assets and permits the use of various means to estimate initial capitalization amounts (e.g., budget, appropriation, or engineering documents and other reports reflecting amounts expended); and, the change in accounting for military equipment is to be reported as a "change in accounting principles" in the financial statements.

- **Implementation Plans.** Mr. Tabone described the guiding principles and implementation objectives used by DoD in developing its implementation plans. He stated that the implementation of the accounting and reporting requirements will be led jointly by the Office of the Under Secretary of Defense (Acquisition, Technology & Logistics) and the Office of the Under Secretary of Defense (Comptroller)/CFO; and, that it will involve the appropriate DoD Components (i.e., the acquisition, procurement, logistics and financial communities) to ensure Components take "ownership" of the requirements.

  Mr. Tabone added that standardized and consistent approaches and methodologies will be developed and should support DoD information requirements, as well as meet FASAB accounting and reporting requirements. In addition, he said that strong internal controls must be built into new processes and systems to ensure the reliability of information. Mr. Tabone noted that data calls will not be acceptable in the future when new processes and systems are in place.

- **FY 2002 Pilot Program Approach-Early Implementation.** Mr. Tabone explained that three pilot programs were being used to learn and develop standard approaches for implementing the accounting and reporting requirements for military equipment. He said that one acquisition program was selected from each Military Department (i.e., the Paladin from the Army, the DDG-51 from the Navy, and the F-15 from the Air Force.) Mr. Tabone added that each pilot program will be valued and reported in the FY 2002 financial statements. In addition, composite or group depreciation will be calculated and reported for the pilot programs in the FY 2002 financial statements. Mr. Tabone also noted that, based on work being done with the pilot programs, policy decisions will be developed to address issues such as: capitalization of weapon system programs versus individual items; capitalization of modifications/upgrades; capitalization threshold or thresholds; definition of full cost (e.g., R&D costs, cost of contractor provided and acquired property); useful lives; work in process.

- **Implementation Status**. Mr. Tabone provided a status on implementing the accounting and reporting requirements. He said: a senior-level working group, which meet regularly, has been established; KPMG LLP has been hired to assist in the implementation; work is being done with the Pilot Program program management offices to develop values, with an expected completion date of October 25, 2002; policies critical to Pilot Program values and depreciation are being addressed; the implementation status has been reviewed with the GAO and the DoDIG, who will attend future working group meetings and comment on revisions to policies and business rules; implementation funding requirements have been Identified and communicated to the OUSD(Comptroller); and, a Statement of Work to continue contractor support in FY 2003 is being developed. Mr. Tabone also provided the following estimates, as of 10/04/02, of valuations and quantities for the three pilot programs:

  - Paladin Program: Program cost through FY 2002: $1.6 billion; Quantity acquired: 958

  - DDG-51 Program: Program cost through 12/31/01: $37.1 billion; Total program estimate: $66 billion; Quantity delivered: 36; Total Quantity to be acquired: 64

  - F-15 Program: Program cost through FY 2002: $33.3 billion; Quantity acquired: 1,104; Quantity presently in service: 775

- **Next Steps.** Mr. Tabone explained that work begun in FY 2002 will continue. This includes: refining pilot program values and depreciation amounts and reporting them in the FY 2002 financial statements; preparing FY 2002 financial statement footnote disclosures; and completing development and coordination of new or modified policies. He added that new FY2003 work would include: developing a process or processes for maintaining baseline values and tracking quantities; developing and implementing a new system for maintaining and reporting military equipment information; reporting values and depreciation in quarterly financial statements; develop valuation strategy and planning for all other military equipment programs and items; and, begin valuing other military equipment programs and items. Other tasks include expanding the senior-level working group to include acquisition, procurement and logistics communities to oversee and participate in the financial management enterprise architecture (FMEA) work and ensuring that the "To Be" FMEA adequately addresses new FASAB and DoD information requirements.

Financial Management Enterprise Architecture Project

The areas Ms. Boutelle addressed during her briefing were:

- **Current DoD – Wide Environment – The Problem.** Ms. Boutellle explained that DoD's environment currently consists of stove-piped, non-integrated, non-standardized processes and systems with the consequence of having inaccurate, unreliable, and untimely financial information. She noted that DoD has almost 1,800 financial management feeder systems.

- **DoD's Response – Sustained Top Leadership Direction.** Ms. Boutelle presented the expectation of The Secretary of Defense, Mr. Donald Rumsfeld. She described his expectation as DoD operating in an efficient, business-like manner and utilizing clean audit opinions to verify data. To accomplish this expectation, all finance and financially-related systems and business processes must be standardized. The approach DoD has taken is the creation of a centralized Financial Management Modernization Program, which includes developing a DoD-wide financial management enterprise architecture (FMEA).

  Ms. Boutell stated that the overall management structure for the Financial Management Modernization Program is a Department-wide effort with a top-down structure. She said: an Executive Committee, a Steering Committee, and financial and CIO working groups have been established. She explained that the Executive Committee will resolve critical path issues, while the Steering Committee manages the operations of the program with the financial and CIO working groups performing the daily operations.

- **The Solution – "Road- Map for the Future".** Ms. Boutelle explained that the FMEA will describe the DoD's Future Business Environment with a goal of providing accurate, reliable and timely information by transforming the DoD's business operations. The FMEA is expected to standardize and integrate business processes and systems and create end-to-end solutions using modern technology. Transforming the DoD's business operations would result in: fewer, more-capable and integrated systems; a reduced cost in business operations; better information for decision-making; and, clean audit opinions.

- **Business Transformation – Approach.** Ms. Boutelle described the transformation approach as taking the DoD's "As Is" business processes and developing the DoD's "To Be" architecture using leading business practices. Ms. Boutelle stated that a contract was awarded to Team IBM, which includes various subcontractors, on April 9, 2002 and that the FMEA contractor/government team consists of approximately 250 people. She said a "strawman" of the "To Be" architecture was delivered on schedule on September 27, 2002. The " strawman" was developed with "out-of-the box" thinking and unconstrained by any existing laws, policy, and regulations. The final architecture and transition plan is scheduled to be delivered in April 2003. In summary, Ms. Boutelle stated that the FMEA was not just a financial debits and credits drill. It will require fundamental changes in all the Department's business processes, both financial and non-financial.

- **Budget Formulation and Execution**

The Board held an educational session on budget formulation and execution. Speakers were:

Mr. Phil Dame, Deputy Assistant Director for Budget Analysis and Systems, Office of Management and Budget (OMB)

Mr. Art Stigile, Chief, Budget Concepts Branch, OMB

Mr. Chris Fairhall, Budget Concepts Branch, OMB

Mr. Robert Kilpatrick, Budget Analysis Branch, OMB

The OMB representatives reviewed with the board key budget terminology, the steps in budget formulation and execution, and trends in budgeting.

Adjournment

The meeting adjourned at 4:30 PM.

- **Steering Committee Meeting**

The steering committee received an updated FY2003 budget, Members requested additional detail on the changes from FY2002 and an updated FY2004 estimate. Mr. Kull noted that OMB may have difficulty meeting the FY2003 amount.

The steering committee discussed the upcoming renewal of the FASAB charter (the charted is renewed every two-years in accordance with the Federal Advisory Committee Act). Steering Committee members agreed on behalf of the principals that the charter should be renewed. The agreement was based on recent actions by the sponsoring agencies (the principals) that demonstrated the commitment to continue FASAB activities. These actions included (1) the January 11, 2002 signing of a new Memorandum of Understanding authorizing FASAB activities, (2) the agreement to fund FASAB for FY2003, (3) appointment of new members to five-year terms, and (4) discussions at quarterly principals meetings regarding FASAB issues.

The steering committee met in closed session to consider personnel matters.

Thursday, October 10, 2002

Agenda Topics

- **Dedicated Collections**

Andrea Palmer led the discussion. Ms. Palmer indicated that the intent was to move toward a draft ED by addressing several issues. Initially, Ms. Palmer asked the Board if some kind of a liability disclosure for social security should be part of this project? Ms. Palmer noted that if the liability question were separated out, it might be possible to have a draft ED by December since there appears to be a consensus that the standard should address special accountability and the identified issues address the outer margins of the project.

Ms. Palmer asked if exchange transactions should be considered special accountability items. Also, if funds are partly or totally funded by appropriations, are such funds dedicated collections? Ms. Palmer noted that these issues relate to defining the universe but there are also reporting issues such as whether when other standards (such as the social insurance standard) also cover the same item we want duplicate reporting. In addition she asked the Board's opinion on whether the standard should address materiality, and whether the standard should address the level at which dedicated collections should be reported. Lastly, she said the paper asked whether the Board wanted a standard disclosure describing the nature of intra-governmental investments.

Chairman Mosso indicated that he would like to settle on a universe with a focus on funds since a focus on transactions is difficult. Mr. Mosso opined that the Board got into this project because of (1) confusing terminology and (2) the governmental nature of the investments; thus, the universe should include all funds with investment authority as well as all trust and special funds. Board members discussed the nature of investment authority for these types of funds. The investment authority provided a means to hold funds for future appropriation or automatically for immediate use, however the money was spent elsewhere. Mr. Reid noted that there are about 15 substantial funds and there are 2 schools of thought about the investments: (1) it's funny money (2) the investments are valid and are logical investment vehicles. He noted that if the funds were issued marketable securities in place of the special issue Treasury securities that they now receive, one would rather have the funds invested in the United States Government rather than Enron. Mr. Kull opined that the key is the burden to the taxpayer, if the funds have to be replenished, the government would have to accumulate a trillion dollars, the total they now represent. Ms. Cohen asked if the law required the invested funds to be spent for a specified purpose, because if so, even though the money was being spent for other purposes, a liability or obligation (in a general sense) was associated with the investment. She noted that people are taxed for what they assume is a specific purpose that the tax will support, and the tax rate would be lower if not for the purpose of funding future requirements.

Mr. Anania indicated that the scope of the project was a matter of concern and suggested that there was a need for a definition of dedicated collections that will help us. He wondered what specific kinds of funds were being discussed; whether the Board had to concern itself with every kind of fund that someone has to pay, especially if the funds are commingled. He suggested that the Board might want to address only those with a special aspect or responsibility tied to it. Ms. Palmer noted that each one of the earmarked funds is enacted in law. Congress establishes a fund and a collection at the same time. Mr. Anania responded that the private sector has contributions for pensions, withheld taxes, etc., all of which are covered by law, and that if there's a liability it gets recorded. He stated that he did not see how a liability could be recorded if it is not a liability. Mr. Kull responded that whether we have a true liability is the question. Mr. Anania asked whether any of the dedicated collections are recorded as liabilities. Mr. Farrell noted that some pensions are recorded as liabilities. He added that on other funds Congress acts as though it has an implied promise, that is has a liability, but then backs up and says we (Congress) can change it whenever we want to so it is not a liability. He expressed the opinion that if Congress changes the law then it is another event, at which point the liability might go away, but until the change is made the promise exists.

Mr. Mosso observed that liabilities occur for different reasons, people working for example. So the collection is different from the liability. Mr. Calder responded that the government does have to record a liability when cash is received. Ms. Cohen asked what the credit is when cash is collected. Ms. Comes stated that in the private sector if services were not provided when money was received the credit would be to "unearned revenue" but with taxes we credit revenue immediately. Several Board members discussed whether an obligation creates a liability. Mr. Kull and Mr. Calder stated that that was the heart of the matter. When Congress passes a law to take money for something is there a direct liability to eventually satisfy the promise made with that collection? Mr. Kull asked if when you have a gas tax that takes a nickel to improve highways, is there a responsibility that should be recorded that says there is a nickel available to improve roads and that's what Congress is going to spend it on? Mr. Anania said it sounded like a liability if you collect money under law. Mr. Farrell agreed that it did, unless historically that money has never been used to repair a pothole and everyone knows it.

Mr. Reid suggested the possibility of recording something on the balance sheet (right side) that is labeled with words that are more precise than "liability". Mr. Calder responded that it still would be a liability. Mr. Anania suggested going back to the definition of liability. Mr. Mosso indicated that for something to be a liability, there has to be an identifiable claim. Mr. Reid opined that what is needed is a definition of a liability that applies in this context; a new category on the balance sheet without using either asset or liability.

Mr. Calder opined that if the Board required it on the balance sheet it would be, in essence, a liability. Now, however, it goes on the statement of financing as a revenue. He stated that the issue is where it goes. He has always felt on Social Security, because it's more egregious or clear-cut, that it represents a liability because of statements made by elected officials over the years that seems to make it a liability. Mr. Jacobson (legal counsel) noted that in a program established by statute, Congress always reserves to itself the right to change the underlying law or affect payments by what it appropriates. . Also the description of beneficiaries is very amorphous. For example, the Highway fund does not identify the amount to go to a state or a locale. Ms. Cohen stated that she thought everything had to be appropriated, including a permanent indefinite appropriation. Mr. Jacobson described what a permanent indefinite appropriation is and that a fund with a permanent indefinite appropriation could receive financing from various types of collections. Mr. Kull said that even if Congress does reserve the power to itself the right to appropriate on an annual basis, what is the public's perception of the obligation. Mr. Jacobson said there might be an implied promise (he hesitated to use the term obligation because it has a very precise use in federal financing) but it is not enforceable. Ms. Cohen wanted to know if the obligation was more likely than not. Mr. Jacobson felt it was more likely than not that Congress would spend <u>most</u> of the money (in the Highway trust fund) for highway improvement but not more likely than not that they would spend <u>all</u> the money for highway improvement. The Board members discussed FASAB's definition of a liability. Mr. Mosso stated that a liability still came down to needing to identify a claimant. In environmental clean-up they had an exception in the requirement of the statute.

Mr. Anania wondered what the Board planned to do, look at each fund and try to apply a liability test to each fund or different groups? He thought it was hard to proceed without a definition. Mr. Patton agreed that the Board needed a definition of a liability that applies to this area. Are collections going into a holding area before they're classified as revenue and what is the appropriate presentation and title for these holdings?. If we have a highway tax should we have something in the statements that represents that undisbursed portion of those taxes? Mr. Kull asked if they were interested in the undisbursed portion or the undisbursed "commitment" for the level of service, because clearly the money is not there from the consumers' point of view. Ms. Cohen opined that she did not think it was the service that mattered but the levying of the tax. If someone gives taxes for X, is there an obligation to spend it for X, but if instead it can be spent whenever, eventually, then it's not a dedicated collection. Mr. Farrell said that in that case, he would say that there is not really a Highway fund and we need to reflect that in the financial statements. If what Congress is saying is "We're calling them special taxes, but they're really not special, they're general," we need to make that transparent to the American citizens. Congress can't have the tax and say we promise to do this for you and not have any accounting. There's either money set aside or there's not.

Mr. Patton wanted to know if the entitlements and non-discretionary payments in the budget had anything to do with this. Mr. Kull replied that programs can be non-discretionary without a dedicated collection.

Mr. Mosso stated that he thought the Board needed to get away from the term dedicated collections and focus on funds since they were not making progress with dedicated collections. Mr. Patton asked wasn't it true that a collection becomes dedicated when it gets into a specific fund. Several Board members discussed the payments from the general fund to the Medicare trust fund and whether they would be considered dedicated collections. Mr. Calder asked for a definition of a fund and Mr. Mosso responded that a fund is an entity account.

Mr. Kull observed that there are a finite number of funds and laws discuss the attributes and that staff could review all the funds and decide on attributes. Then we could develop something that makes sense. Ms. Palmer responded that the staff had accumulated much of that information over the life of the project. Ms. Comes noted that doing additional work in that area would only make sense if the Board first identified the attributes that were of interest, such as ones that make the fund a liability or meriting special accountability.

Mr. Patton noted that normally a definition/concept precedes a profile. Mr. Kull asked how one would know if a definition would be sufficiently robust without knowing what type of funds are out there and the exceptions. Mr. Patton replied that Congress could invent something new six months from now so what the Board needs to define are the political and economic characteristics that create a liability. Mr. Mosso noted that every fund has a liability just before payment. Mr. Reid again suggested the need for a special classification such as trust fund balance, something akin to unearned revenue. Mr. Patton noted that such an approach goes to the need for conceptual development of the fundamental purpose and definition of the model. Mr. Reid responded that the model is preventing us from showing what's appropriate. He noted that in state and local government financial statements you see the separate funds all together in one place. FASAB has a consolidated model, and although he might not agree with setting up basic statements and not consolidating them, he does think it is possible to show the net of the investments, where there is a disclosure with an array but the net is rolled up into the balance sheet. Not quite a liability yet going beyond a rigid definition of a liability.

Ms. Comes noted that staff had looked at the notion of restricted equity. Mr. Anania agreed that it would be equity for which there is an obligation. Mr. Patton objected because when he heard the term equity he thinks of private enterprise, and did they mean net position. Mr. Mosso stated that he thinks of it as "taxpayer equity". Mr. Anania questioned how the Board could put something that was not a liability on the financial statements. Mr. Kull responded that they should not try too hard to fit the private model; the federal government is unique.

Mr. Anania mentioned GASB's dual model and suggested that there may be value in what GASB concluded. Ms. Palmer reminded the Board that fund accounting had been suggested as an option in earlier issue papers and the Board had not been receptive.

Mr. Mosso noted that every agency balance sheet has a liability section and an equity section and all of the funds that the Board is interested in are going into the equity section – maybe a separate section of equity is needed. He noted that although some Board members wanted to call the investments (i.e., trust fund balances) a liability, he thought they would find debits and credits tripping all over themselves. Mr. Reid noted that the CFR now has robust disclosures (footnotes 10 and 19). Are these enough? Are we telling the correct story with the statements? Mr. Patton indicated that footnote 19 is too obscure and that something is needed on the face of the financial statements; the Board needed to be creative. Mr. Anania suggested a split in net position to show the restriction. Mr. Mosso agreed that this was a possibility and is consistent with the present model but it still leaves the question about which balances you go with – special and trust funds perhaps. Mr. Reid observed that if the objective is to show investments then the Board would need to address intra-governmental eliminations. That when debt is subtracted from the fund balance it almost all goes away, so the Board would need to consider a gross-up. Mr. Mosso observed that we're kicking around a segregated equity section. If we tentatively adopted that approach we could move on to what we want to segregate. Mr. Reid favored this approach but this approach would need to make the debt obvious – all nonmarketable debt (about $2T) would need to be shown. Mr. Reid asked how many special and trust funds would be in play? Ms. Palmer indicated about 200. Mr. Reid suggested setting a dollar threshold >$1B. Ms. Palmer indicated that such a threshold would bring 30-40 funds into play. Mr. Anania indicated that doing this for purposes of reporting is not permissible – it could be done for disclosure purposes.

Mr. Mosso indicated that the Board should go forward and some members may believe that some funds are liabilities but those members will see the debit/credit problems of classifying dedicated funds as liabilities. Mr. Calder asked if Mr. Mosso could accept the labels given to trust and special funds? Mr. Mosso answered that we should start with the funds with the labels and refine to an underlying concept. Mr. Calder agreed to the proposal with that caveat. Mr. Mosso noted that the Board could address liability issues in other projects. Responding to Mr. Anania's earlier question about why the decision to only include trust funds and special funds, Mr. Mosso indicated there was a need to determine generally what would be included and what would be excluded – tinkering would come later. Mr. Farrell asked if social insurance issues had been set aside? Mr. Mosso answered affirmatively except for segregating the equity section. Mr. Reid added that this approach will not solve the unrecorded liability problem - the segregation only addresses what has been collected.

Mr. Mosso indicated that another issue that needs to be addressed is what are the appropriate disclosures, suggesting that the funds need to be looked at individually to see what should be disclosed. Mr. Patton asked whether the receipts would go straight to equity and not be reported as revenue? Mr. Mosso asked Ms. Palmer to illustrate the entries. Mr. Reid noted that he had no serious problems with the currently required disclosures but that the current presentation concerned him. Mr. Mosso asked if the Board needs to come up with some boiler-plate language to describe the effect of intra-governmental investments?

Issues to be considered at the next meeting were identified: (1) the name of the category that will be segregated; (2) the intra-governmental investments issue; (3) the items that will be included/excluded from the special category: and; (4) an illustration of the flows. Mr. Reid noted that at the CFR level there is an elimination issue that needs to be addressed separately. Ms. Palmer noted that there would not be a draft ED for the next meeting.

- **Intra-departmental Cost Interpretation**

Staff explained that the Intra-departmental Cost Project Draft Interpretation had been revised to clarify and expand discussion on areas identified by the Board at the August meeting. Specifically the Draft Interpretation was revised to:

1.) Clarify the interpretation is specific to imputed costs.

2.) Use of simpler terminology--no longer include 'inter-entity' after the terms inter-departmental and intra-departmental

3.) Define imputed intra-departmental costs and inter-departmental costs, including an example

4.) Add additional language regarding recognition criteria

5.) Add language referencing the survey that was conducted

6.) Add language regarding existing cost accounting guidance that is available

7.) Clarify reporting disclosures

8.) Use of a chart as an illustration to convey the inter/intra departmental relationships

9.) Add language regarding OMB guidance on specific inter-departmental costs that are imputed

Staff also explained that the revised interpretation was forwarded to Board members for comments prior to the October meeting. Comments were received from four Board Members and their comments were considered in preparing the pre-ballot exposure draft, which was included in the October Board materials. The most significant change was the combining of the short illustration that was previously in the text of the interpretation with the illustration in Appendix B. Other changes included the addition of subheadings within the Basis for Conclusion and incorporating one of the footnotes into the text.

Staff explained that the goal of the meeting was to obtain the Board's input and comments on the pre-ballot Exposure Draft. The Board provided the following comments:

- Mr. Calder suggested that the definition of Department, within the Summary of the Issue section, implies that it is contingent upon OMB action. It was agreed that the sentence would be clarified so that it includes all reporting entities, or entities preparing financial statements, regardless of OMB designation.

- Mr. Calder expressed that paragraph 110 of SFFAS No. 4 alone does not specifically prohibit recognition of imputed costs. However, paragraph 110 does hinge upon OMB guidance on identifying the specific inter-entity cost for recognition. Paragraph 110 in conjunction with OMB Bulletin 01-09, *Form and Content of Agency Financial Statements*, Section 4.3 second paragraph which states "Reporting entities are required to recognize the following costs…To ensure consistency, agencies should not recognize costs other than those listed until OMB provides further guidance." does limit the recognition of certain costs. It was agreed that the interpretation would be clarified to state that paragraph 110, in conjunction with the OMB Bulletin that has led to the question as to whether the recognition of the imputed intra-departmental costs is allowed.

- Messrs. Calder and Anania suggested that the wording within the exposure draft interpretation be revised to remove language that references paragraph 110 as 'prohibiting or precluding.' Additionally, the interpretation should focus on that there is no limitation on the recognition of imputed intra-departmental costs. It was agreed by the Board that the language in the interpretation would be changed throughout to soften the emphasis of the standard actually prohibiting or precluding recognition.

- Mr. Farrell posed to the Board that in essence, the Board will be requiring the same type of transaction to be treated differently depending on the customer. Staff clarified that the difference only occurs when there is reimbursement less than full costs. Normal exchange transactions for intra-departmental and inter-departmental costs are handled the same. The interpretation clarifies that imputed costs between entities within the same larger reporting entity (which are eventually eliminated at the consolidated level) should be recognized and included in component level financial statements. Staff further explained that the AAPC Inter-entity Task Force is currently working on other imputed inter-departmental costs to be recognized.

- Mr. Calder suggested that the definition of imputed inter-departmental costs was counter-intuitive, as it did not clearly acknowledge the limitation on recognition. It was agreed that the definition would be clarified.

- Mr. Patton suggested that the title of the Interpretation be changed from "A*ccounting for Imputed Intra-departmental Costs: An Interpretation of SFFAS No. 4"* to "Accounting for Inter-entity Costs" as the interpretation does speak to specifics of both intra-departmental costs and inter-departmental costs. The Chairman noted that the interpretation does not make any new requirements for inter-departmental costs. Staff further explained that inter-departmental is explained to the extent of presenting the differentiation with intra-departmental, as both are new terms. Staff also explained that there is some resistance to change the title to "Accounting for Inter-entity Costs" as there is currently an AAPC Task Force currently working on the inter-departmental costs for recognition. The Chairman suggested that the focus of the interpretation will be streamlined somewhat based on the other agreed upon revisions, which will most likely address this concern.

- Mr. Calder stated that he did agree with the use of the term reporting entity as used in the interpretation, but requested that it either be defined or referenced to where it is defined.

- Mr. Calder suggested that we use the term Consolidated Financial Report (CFR) instead of Financial Report of the United Stated Government (FRUSG) in the interpretation. Staff noted that FRUSG was used because it was the title of the last issuance. Staff agreed to confer with Treasury on the preferred title and what the trend for the title will be in the future.

- Several Board Members provided other minor wording changes that staff agreed to incorporate.

In concluding the agenda item, it was agreed that staff would incorporate the above changes and forward the revised pre-ballot Exposure Draft for final comments within two-weeks. The Board members will then have four days to comment on the revisions. After this, staff will forward the final Exposure Draft with ballot to the Board for vote.

- **Fiduciary Activity**

The staff presented a draft exposure draft (ED) based on the staff's interpretation of the members' direction at the August Board meeting. The staff explained that although the accounting standards section of the ED was fully developed, some sections of the ED were in outline form for discussion.

The Board provided comments on the ED paragraph-by-paragraph, through paragraph 16. The members approved the title "fiduciary activity" and directed the following changes:

- Use of the term "evidence of" in place of "intent" or "manifest intent" because determining intent can be problematic.
- Eliminate the explicit reference to Federal entities receiving assets from other Federal entities because it might be confusing. The examples of such activity could be retained.
- Retain and expand the concept in paragraph 13 whereby the terms "fiduciary" and "trust" would be limited to the fiduciary activity addressed in the standard.
- Remove the "secondary characteristics" presented in paragraph 15. Thus, the standard would have only primary characteristics. The substance of the "second characteristics" could be used as examples for the basis for conclusions.
- And make other editorial changes specifically identified by the members.

Mr. Patton said that the standard would be easier to understand if the entity and CFR accounting provisions were presented separately. Mr. Anania suggested that all standards should be so constructed. Mr. Reid preferred a case-by-case approach.

The Board discussed the three methods for holding fiduciary assets presented by the staff: (1) commingled with the entity's cash, (2) not commingled, and (3) separate and apart from the entity. The Board preferred to define "commingled" to mean either entity or Treasury cash, which would cover most cases since relatively little cash is held outside the Treasury.

The allotted time expired before the detailed discussion of the proposed accounting for each method could be concluded. Mr. Mosso directed the staff to make the changes as indicated by the members and provide pro forma illustrations for each of the three methods. Mr. Mosso indicated that the changes and illustrations should be sent to the members for review and comment as soon as possible and rather than waiting for the next meeting in December.

- **Reclassification of Stewardship Responsibilities and Eliminating Current Service Assessments**

Social Insurance

The Chairman introduced AICPA representatives who would participate in the discussion:

Chuck Landes, AICPA's Director of Auditing Standards (by speakerphone from New York)

Pat McNamee, Chairman of AICPA's FASAB liaison taskforce and social Insurance (SI) taskforce, and Wendy Frederick, AICPA Technical Manager, Washington DC.

Mr. McNamee thanked the Board for the opportunity to discuss these issues. He noted that it has been and remains the position of the AICPA that some items of SI information meet the criteria for liability recognition. With regard to other items of SI information that are classified as Required Supplementary Stewardship Information (RSSI), AICPA believes that suitable measurement and presentation criteria that can be consistently applied are needed for audit purposes for auditors to provide assurance, whether via audit or by means of an attestation engagement.

Also, AICPA had suggested that it might not be cost beneficial if all required SI information became an integral part of the basic financial statements, as was proposed in FASAB's exposure draft. In response to a request from FASAB, AICPA established a new taskforce to consider what kind of audit guidance might be needed or appropriate, if the Statement of Social Insurance were deemed a basic financial statement. That group has meet once. Key considerations were suitability of criteria and ability to audit and report in the context of a general purpose report.

Mr. McNamee provided a handout that identified different areas of the Statement of Social Insurance (SOSI). Page 58 of the Financial Report of the U.S. Government, as marked and discussed during the Board meeting, is attached to these minutes as a separate file.] The taskforce believes there could be different audit implications associated with different components or elements of the SOSI.

Mr. McNamee started by discussing area B1 [the actuarial present value (APV) of expected future benefits to those currently receiving benefits]. The taskforce concluded this item is the most comparable to liabilities for pensions and postretirement healthcare, for which there is established accounting and auditing literature. The taskforce believes it would be straightforward to develop guidance for how to audit what is in area B1.

[1] SFFAS 17 defines these programs as SI: Social Security (OASDI), Medicare (HI and SMI), Railroad Retirement benefits, Black Lung benefits, and Unemployment Insurance (UI). UI is not reported in the SOSI.

As one moves down, uncertainty increases. Area B2 [the APV of expected future benefits to current participants who are not yet receiving benefits] is more uncertain. It is for a closed group, but it includes participants as young as 15 years old, and involves projections for up to 75 years. Area B3 has to do with future participants: those under age 15 and people not yet born or in this country, so area B3 is even more uncertain than area B2.

Similarly, area A (parts 1, 2, and 3) involves projections of future revenues for periods of up to 75 years. Mr. McNamee noted that the audit guide on forecasts suggests that one begins to lose reliability when the forecast period exceeds 3 to 5 years. The attestation standard and the audit guide distinguish between a forecast and a projection. A forecast is intended to reflect management's judgment about what is most likely to happen, and is therefore regarded as suitable for general use.

A projection, on the other hand, may be based on hypothetical assumptions, not necessarily what is considered most likely to happen. The examples in existing audit literature deal with a limited number of assumptions. Such projections are generally done for a limited audience. Existing audit literature restricts the auditor from providing assurance regarding projections in a report intended for general distribution. SI disclosures in areas A and B (1, 2, and 3) go so far into the future and contain so many hypothetical assumptions that it is hard to fit them into the existing audit framework of general distribution assurance.

Mr. Calder noted that the Trustee's report asserts that the middle projection is the most likely. The auditor, he suggested, merely reports on the reasonableness of the assumptions and computations, not the achievability of the results.

Chuck Landes said that that auditors look for a reasonably objective basis to opine on prospective information. When the auditor opines on a forecast, the auditor warrants that there is a reasonable basis for the assumptions. The further into the future one goes, the less evidence there could be that there is credible, reasonably objective evidence. At some point—no one knows for certain where that is—one crosses over to hypothetical assumptions about which it is difficult to give much assurance to the user. Similar issues arise in "fair value" accounting for items where there is no readily determinable market value.

Mr. Reid noted that for this particular schedule, the assumptions are well documented, with over 50 years of data and experience in some cases. Controls over the process are tight and well documented, with provision for periodic review by independent experts.

Mr. Anania noted that accounting standards call for recognition of liabilities that stretch out more than 3 to 5 years. Besides pensions and retiree healthcare obligations, there are things like environmental clean up liabilities, some insurance liabilities, etc. He could understand excluding future participants, but would like a fuller discussion of the distinction AICPA sees regarding the amounts reported for current participants.

Mr. McNamee agreed that part of area B2 could be analogous to pension accounting, depending on how one defined the cohort (which currently includes 15 year olds). However, there are many dynamic factors involved, which interact, and which go far out to the future. Mr. Anania asked whether the group had considered a shorter cutoff of 5 or 10 years. Mr. McNamee said the group had not addressed that, and that they realized the long term perspective is important for the Board's purposes. Taking that as a given, the taskforce had focused on the challenge of fitting the SOSI presentation into the existing model. In AICPA's standards, the sample auditor's report on projections makes reference to the assumptions and reports in the context of those assumptions. Conceivably something like that could be done with respect to the SOSI, but currently the auditing standards don't provide for doing this in the context of a general purpose report. At the same time, the taskforce recognizes that the SOSI is not being used to sell stock in an investment; it is something different from financial projections as we know them in the private sector.

Mr. Reid asked how this position could be reconciled with AICPA's earlier recommendation that a liability should be recognized for SI. Mr. McNamee replied that "B1" and part of "B2" might constitute a liability (for example, one might accrete a liability as people worked the 40 quarters necessary to become entitled to some benefit), but not unearned revenues in "A (1,2 and 3)," nor amounts relating to future participants in "B3." The SOSI mixes past events and future events. Ms. Frederick noted that projected future obligations are disclosed in pension and retiree healthcare accounting, but are not recognized as a liability [only that portion of the projected obligation that has been attributed to the employee's service to date is recognized].

Mr. Mosso noted that Board's leaning is to make the SOSI a basic statement comparable to the Statement of Net Cost and Balance Sheet, at least for an interim period (with the question of liability recognition being beyond the scope of the current project). He asked what type of opinion that would lead to on the SOSI, and how much time would be needed to implement that?

Mr. McNamee indicated that the task force would investigate adapting the existing audit literature to craft a procedure for a general distribution report on the SOSI as a projection. Mr. Mosso asked whether the auditor might be able to provide such a "projection opinion" with reference to hypothetical assumptions on A (1, 2, and 3) and B3, with a standard opinion on B1 and B2 in the same report?

Mr. Landes (noting that he had not seen the handout being discussed) said his initial reaction was that it sounded rather like piecemeal opinion, which are not permitted; he would like to investigate this to see how to accommodate the Board's need. Depending on how the information were labeled, perhaps it would be possible to have an opinion regarding some information that would run to conformance with GAAP, while identifying the other information as something different. The Chairman said it was not fair to ask Mr. Landes to discuss it further at that time, since he had not seen the handout.

Mr. McNamee noted that the taskforce's purpose was not to disrupt the Board's plans. Rather, its objective was to share its concerns—based on its initial meeting—that the proposal to make the SOSI an audited statement involves some new challenges: it is not a straightforward audit or attestation engagement pursuant to current guidelines. The Board had provided helpful feedback to the taskforce and the Auditing Standards Division; they will drill further into the numbers.

In response to a question about timing, he indicated that the taskforce's work could not be completed until sometime in 2003. Discussions with preparers indicate that implementation would take time, and the relevant guidance ideally should be available before the beginning of the fiscal year in which the new accounting standard would be effective. Accordingly, from a practical standpoint, the sense of the taskforce was that FY 2005 would be the earliest desirable effective date.

Mr. Calder said that area A in the SOSI should be divided so it corresponds to areas B1, B2, and B3. He would make the standard effective immediately; it would be up to the auditor to determine whether it could be audited. Mr. Kull observed that AICPA had recommended that, if the RSSI category were eliminated, SI information should be classified as RSI, pending liability recognition.

Mr. Farrell observed that SFFAS 17 calls for a lot of other information on SI, which may be useful, but in his opinion is not essential to accompany the SOSI. He asked whether there is a cost differential based on whether information actually must be presented as audited information. For example, in doing a routine audit, the auditor would examine how bad debts are calculated. But if a detailed schedule of bad debts was presented in the notes, the auditor would probably do more work on it. Mr. McNamee agreed, saying that was the part of what AICPA meant to convey in its comments on the exposure draft. Audit level assurance on all the detailed required information would change materiality and increase cost.

The Chairman and Board members thanked Messrs. Landes and McNamee and Ms. Frederick.

Later the Chairman asked members to review their thoughts on how the SOSI should be classified, in light of the discussion with AICPA.

Mr. Reid said that if the Board were going to reconsider liability recognition, he would table this issue for now. Mr. Kull alluded to discussions with the JFMIP principals, at which the Secretary of the Treasury expressed interest in a broader review of liability recognition first. Also, he said, the audit community is not ready to deal with the SOSI as a basic statement. Mr. Mosso suggested that we could make the SOSI basic and see what the auditors do. He is not sure when, or whether, we will see a SI liability recognized.

Mr. Reid said that if AICPA said that they could not audit it, he would come back to GAO and ask if it could craft a standard for government auditors to follow to get this done. Mr. Calder said GAO was looking at this. He noted that the Board agrees this is vital information for citizens. The Board may later decide a liability should be recognized, but in the meantime the SOSI should be up front in the report, and we should get whatever audit assurance we can on the information. Mr. Kull noted that GAO has authority to audit this information now.

Mr. Anania said he thought AICPA had not fully answered his question about why these numbers were different from some other long-term liabilities. He also has a concern that getting an opinion will be problematic. His current thinking would not be to move the SOSI into basic status now, but to work on getting more information about B and C so we can deal with the liability question.

Mr. Patton, recalling earlier comments from AICPA, suggested that we should make at least the SOSI basic. We have a list of criteria (in the exposure draft) that distinguish basic information from other information. These factors include whether the information is essential to fair presentation, whether it is of interest to a wide audience, etc.; from his perspective the SOSI meets the criteria for basic information.

Mr. Schumacher said he had been leaning toward making the SOSI basic, but he now has concerns if doing so would lead to a disclaimer on it. On the other hand, if FASAB does nothing, we may never get to where we want to go. Mr. Kull noted that we needn't rely on AICPA: GAO can do this as well.

Mr. Farrell noted that the Government does not have a clean opinion now, so making the SOSI basic would not jeopardize a clean opinion. (Mr. Kull interjected that all the civilian agencies are close, and the Social Security Administration has one now.) Therefore, Mr. Farrell is in favor of pushing AICPA to get something done. However, he does not agree with presentation of the "B3" section of the SOSI. He would eliminate that.

Mr. Anania said that if we change the statement by eliminating B3, he would like to examine B2 as well.

Mr. Farrell noted that the SOSI precedes the notes in the current government wide report prepared by Treasury. It is not even labeled unaudited: one has to look two pages earlier to see that the section is unaudited. Only accountants would notice the difference. Mr. Mosso agreed, but said the auditor's review is important to enhance credibility. He would hate to see the statement labeled "unaudited" given its importance.

Current Services Assessment (CSA)

Mr. Robert Kilpatrick, of OMB, joined Mr. Bramlett as staff for this part of the discussion. Mr. Bramlett noted that Mr. Kilpatrick had written two memos, previously provided to the Board, which discussed several issues that would need to be worked through if the Board decided to mandate use of OMB's Midsession Review current services estimates in lieu of the current services estimates published in the President's Budget. Mr. Kull had suggested this option at the last Board meeting. Mr. Bramlett observed that the threshold question was whether the Board wanted to eliminate the CSA. If so, there would be no need to address the issues discussed in Mr. Kilpatrick's memos.

Mr. Anania said the question is how effective is the CSA requirement? Mr. Patton said the information is taken directly from another source, so the value added may be small. Mr. Calder suggested that one of the reasons for the original CSA requirement was that there is no audit of the budget; as a result the "actual" numbers, which are the first column of the CSA, are not audited. However, there was some thought that reconciliation of the "actual" numbers in the CSA to the financials would offer peripheral assurance about the budget numbers. Mr. Kull said there was probably a sense that it would add to the integrity of the budget numbers. Mr. Calder agreed, and said that we would break the nexus there by reporting the Midsession Review numbers, i.e., that objective would be gone. Mr. Kilpatrick said he did not think the nexus was ever established in practice; he does not think the CSA contributes to budgetary integrity (unlike the Statement of Budgetary Resources). The question, to his mind, is whether the CSA contributes to the financial report.

The Board agreed to eliminate the CSA requirement.

Risk Assumed

The Board agreed that “risk assumed” would become required supplementary information (RSI).

Adjournment

The meeting adjourned at 4:00 PM.

Attachment 1 – FY2001 CFR Page 58

United States Government
Statement of Social Insurance

Present Value of Long-Range Actuarial Projections 1	Contributions and Earmarked Taxes 2		Benefit Payments 3		Benefit Payments in Excess of Contributions and Earmarked Taxes	
(In billions of dollars)	2001	2000	2001	2000	2001	2000
Participants Who Are Currently Receiving Benefits:	**A1**		**B1**			
Federal Old-Age,Survivors and Disability Insurance (Social Security)	309	266	4,255	4,020	3,946	3,754
Federal Hospital Insurance (Medicare Part A)	113	97	1693	1681	1580	1584
Federal Supplementary Medical Insurance (Medicare Part B)	258	234	1159	1051	901	817
Railroad Retirement	56	2	81	27	25	25
Black Lung (Part C)4	8	8	4	4	-4	-4
Participants Who Are Not Currently Receiving Benefits:						
Federal Old-Age,Survivors and Disability Insurance (Social Security)	**A2** 12349	11335	**B2** 18944	17217	6595	5882
Federal Hospital Insurance (Medicare Part A)	4136	3757	8568	6702	4432	2945
Federal Supplementary Medical Insurance (Medicare Part B)	1845	1527	7415	6094	5570	4567
Railroad Retirement	57	26	67	39	10	13

Future Participants:5

	A3		B3			
Federal Old-Age,Survivors and Disability Insurance (Social Security)	11035	10088	4700	4297	-6335	-5791
Federal Hospital Insurance (Medicare Part A)	3507	3179	2225	1349	-1282	-1830
Federal Supplementary Medical Insurance (Medicare Part B)	593	404	2206	1514	1613	1110
Railroad Retirement	29	40	13	10	-16	-30

	Valuation Period	Valuation Date	Net Present Value of Negative Cashflow 6
Federal Old-Age,Survivors and Disability Insurance (Social Security) 2000	1/1/2000 – 12/31/2074	1/1/2000	3,845
Federal Old-Age,Survivors and Disability Insurance (Social Security) 2001	1/1/2001 – 12/31/2075	1/1/2001	4,206
Federal Hospital Insurance (Medicare Part A) 2000	1/1/2000 – 12/31/2074	1/1/2000	2699
Federal Hospital Insurance (Medicare Part A) 2001	1/1/2001 – 12/31/2075	1/1/2001	4730
Federal Supplementary Medical Insurance (Medicare Part B) 2000	1/1/2000 – 12/31/2074	1/1/2000	6494
Federal Supplementary Medical Insurance (Medicare Part B) 2001	1/1/2001 – 12/31/2075	1/1/2001	8084
Railroad Retirement 2000	9/30/2000 – 12/31/2073	12/31/1998	-21
Railroad Retirement 2001	1/1/2001 – 12/31/2076	1/1/2001	-10

Black Lung (Part C) 2000 …………………… ....9/30/2000 – 9/30/2040		6/30/2000	-4
Black Lung (Part C) 2001 ....9/30/2001 – 9/30/2040		6/30/2001	-4

The following notes are an integral
part of this financial statement.