Federal Accounting Standards Advisory Board

October 7, 2004

Memorandum

To: Members of the Board

From: Melissa Loughan, Assistant Director

Through: Wendy M. Comes, Executive Director

Subj: **Heritage Assets and Stewardship Land Project, Tab H**[1]

The Heritage Assets and Stewardship Land project was last on the agenda in March 2004, when the public hearing was held on the Exposure Draft *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information*. As you recall, the participants at the public hearing did not support the Board's proposal. The testimonies reiterated many of the issues conveyed in the comment letters, which included the following:

- Need for more specific guidance, especially as it relates to reporting unit information.
- Cost-benefit considerations as the cost to implement and audit the proposed standard would be significant.
- Agencies would most likely present less information and/or the information would be disjointed when presented in different sections of the report.

The project has not been on the agenda since March to allow time for staff to research issues further, review alternatives for an incremental or staggered transition toward implementation of the proposed standard and develop options for consideration by the Board.

A staff issues paper is included in the binder materials that details key areas for discussion, such as Accountability and Stewardship Considerations, Categorization and Unitization, Materiality, Audit Costs, and Possible Phased Implementation Methods. Each topic area includes a Staff Analysis/Comments Section and Questions for the Board, which will hopefully guide the discussion.

The main objective for the October Board meeting is to discuss the above areas and related questions for the Board, so staff will learn the Board's direction and determine next actions on the project.

If you have questions or concerns, please contact me at 202-512-5976 or by email at loughanm@fasab.gov.

[1] The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

Heritage Assets and Stewardship Land, Tab H
Staff Issue Paper--Topics for Discussion

Status of Heritage Assets & Stewardship Land Project 2
High-level questions for the Board 3
Current Standards for Heritage-type Assets for Other Standard-Setting Bodies 4
FAS 116 Accounting for Contributions Made and Contributions Received: 4
GASB 34 Section--Reporting Works of Art and Historical Treasures 4
Staff Analysis/Comments 5
Questions for the Board 5
Accountability and Stewardship Considerations 5
Federal Real Property Asset Management Initiative 5
Executive Order 13327 Federal Real Property Asset Management 6
Executive Order 13287 Preserve America 6
Advisory Council Guidelines on Implementing Executive Order 13287 Preserve America 7
Becoming Better Stewards of Our Past, Recommendations for Enhancing Federal Management of Historic Properties, March 2004 8
National Historic Preservation Act Section 110 8
Staff Analysis/Comments 8
Questions for the Board 9
Categorization and Unitization Issues 9
Looking at SFFAS 8 9
Categorization 10
Unitization 10
Heritage Assets Categorization Project 11
Staff Analysis/Comments 12
Questions for the Board 13
Materiality Issues 13
Language in the current proposal 13
AAPC Stewardship Guidance Workgroup 13
Staff Analysis/Comments 24
Questions for the Board 24
Audit Cost Issue 24
Purpose of Roundtable with OIG and CPA Firms 24
Participants 25
Questions provided to participants for consideration 25
Discussion Summary 26
Staff Analysis/Comments 27
Questions for the Board 28
Possible Phased Implementation Methods 28
Based on proposed required reporting disclosures 28
Based on audit assertions 30
Based on entity 31
Staff Analysis/Comments 31
Questions for the Board 31
High-level questions for the Board and Staff Recommendations 31

Status of Heritage Assets & Stewardship Land Project

As it has been several months since the Heritage Assets and Stewardship Land Project has been on the agenda, staff thought it would be helpful to provide the Board with a brief history and status of the project.

The ED *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information* was issued on August 20, 2003 with comments requested by November 10, 2003. The ED proposes that heritage assets and stewardship land information be classified as basic information, except for condition information which will be classified as required supplementary information (RSI).

The ED provides for a line item to be shown on the balance sheet for significant heritage assets and stewardship land, but no financial amount should be shown. Instead, the line item would reference a note disclosure that would provide minimum reporting requirements. The ED introduces minor changes to the current disclosure requirements for heritage assets and stewardship land by requiring additional reporting disclosures about entity stewardship policies and an explanation of how heritage assets and stewardship land are pertinent to the entity's mission. The ED includes disclosure requirements for the U.S. Government-wide Financial Statement that would provide for a general discussion and direct users to the applicable entities' financial statements for more detailed information on heritage assets and stewardship land. The ED also incorporates the revised multi-use heritage asset standards of SFFAS 16 and the deferred maintenance reporting requirements related to heritage assets and stewardship land from SFFAS 14. Accordingly, the ED proposes rescissions to those standards. As a result, the ED will provide all current standards for heritage assets and stewardship land.

The Board discussed the comments received on the ED at the December 10-11, 2003 FASAB meeting. Based on the comment letters received, staff determined the following summary of responses:

- A majority of the respondents do not agree with the Board's proposal for heritage assets and stewardship land to be reported as basic information.
- Most respondents agree with the Board's new disclosure requirements and do not foresee any problems with the new disclosure requirements about entity stewardship policies and an explanation of how heritage assets and stewardship land are pertinent to the entity's mission.
- Most respondents do not agree with the proposed effective date and believed additional time was necessary for implementation.

The Board held a public hearing on the ED and comments in conjunction with the March 2004 Board meeting. Individuals from the Library of Congress, U.S. Department of Agriculture, Department of Interior (including representatives from the CFO, OIG and IPA currently performing the DOI audit), and a representative from the Institute for Truth in Accounting provided testimony to the Board.

The major issues conveyed in the comment letters and reiterated at the public hearing included the following:

- Need for more specific guidance, especially as it relates to reporting unit information.

- Cost-benefit considerations as the cost to implement and audit the proposed standard would be significant.
- Agencies would most likely present less information and/or the information would be disjointed when presented in different sections of the report.

The project has not been on the agenda since March to allow time for staff to research issues further, review alternatives for an incremental or staggered transition toward implementation of the proposed standard and develop options for consideration by the Board. In addition, the project has not been on the agenda as next actions on this ED may depend upon and follow the Board's decisions regarding the "Systems and Control" and "Stewardship" Objectives in the Concepts project.

<u>High-level questions for the Board</u>

As noted above, the Board is currently working on a Concepts Project, including an Elements project that may influence the Board's decision on the HA & SL project. Accordingly, staff would like to ensure the Board's direction on the HA & SL project is consistent and supportive of those efforts. Therefore, staff believed it would be helpful to ask the following:

- Staff is currently working on a White Paper in the Concepts Project that will look at the objectives more closely. As this project relates closely to the "Systems and Control" and "Stewardship" Objectives, does the Board foresee any problems with moving forward with the HA & SL project?
- In conjunction with the Concepts Project, staff has drafted a potential "assets" section of a concepts statement on elements. As this project closely relates to the asset definition, does the Board foresee any problems with moving forward with the HA & SL project? As envisioned, staff plans to test the working draft definition for asset against heritage assets and stewardship land.

There are other high-level questions for the Board that will need to be discussed to determine next actions on the project, but staff believes these questions would best be addressed after the Board members read the binder materials related to the heritage assets and stewardship land project.

Staff has included a Staff Analysis/Comments Section and Questions for the Board after each discussion area, which will guide our Board meeting discussion. Through that discussion, staff will learn the Board's direction on various issues and most likely answer the other high-level questions.

Meaning, after review of the Binder materials and discussion at the Board meeting, does the Board still want to move forward with the current proposal? More specifically:

- Does the Board agree with the disclosure requirements in the proposed standard?
- Does the Board agree that the heritage asset and stewardship land information should be classified as basic, except condition information, which is RSI?
- Are there Board members that wish to present alternatives for consideration?

Current Standards for Heritage-type Assets for Other Standard-Setting Bodies

Although provided and discussed in previous Board meetings, staff thought it would be helpful to include a summary of the current standards for heritage assets for other standard setters.

It is important to note that while FASAB's proposed standard disclosure and presentation for heritage assets is very similar to the other standard setting bodies—there are two major differences. **First, GASB and FASB encourage capitalization of collections and the FASAB proposal does not. The other difference relates to the required disclosures. Specifically, the Board's current proposal requires a description of each major category of heritage assets and specific unit information for those categories. However, the other standard setters simply require a description of the collections**.

Staff would like to note that in our review of museum reporting practices (See **Exhibit 1** for summary), there were very few museums that actually elected to capitalize their collections. In addition, the description of the collections was very brief in the footnotes. However, many museums actually listed all of their acquisitions (individually) for the year in their annual reports.

<u>FAS 116 Accounting for Contributions Made and Contributions Received:</u>

FAS 116 defines collections, provides guidance on capitalizing collections, and other works of art and historical treasures. It provides that works of art, historical treasures and similar items that are not part of a collection should be recognized as assets in the financial statements. **Although it encourages capitalization of collections, it does not require that items be capitalized as long as three conditions are met.** Those conditions are that collections be: 1) held for public exhibition, education, or research, 2) protected and preserved, and 3) subject to a policy that requires that proceeds from sales of items be used to purchase like items. If the conditions are not met, the collections must be capitalized. FAS 116 encourages entities to either capitalize retroactively collections acquired in previous periods or capitalize prospectively.

Those who do not capitalize or who capitalize prospectively must:

- **Describe collections**
- **Describe the relative significance of collections**
- **Describe collections' accounting policies**
- **Describe collections' stewardship policies**
- **Describe deaccessed items**
- **Disclose deaccessed items' fair value**
- **Refer to the above disclosures in a line item on the face of the statement of financial position.**

<u>GASB 34 Section--Reporting Works of Art and Historical Treasures</u>

GASB 34 ¶26-27 provides that governments should capitalize works of art, historical treasures, and similar assets at their historical cost or fair value at date of donation (estimated if necessary) whether they are held as individual items or in a collection.

Governments are encouraged, but not required, to capitalize a collection (and all additions to that collection) whether donated or purchased that meets all of the following conditions; the collection is:

a. Held for public exhibition, education, or research in furtherance of public service, rather than financial gain
b. Protected, kept unencumbered, cared for, and preserved
c. Subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections.

Capitalized collections or individual items that are exhaustible, such as exhibits whose useful lives are diminished by display or educational or research applications, should be depreciated over their estimated useful lives. Depreciation is not required for collections or individual items that are inexhaustible.

For collections not capitalized, disclosures should provide a description of the collection and the reasons these assets are not capitalized.

Staff Analysis/Comments

Staff notes that there are two major differences between the Board's current proposal and other standard setters. First, GASB and FASB encourage capitalization of collections and the FASAB proposal does not. It should be noted that in our review of museum reporting practices, there were very few museums that actually elected to capitalize their collections. The other difference relates to the required disclosures. Specifically, the Board's current proposal requires a description of each major category of heritage assets and specific unit information for those categories. However, the other standard setters simply require a description of the collection. Although not required, staff noted in their review of museum reports that several museums actually listed specific individual acquisitions in their annual reports.

Questions for the Board

- Does the Board have any questions or comments about the comparison of FASAB's proposal to FASB and GASB current standards?

Accountability and Stewardship Considerations

As noted in the comparison of the FASAB proposed standard with other current standards, one main difference is FASAB's reporting requirement of unit information. It may be logical for the Board to consider further whether this is an appropriate requirement.

As the Board deliberates this issue further, staff believed the Board would be interested to learn about some recent initiatives that promote accountability and stewardship over real property assets and heritage assets. A brief summary of each is included below and more detailed information on each is attached.

Federal Real Property Asset Management Initiative

The President's Management Agenda (PMA) is the Administration's bold strategy for improving the management and performance of the federal government. The Agenda contains five government-wide goals along with program initiatives and agency specific goals and to improve federal management and deliver results that matter to the American people. In February 2004, the Federal Real Property Management Initiative was added to the PMA.

The initiative resulted from acknowledgement that the Federal Government has never done a good enough job of managing its real property assets. **Specific problems cited in the area of real property management include:** ***Lack of accountability within the Federal Government, Lack of useful property informatio****n within Federal agencies, and Abundance of underused or unneeded Federal property.* The initiative includes *Establishing a Senior Real Property Officer at Federal agencies, Establishing a Federal Real Property Council, and Reforming the authorities for managing Federal real property.*

For more information on the Federal Real Property Management Initiative, see **Exhibit 2**.

Executive Order 13327 Federal Real Property Asset Management

In conjunction with the PMA initiative above, the President also signed the Federal Real Property Asset Management Executive Order. The purpose of the order is "to promote the efficient and economical use of Federal real property resources in accordance with their value as national assets and in the best interests of the Nation." Specifcally, it states that "**It is the policy of the United States to promote the efficient and economical use of America's real property assets and to assure management accountability for implementing Federal real property management reforms**. Based on this policy, executive branch departments and agencies shall recognize the importance of real property resources through increased management attention, the establishment of clear goals and objectives, improved policies and levels of accountability, and other appropriate action."

Although the order does exclude "public domain land (including lands withdrawn for military purposes) or land reserved or dedicated for national forest, national park, or national wildlife refuge purposes except for improvements on those lands," it does "incorporate planning and management requirements for historic property under Executive Order 13287 [Preserve America] of March 3, 2003." It also states that "**In order to ensure that Federally owned lands, other than the real property covered by this order, are managed in the most effective and economic manner, the Departments of Agriculture and the Interior shall take such steps as are appropriate to improve their management of public lands and National Forest System lands and shall develop appropriate legislative proposals necessary to facilitate that result**."

For the complete text of Executive Order 13327 Federal Real Property Asset Management, see **Exhibit 3**.

Executive Order 13287 Preserve America

As noted above, the Executive Order 13327 Federal Real Property Asset Management incorporated the planning and management requirements for historic property under Executive Order 13287 Preserve America. Issued in March 2003, the order reaffirms the National Historic Preservation Act that directs the Federal Government to administer federally owned, administered, and controlled histroic resources in a spirit of stewardship. The Executive Order includes a number of actions that are intended to encourage better accountability for the use of federally owned historic properties.

The order provides that it is "the policy of the Federal Government to provide leadership in preserving America's heritage by actively advancing the protection, enhancement, and contemporary use of the historic properties owned by the Federal Government, and by promoting intergovernmental cooperation and partnerships for the preservation and use of historic properties." It further states that "**The Federal Government shall recognize and**

manage the historic properties in its ownership as assets that can support department and agency missions while contributing to the vitality and economic well-being of the Nation's communities and fostering a broader appreciation for the development of the United States and its underlying values."

One of the intents of the order is to improve federal agency planning and accountability of historic property. It emphasizes that accurate information on the state of Federally owned historic properties is essential to achieving the goals of this order and requires "**Each agency with real property management responsibilities shall prepare an assessment of the current status of its inventory of historic properties required by section 110(a)(2) of the NHPA (16 U.S.C. 470h-2(a)(2)), the general condition and management needs of such properties, and the steps underway or planned to meet those management needs**." The order also requires "Each agency with real property management responsibilities shall, by September 30, 2005, and every third year thereafter, prepare a report on its progress in identifying, protecting, and using historic properties in its ownership and make the report available to the Council and the Secretary."

The order also requires that "Each agency shall ensure that the management of historic properties in its ownership is conducted in a manner that promotes the long-term preservation and use of those properties as Federal assets and, where consistent with agency missions, governing law, and the nature of the properties, contributes to the local community and its economy" as a way to improve stewardship over the historic properties.

For the complete text of Executive Order 13287 Preserve America, see **Exhibit 4**.

<u>Advisory Council Guidelines on Implementing Executive Order 13287 Preserve America</u>

Section 3(c) of Executive Order 13287 requires the ACHP to prepare a report to the President by February 2006, and every third year thereafter, on the state of the Federal Government's historic properties and their contribution to local economic development. The primary basis for this report will be provided by agencies with real property management responsibilities in accordance with the provisions of Sections 3(a)-(c) of order. Agencies are to prepare and, not later than September 30, 2004, submit to the Chairman of the ACHP and the Secretary of the Interior an assessment of: 1) the current status of their inventory of historic properties as required by Section 110(a)(2) of NHPA; 2) the general conditions and management needs of such properties; 3) the steps underway or planned to meet the management needs of such properties; and 4) an evaluation of the suitability of the agencies' types of historic properties to contribute to community economic development initiatives, including heritage tourism.

In addition, agencies are to review their regulations, management policies, and operating procedures for compliance with Sections 110 and 111 of NHPA, and provide the results of that review to the ACHP and the Secretary of the Interior no later than September 30, 2004. Subsequently, on September 30, 2005, and every third year thereafter, **each agency with real property management responsibilities must prepare and submit to the ACHP and the Secretary of the Interior a report detailing the progress that the agency has made in identifying, protecting and using historic properties in its ownership**.

The Advisory Council on Historic Preservation (ACHP) published advisory guidelines intended to assist Federal agencies with real property management responsibilities in preparing the assessments and reports outlined in the order. Agencies are encouraged to use the advisory guidelines as a template to ensure that adequate, complete, and useful information is submitted.

See **Exhibit 5** for the complete Advisory Council Guidelines on Implementing Executive Order 13287 Preserve America. It is important to note on page 8 of the guidelines, it provides "Does your agency coordinate its data gathering for historic properties under its ownership or control with required Federal audit, accounting, and financial management reporting?" as one of the "10 Major Questions to Address in the Section 3 Reports." In this section, the guide discusses FASAB's reporting requirements for heritage assets.

Becoming Better Stewards of Our Past, Recommendations for Enhancing Federal Management of Historic Properties, March 2004

As noted above, EO 13287 Preserve America directed the Advisory Council on Historic Preservation to provide the President and heads of Federal agencies with recommendations on further stimulation the initiative, creativity, and efficiency in the Federal stewardship of historic properties.

Their first report *Becoming Better Stewards of Our Past*, Recommendations for Enhancing Federal Management of Historic Properties issued in March 2004 included several recommendations. One of particular interest was "The Federal Government should create or enhance accountability systems to measure success in the stewardship of federally owned historic properties." **The recommendation included a discussion of FASAB and suggested "The Board should review and, if appropriate, revise or clarify its guidance on heritage asset reporting to improve consistent and comparable data collection and reporting**." The report also suggested that OMB should consider making specific recommendations to agencies on improving their management of historic properties.

The excerpt from the report is included at **Exhibit 6** for your information. The complete report can be found at http://www.achp.gov/pubs-2004stewardshipreport.html

National Historic Preservation Act Section 110

Although this Act was last amended in 2000, staff believed Section 110 may be helpful for the Board's consideration since Executive Order 13287 Preserve America does reaffirm this Act and includes many references to this particular section. The purpose of NHPA is to administer federally owned, administered, and controlled histroic resources in a spirit of stewardship. Section 110 of NHPA addresses Federal agencies' responsibility to preserve and use historic properties. Section 110 requires each Federal agency to establish a preservation program that ensures that "**historic properties under the jurisdiction or control of the agency, are identified, evaluated, and nominated to the National Register" and that such assets "are managed and maintained in that considers the preservation of their historic, archaeological, architectural, and cultural values**."

For excerpt text from the National Historic Preservation Act, see **Exhibit 7**.

NOTE: There are many other long-standing specific laws, regualtions and policies that are specific to entities or specific to certain types of assets that are not included here. This listing pertains to recent government-wide intiatives.

Staff Analysis/Comments

Staff notes that there have been several recent initiatives that promote accountability and stewardship over real property assets and heritage assets. Staff believes that these initiatives should be considered as the Board deliberates the issues further. Staff believes these initiatives

provide further support for the Board's decision to classify the heritage assets and stewardship land as basic information and the importance of accountability for these types of assets.

Questions for the Board

- Does the Board have any comments or questions about the recent initiatives?
- Are there any areas that the Board would like staff to research further?

Categorization and Unitization Issues

Comment letter respondents and public hearing participants noted unitization as a major implementation issue. Therefore, the Board directed to staff to research the unitization issue further.

Staff believes that in looking at the issue of units, it is appropriate to look at categorization first, as staff believes this is the emphasis of the proposed standard. Staff believes the issue may better be described as what is the proper aggregation or categorization of assets for presentation and what is the proper unit of reporting within those categories.

Looking at SFFAS 8

Considering the ED is reclassifying the information previously reported as RSSI for HA and SL, staff thought it would be appropriate to look at SFFAS 8 for a better understanding of the Board's original intent with categorization and unitization.

SFFAS 8 provides considerable latitude on how to present information on HA and SL. Because of the unique character of this information, agencies are encouraged to experiment with various narratives, tables and schedules. The lack of specific requirements for heritage asset information was intended to encourage creativity in reporting the variety of heritage assets held by federal entities. It should be noted that Appendix B of SFFAS 8 illustrates sample report formats that entities might refer to when reporting on SL and HA. Appendix B was only intended as a guideline, since the Board provided entities with "maximum flexibility" when applying the stewardship standards, according to the Basis for Conclusions to SFFAS 8, paragraph 124.

Specifically, the Basis for Conclusions provides the following:

> 123. When the Board developed the standards for stewardship reporting, its intention was to provide overall guidance on definitions, recognition, measurement, and minimum and recommended reporting. This broad guidance was intended to provide the basic reporting requirements while allowing each entity maximum flexibility in such areas as determining what constitutes the individual stewardship items for that entity, which costs are directly attributable to the stewardship item, and how best to report on multi-use items so that users will gain the best picture of the entity's financial and performance information.
>
> 124. The Board believes that the desire for more specific guidance expressed by several respondents stems from the belief that without such guidance, an entity's determination of how to apply the standards could be questioned. Nevertheless, the Board reiterates its position that entities should be provided maximum flexibility when applying the stewardship standards. However, **entities should make the determination of how best to apply the stewardship standards based on a thorough analysis of their individual entity, including its mission,**

financial practices, and the impact of its mission and operation on financial report users and on the Nation. Finally, all entity determinations of the applicability of stewardship standards should be thoroughly documented.

Categorization

The proposed standard (as well as SFFAS 8) emphasizes reporting on asset categories, rather than individual assets. Par. 28 c) of the proposed standard requires "A concise description of each major category of heritage asset" and then certain reporting requirements for them. Similarly, par. 44 c) requires "A concise description of each category of major stewardship land use" and then certain reporting requirements for them.

Based on this, it would appear that entities should designate asset reporting categories that allow inclusion and aggregation of their SL and HA. Entities should determine the appropriate level of detail for their categorization. It is helpful if entities designate asset categories that are meaningful and reflect how the entity views the assets for management purposes. Doing so increases the likelihood that information about the categories will be readily available from existing management systems.

The information that is appropriate for reporting SL and HA can vary from one entity to another. The amount and level of detail of the information presented depends, in part, on the mission of the entity and the materiality of the assets in question. For example, the extensive and detailed categories and subcategories reported by the Department of the Interior, which has a stewardship mission, might be more extensive than is appropriate for the Department of Defense, which does not.

Unitization

Par. 27 and 43 of the proposed standard, state that categories of SL and HA shall be quantified in physical units, rather than in monetary terms. However, the proposed standard does not define the term "physical units" or specify which physical units should be used to quantify the variety of SL and HA categories held by federal entities. The selection of the physical unit for quantifying a category is left up to entities. The proposed standard is consistent with the language and Board's intent in SFFAS 8.

Although the standard does not specify it, it is logical that entities should select physical units that are meaningful and based on how they actually manage the assets. Accordingly, quantities should be measured in a manner consistent with data available from existing management systems.

Defining physical units as individual items to be counted is not necessary. Particularly for collection-type heritage assets, it may be appropriate to define the physical unit as a collection, or a group of assets located at one facility, and then count the number of collections or facilities. Meaning, the level of detail may differ by entity, however; each entity should measure their asset quantities in a manner consistent with how they manage.

Based on the proposed standard (as with SFFAS 8) entities have considerable latitude and flexibility in designating categories and determining a meaningful level of aggregation for reporting. For example, should a library report that it has Justice Blackman's collection of papers or that it has 10,000 pieces of paper in Justice Blackman's collection? Further, should a

museum report that is has 10 dinosaur skeletons or 10,000 dinosaur bones, or simply provide a narrative description of the types of skeletons (other similar items) at a particular facility?

Ultimately, the answer is influenced by how the entity manages and materiality considerations. Curators may be required to count the number of individual items in a museum collection for control purposes. But due to materiality considerations, entities may choose to report a higher level of aggregation such as the number of collections or facilities in which individual items are located. Although individual item counts may not be necessary to support the reporting requirements in the proposed standard, this does not mean that item counts for management control and safeguarding purposes at specific locations are not necessary. For example, as discussed in the Accountability and Stewardship Considerations section above, there are public laws and other regulations that may require such counts.

Heritage Assets Categorization Project

The Board also requested staff to determine if there was a way to provide additional guidance on the categorization and unitization issue. As presented at previous Board meetings, in 1998-1999 there was a multi-agency team engaged in a project to identify and define standard categories and subcategories for heritage assets that would facilitate reporting of complete, consistent, and comparable heritage asset information by Federal agencies, consolidating departments, and the U. S. Government. These standard categories and subcategories were intended to provide an overarching, high-level framework for aggregating the various heritage asset categories that are reported by agencies throughout the government.

The team developed proposed standard categories, subcategories, and physical units of measurement for heritage assets based on an analysis of the government's heritage assets, and consultation with experts in the field of federal museum management and historic preservation, representatives from the Departments of Defense and Interior, the Smithsonian Institution, the GAO, and other entities. The team also developed definitions for the proposed categories and developed crosswalk to entities' reports to show how the various categories reported by Federal agencies fit within the proposed standard categories.

The Proposed Standard Heritage Asset Categories, Subcategories and Related Physical Units determined by the team are as follows:

Category	Subcategories	Physical Units[1]
Natural Heritage Assets		
	Wildlife Preservation Areas	Item Count
	Land Protection Areas	Item Count
Cultural Heritage Assets		
	Structures	Item Count
	Monuments and Memorials	Item Count
	Heritage Sites	Item Count
Collection-type Heritage Assets		

[1] This chart was drawn from the Heritage Asset Categorization Team's report. Staff believes that this would be a good starting point, but certain areas, such as physical units could be expanded upon to show further levels of aggregation and units at sub-category levels—meaning that item counts could be things such as the number of museums in that category, number of collections in that category, or individual items in that category.

	Biology	Item Count
	Geology	Item Count
	Paleontology	Item Count
	Archeology	Item Count
	Ethnology	Item Count
	History	Item Count
	Archival	Cubic Feet
	Artwork	Item Count

The complete Heritage Asset Categorization project report is included at **Exhibit 8**.

Staff Analysis/Comments

Staff recognizes that there may be difficulties for agencies in determining the appropriate level of aggregation for reporting categories of heritage assets. However, staff believes that the agencies are in the best position to determine the most meaningful level of presentation. Staff believes that ultimately the presentation would depend upon the specifics of the entity—its mission, the types of heritage assets, how it manages, and materiality considerations. It would be difficult for the proposed standard to define such specific reporting requirements, as they may be unique to each entity.

In drafting the proposed standard, staff had envisioned the required disclosures to be presented in a concise format similar to the format that most entities present for general property, plant and equipment—which is also similar to the example illustrations provided in SFFAS 8.

Staff also notes that the Board has tried to limit detailed illustrations and specific examples as the Board believed there would be the risk in that the auditors would believe that unless the preparers followed the specific examples, the preparers would not be adhering to the standards and/or preparers might use the examples as a justification for providing only minimum reporting.

Staff notes that there has been work by various task forces or organizations to address issues identified such as standardized categories, definitions of units of measurements, and other areas where prescriptive guidance has been requested. The task forces did contain representatives from pertinent agencies and experts in the field, which most likely would provide for a more comprehensive assessment than could be provided by the Board.

Considering the extensive research performed by the Heritage Assets Categorization Team, their proposed categories and subcategories and related physical units should be a good starting point for additional guidance that could be included in a Technical Release or Staff Implementation Guidance. For instance, staff believes that certain areas such as physical units could be expanded upon to show further levels of aggregation and units at sub-category levels—meaning that item counts could be things such as the number of museums with that category, number of collections in that category, or individual items in that category. Staff believes it would be difficult to include specific categories and units in proposed standard as there are many items that are unique to each agency. In addition, staff believes that any guidance would have to include categories and units as "suggested" or "potential", even in a Technical Release.

Staff does believe that additional language could be added to the proposed standard to reiterate that categorization and unitization is determined by the preparer and the preparer should document the reasoning for major class determinations.

Staff does believe that additional language could be added to the proposed standard to clarify that reporting is at the majpr category level, to ensure that readers do not interpret this to mean an item-by-item count.

Staff does believe that additional explanatory language could be added to the Basis for Conclusion that conveys the information included in the Categorization and Unitization section above.

Questions for the Board

- Does the Board wish to reconsider the specific reporting requirements in the proposed standard—specifically, does the Board still wish to include reporting unit information by major category?
- Does the Board wish to prescribe specific reporting categories and units in the proposed standard
- Does the Board wish to include additional specific language about categories or units in the proposed standard?
- Does the Board wish to include additional specific language about categories or units in the Basis for Conclusion?
- Does the Board wish to include sample or suggested reporting formats in the proposed standard?

Materiality Issues

The concept of materiality and how it would apply in the reporting of this type of non-financial information has come up during several Board discussions of the HA & SL project. Staff wanted to find out if this is an area that the Board would like to address further in the HA & SL project.

Language in the current proposal

The current proposal has the standard "**The provisions of this Statement need not be applied to immaterial items**" included.

Par. 28 and 44 of the proposed standard requires disclosures for "**Entities with significant heritage assets/ stewardship land…**" (Note: The ED shows "Entities with significant amounts of heritage assets/ stewardship land…" but the Board decided to remove the "amounts of" at a previous Board meeting. In earlier drafts of the ED, the language read "Entities with material heritage assets/ stewardship land…" but the Board decided to replace material with significant.

AAPC Stewardship Guidance Workgroup

The AAPC Stewardship Guidance Workgroup included a detailed discussion on the application of materiality in HA and SL in their draft guide that the Board may find helpful. As you may recall, the AAPC Stewardship Guidance Workgroup has done extensive research and collaboration on how to report and audit stewardship land and heritage assets, drawing upon early implementation experience of the Departments of Interior, Defense, Agriculture, and other agencies. The group developed a Draft guide-- Reporting and Assurances Guide for

Stewardship Land and Heritage Assets—that was exposed for comments. However, in 2002 the AAPC decided not to finalize the guide based on FASAB's decision to reclassify RSSI. The AAPC plans to re-evaluate the guide and make necessary revisions after FASAB finalizes this project.

The following is an excerpt from the Reporting and Assurances Guide for Stewardship Land and Heritage Assets prepared by the Stewardship Guidance Workgroup commissioned by the AAPC. The complete Guide was provided to Board members at the February 2003 Board Meeting.

SECTION 2. DETERMINING MATERIALITY

In the interest of meaningful and cost effective information, preparers and auditors of SL and HA information need to understand and apply the concept of materiality in order to decide what is material and what is not. SFFAS No. 8, paragraph 41, states "The provisions of this statement need not be applied to immaterial items." Key issues are (1) how should materiality be applied to SL and HA that are not reported in dollars, and (2) what is the appropriate level of detail for reporting and auditing SL and HA information?

The preparer's and the auditor's consideration of materiality is a matter of professional judgment and is influenced by their perception of (1) the information necessary to demonstrate accountability for SL and HA, and (2) the needs of a reasonable person who will rely on the principal financial statements and the stewardship report. This approach incorporates two fundamental values of federal financial reporting: accountability and decision usefulness. However, while they operate from the same theoretical framework, the preparer's and the auditor's roles in applying the materiality concept differ.

In formulating the stewardship report, the preparer should identify meaningful levels of aggregation by determining whether assets are material enough to warrant classification and presentation in separate categories. In examining SL and HA, the auditor should assess risk, plan tests, evaluate any omissions or misstatements, and express an opinion in light of his or her judgments about materiality.

Materiality has both quantitative and qualitative characteristics. Traditional materiality judgments about financial information are primarily quantitative and focused on dollar amounts. However, the fact that SL and HA are not reported in dollars requires special attention to qualitative factors such as the nature of the assets and the circumstances in which the materiality judgment is made.

The preparer's and the auditor's materiality judgments for SL and HA are concerned with thresholds. FASB's Statement of Financial Accounting Concepts No. 2, paragraph 126 asks, "Is an item, an error, or an omission large enough, considering its nature and the attendant circumstances, to pass over the threshold of what separates material from immaterial items?"

ACCOUNTABILITY AND DECISION USEFULNESS

Traditional definitions of materiality for financial information center on "decision usefulness," a concept which relates to the needs of a reasonable person who relies on reported information to make decisions. The focus on decision usefulness originated from the primary objective of financial reporting for business enterprises established by FASB: "Financial reporting should

provide information that is useful to present and potential investors and creditors and other users making rational investment, credit, and similar decisions."[2]

However, the users of SL and HA information and their needs are not well understood because we are in the infancy of stewardship reporting. These needs will likely evolve and be more clearly identified as the information is made available and attracts users who rely on it for making decisions.[3] In the meantime, attempting to make materiality determinations about SL and HA information based solely on user needs (i.e., decision usefulness) is an uncertain approach.

A different approach to determining materiality is one based on *accountability*, the primary value of federal financial reporting from which decision usefulness flows, according to SFFAC No. 1. As the standard-setting body for the federal government, FASAB stated that there are *two* values that provide the foundation for governmental financial reporting: "accountability" and its corollary, "decision usefulness." FASAB explained that "Because a democratic government should be accountable for its integrity, performance, and stewardship, it follows that the government must provide information useful to assess that accountability.[4]

Under an "accountability approach" to materiality, preparer's and auditors use their professional judgment to decide, on behalf of users, what information is needed to demonstrate accountability over SL and HA in keeping with federal accounting concepts and standards. Materiality is then evaluated in relation to the information considered necessary for accountability.

In essence, the accountability approach to materiality considers the information needed to answer the question, "What did the government do with the SL and HA entrusted to it."[5] Thus, the accountability approach provides the advantage that materiality determinations can be made in circumstances where the decision usefulness of information is not yet apparent.

Ideally, the accountability and decision usefulness approaches should be balanced so that materiality determinations for SL and HA draw upon both approaches to the extent possible. Under the resulting "balanced approach," the materiality of any omissions or misstatements are scrutinized in relation to (1) the information needed to demonstrate accountability, and (2) decision usefulness, once users' decision-making needs are known.

OPERATIVE DEFINITIONS

SFFAS No. 8, paragraph 41 provides the following definition of materiality:

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[2] Source: FASB's Statement of Financial Concepts No. 1: *Objectives of Financial Reporting by Business Enterprises,* paragraph 34.

[3] For a summary of the users of federal financial reports and their stewardship information needs, as originally identified in SFFAC No. 1 and SFFAS No. 6, see the following subsection on *Operative Definitions*.

[4] Statement of Federal Financial Accounting Concepts (SFFAC) No. 1, *Objectives of Federal Financial Reporting,* paragraphs 71 and 72.

[5] SFFAC No. 1, paragraph 105, states "The federal government derives its just powers from the consent of the governed. It therefore has a special responsibility to report on its actions and the results of those actions. …Providing this information to the public, the news media, and elected officials is an essential part of accountability in government."

"The determination of whether an item is material depends upon the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement."

This definition of materiality is authoritative for supplementary stewardship reporting under SFFAS No. 8. However, to understand and apply the definition as it relates to SL and HA, it is helpful to develop a working understanding of the term "reasonable person." For purposes of this guide, "reasonable person" is defined as:

A reader of financial reports who uses SL and HA information to contribute to an understanding of an entity's mission, operations, and financial condition.[6]

As such, a reader may belong to any of the four groups of "users of federal financial reports" described in SFFAC No. 1, paragraphs 75 through 87: citizens, Congress, federal executives, and program managers.[7] As described in the subsection on *Accountability and Decision Usefulness,* the users of SL and HA information and their decision making needs will likely evolve and be more clearly identified as this new information is made available.

Although each user group may have specific information needs which are not yet fully understood, the accountability approach to materiality affirms that the stewardship report should provide readers with an understanding of the nature and scope of the assets entrusted to federal entities and the physical condition and/or the security of those assets. Because the government must demonstrate that it is being an appropriate steward, as a minimum readers should be able to refer to the stewardship report for answers to the following questions:

"What and where are the important assets?"

"Is the government effectively managing and safeguarding its assets?"[8]

Accordingly, an item is material if omitting or misstating it would change a reader's conclusions regarding these essential questions. Citizens want assurances that the SL and HA entrusted to the government are protected and used for the purposes intended.[9] Congress, executives, and program managers need to demonstrate to those to whom they are accountable that they have, in fact, protected those resources and used them well.

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[6] This definition is based SFFAS No. 8, paragraph 1 which states that information about stewardship resources "...is important to an understanding of the operations and financial condition of the Federal Government at the date of the financial statements." FASAB introduced the concept of "financial condition" in SFFAC No. 1. Financial condition is a broader and more forward-looking concept than "financial position." The concept of financial *position* is that of a point-in-time snapshot of an entity's economic resources and the claims upon those resources. However, financial *condition* allows an assessment of an entity on the basis of additional data that could include financial and nonfinancial information. Information about financial condition can be conveyed in a variety of schedules, notes, projections, and narrative disclosures.

[7] In this guide, the terms "reader," "user," and "reasonable person" are used interchangeably and are considered synonymous with the definition of reasonable person.

[8] Source: Basis for Conclusions to SFFAS No. 6, paragraph 125.

[9] "Citizens" includes individual citizens as well as the general news media and more specialized users such as trade journals; public interest and advocacy groups; state and local legislators and executives; and analysts from corporations, academe, and elsewhere, according to SFFAC No. 1, paragraph 76.

MEASUREMENT ISSUES

In the traditional financial reporting context, quantitative measures of materiality are used as a simple and convenient way to assess materiality, with a focus on users who evaluate an entity's financial performance in order to make investment and credit decisions. Accordingly, auditors have arrived at reasonable gauges of materiality in terms of dollars reported in the basic financial statements.[10]

However, for SL and HA, there is no unifying theme upon which to base quantitative measures of materiality, such as net income. And, for heritage assets in particular, there is no common unit of measure, such as dollars, that can be used to evaluate the impact of omissions and misstatements among SL and HA categories.[11] For example, a preparer might report quantities for six separate categories of heritage assets such as 10,000 museum objects, 6,000 linear feet of archival documents, 4,000 cubic feet archeological artifacts, 2,500 paleontological items, 1,000 pieces of artwork, and 500 geological specimens.

These diverse categories with their different measures seem to have as much in common as apples, oranges, and bananas. To avoid comparability problems, an auditor might consider the quantity reported for each category to be a *separate representation* by management which stands on its own *to be examined separately*. Accordingly, the representation for a particular category might be expected to be accurate to within some range, such as a percentage of the quantity reported in that category. However, setting a materiality threshold for each category by using this "separate representation method" could be inefficient, perhaps resulting in inordinate audit resources being devoted to examining categories and evaluating omissions and misstatements that are relatively insignificant.

In contrast, a more efficient and preferable method would be for the auditor to take a *collective view* that aggregates all six reported categories into a "fruit basket" of heritage assets. Then, even though the basket consists of different "fruits," the auditor could use professional judgment to plan his work and evaluate any omissions or misstatements *in relation to the entire basket*. Also, the auditor could consider whether, in aggregate, the six reported categories "in the basket" represent a materially complete presentation of the heritage assets for which the entity should be accountable.[12] Accordingly, the auditor's conclusions relate to the fairness of the presentation for heritage assets *taken as a whole*.

Obviously, the auditor's conclusions about heritage assets do not apply to other types of assets, such as stewardship land. Under the collective view method, information reported on stewardship land categories would be aggregated into its own "basket" and the auditor would draw separate conclusions about fairness of the presentation of stewardship land *taken as a whole*.

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[10] While both preparers and auditors deal with measurement issues related to materiality, this section focuses on the auditor's perspective.

[11] Unlike heritage assets, stewardship land categories are quantified with a common unit of measure, (i.e., acres).

[12] The words "materially complete" reflect the intent that the completeness assertion should not be taken to extremes by the auditor (or the preparer). See the subsection on *Completeness, Materiality, and Meaningful Aggregation*.

Although stewardship land is quantified with a common unit of measure, an entity's stewardship land may include diverse categories that are not easily comparable on an acre for acre basis. Different parcels of stewardship land may have significantly different *qualitative* characteristics that should be considered, in addition to acreage, when making materiality judgments. Considering only the quantitative measure of acreage when assessing materiality for multiple categories of stewardship land may fail to take into account significant, relevant qualitative factors.

The "collective view method" is useful for stewardship land and heritage assets because it augments (a) traditional materiality judgments that are primarily quantitative, with (b) *subjective, qualitative judgments of the relative importance of a variety of asset categories*. The subsection on *Qualitative Considerations* provides additional guidance and decision tools for making materiality judgments involving SL and HA.[13]

Precedents for the "collective view method" can be found in both the Codification Statements on Auditing Standards (AU) and Statements on Standards For Attestation Engagements (AU). For financial statement audits, materiality is evaluated in light of a collective view of the financial statements. For example, according to AU 312.03, the phrase "presents fairly, in all material respects" indicates the auditor's belief that the financial statements *taken as a whole* are not materially misstated. AU 312.05 states that "When reaching a conclusion as to whether the effect of misstatements, individually or in the aggregate, is material, the auditor ordinarily should consider their nature and amount in relation to the nature and amount of items in the financial statements under audit."

A collective view can also be taken on attest engagements. As defined by AT 100.01: "An attest engagement is one in which a practitioner is engaged to issue or does issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party." Footnote 3 to AT 100.01 defines an assertion as follows: "An assertion is any declaration, *or set of related declarations taken as whole* (emphasis added), by a party responsible for it." In this context, the collective view of stewardship land information is one "set of related declarations taken as a whole" and the collective view of heritage asset information is another "set of related declarations taken as a whole."

Additional precedent for the collective view method appears in AT 100.50 which describes reaching conclusions about assertions in the plural, not the singular: "The practitioner should consider the concept of materiality in applying this standard. In expressing a conclusion on the conformity of a presentation of **assertions** (emphasis added) with established or stated criteria, the auditor should consider the omission or a misstatement of an individual assertion to be material if the magnitude of the omission or misstatement--individually or when aggregated with other omissions and misstatements--is such that a reasonable person relying on the presentation of the **assertions** (emphasis added) would be influenced by the inclusion or the

[13] The auditor's job is challenging because (a) SFFAS No. 8 intentionally allows considerable latitude on how to present information on SL and HA, and (b) related materiality judgments require special attention to qualitative factors. Providing examination-level assurance would be made easier if management were to provide a well-crafted, written representation that explains the criteria it used to develop the information presented on SL and HA. Such a representation would include a clear statement of the qualitative materiality considerations involved in formulating the presentation. For example, on what basis did management determine that (a) the presentation is materially complete, (b) meaningful levels of aggregation are reported, and (c) an appropriate level of detail is provided?

correction of the individual assertion. The relative, rather than the absolute, size of an omission or misstatement determines whether it is material in a given situation."

Since both the AU and the AT standards require the auditor to consider the relative size of omissions or misstatements, the question arises, "Relative to what?" Under the collective view method, the logical answer is "Relative to all of management's representations about either (1) stewardship land taken as a whole, or (2) heritage assets taken as a whole.

The collective view method does not attempt to evaluate the materiality of stewardship land or heritage assets in relation to the dollar amounts reported in the basic financial statements. This guide is based on the assumption that the information to be examined on SL and HA will be appear in a separate presentation that is distinct from the principal financial statements; (i.e., not part of, but in addition to the principal financial statements).

COMPLETENESS, MATERIALITY, AND MEANINGFUL AGGREGATION

SFFAS No. 8 requires that entities demonstrate accountability for their SL and HA. As discussed in the subsection on *Categorization,* the standard emphasizes reporting on major categories in physical units. Inherent in such reporting is the completeness assertion.

The intent is that the preparer should *do what is reasonable* to report the entity's SL and HA, and the auditor should satisfy himself that the presentation is *materially complete*. The preparer's and the auditor's viewpoints on materiality should be high enough to avoid burdensome reporting of unnecessary detail and overauditing.

To do so, preparers and auditors must differentiate between (a) detailed records that may be needed for management control and safeguarding purposes, and (b) presentations that are material for stewardship reporting. Entities may track individual assets and asset categories for control purposes that do not warrant separate presentation in their stewardship reports. Moreover, preparers need not report de minimis items (trifles), and auditors should avoid looking at materiality so strictly that *any* omission is automatically considered material.

Given that the entity's SL and HA should be reported in accordance with the completeness assertion, the preparer's consideration of materiality is *not* a screening exercise to determine which assets should be excluded from the stewardship report. Rather, the preparers' consideration of materiality focuses on identifying *meaningful levels of aggregation* for reporting; i.e., determining which SL and HA warrant classification and presentation in separate categories.

In order to meet the reporting objectives of SFFAS No. 8, consistent with the completeness assertion, and with a focus on meaningful aggregation, preparers should analyze the entity's SL and HA and apply the following treatments:

- For related assets that are considered material, establish separate categories and disclose the number of physical units in each category.

- For assets not warranting separate categories, include in a narrative summary describing those assets, but do not report physical units.[14]

[14] In aggregate, the assets included in this narrative summary may be material, but no additional presentation is required.

Auditors should perform their own analysis of the relative importance of the entity's SL and HA and should not assume that a preparer's analysis and presentation are correct. Based on their analysis, auditors should apply the following treatments, in keeping with the "collective view method" discussed in the preceding section:

- For assets that should be reported in separate categories with physical units, take a collective view that aggregates the assets in all categories and addresses their relative importance in order to assess risk, plan tests, and evaluate any omissions or misstatements.

- For assets that should be included in the descriptive narrative summary read for reasonableness.

The section on *Qualitative Considerations* provides additional guidance and decision tools to assist both preparers and auditors in making materiality judgments involving SL and HA. In particular, the flowchart in Figure 2 depicts the logic for determining the treatments to be applied by preparers and auditors.

The aggregation of SL and HA into meaningful (material) categories is analagous to a company whose financial statements report separate dollar amounts for various types of PP&E such as buildings, equipment, construction in progress, etc. The idea here is that reporting only one large, undifferentiated amount for PP&E might not meet the decision-making needs of users of the balance sheet. That is, it is probable that the judgement of a reasonable person relying on the company's PP&E information would be changed or influenced by the presentation of the additional details.

Similarly, a manufacturing company might report its inventory with separate dollar amounts for raw materials, work-in-progress, and finished goods. This breakdown provides a meaningful level of aggregation for the reader who wants to know where the manufacturing process stands in terms of incurring costs and adding value in order to convert inventory into cash through the earnings cycle.

Just as the categories for reporting inventory relate to the earnings processes of a manufacturing company, the categories for reporting SL and HA should relate to the stewardship processes and responsibilities of the government entity. This can be accomplished, in part, by including an analysis of the entity's mission as part of the determination of which asset categories are material and warrant separate classification and presentation. Other factors to be considered are whether the asset categories are considered "important to the nation" and whether they are "visible, vulnerable, or controversial." See the Focus Questions in Figure 1, below.

As mentioned in the subsection on Categorization, "The amount and level of detail of the information presented depends, in part, on the mission of the entity." Also, the Basis for Conclusions section to SFFAS No. 8, paragraph 124 states, "…entities should make the determination of how best to apply the stewardship standards based on a thorough analysis of their individual entity, including its mission, financial practices, and the impact of its mission and operation on financial report users and on the nation."

QUALITATIVE CONSIDERATIONS

To help ensure that significant, relevant factors are considered when making materiality determinations for SL and HA reporting categories, preparers should consider the focus

questions and related subquestions presented in Figure 1, below. These questions highlight the nature of the assets and the surrounding circumstances, and may help preparers decide whether presentation in a separate category with physical units is needed to demonstrate accountability. Auditors should also refer to these questions when applying the “collective view method” for assessing risk, planning tests, evaluating any omissions or misstatements, and expressing an opinion.

The focus questions and subquestions illustrate that subjective, professional judgment is inherent to materiality considerations for SL and HA. FASB’s Statement of Financial Accounting Concepts No. 2, paragraph 131, states that "...materiality judgments can properly be made only by those who have all the facts. ...no general standards of materiality can be formulated to take into account all the considerations that enter into an experienced human judgment."

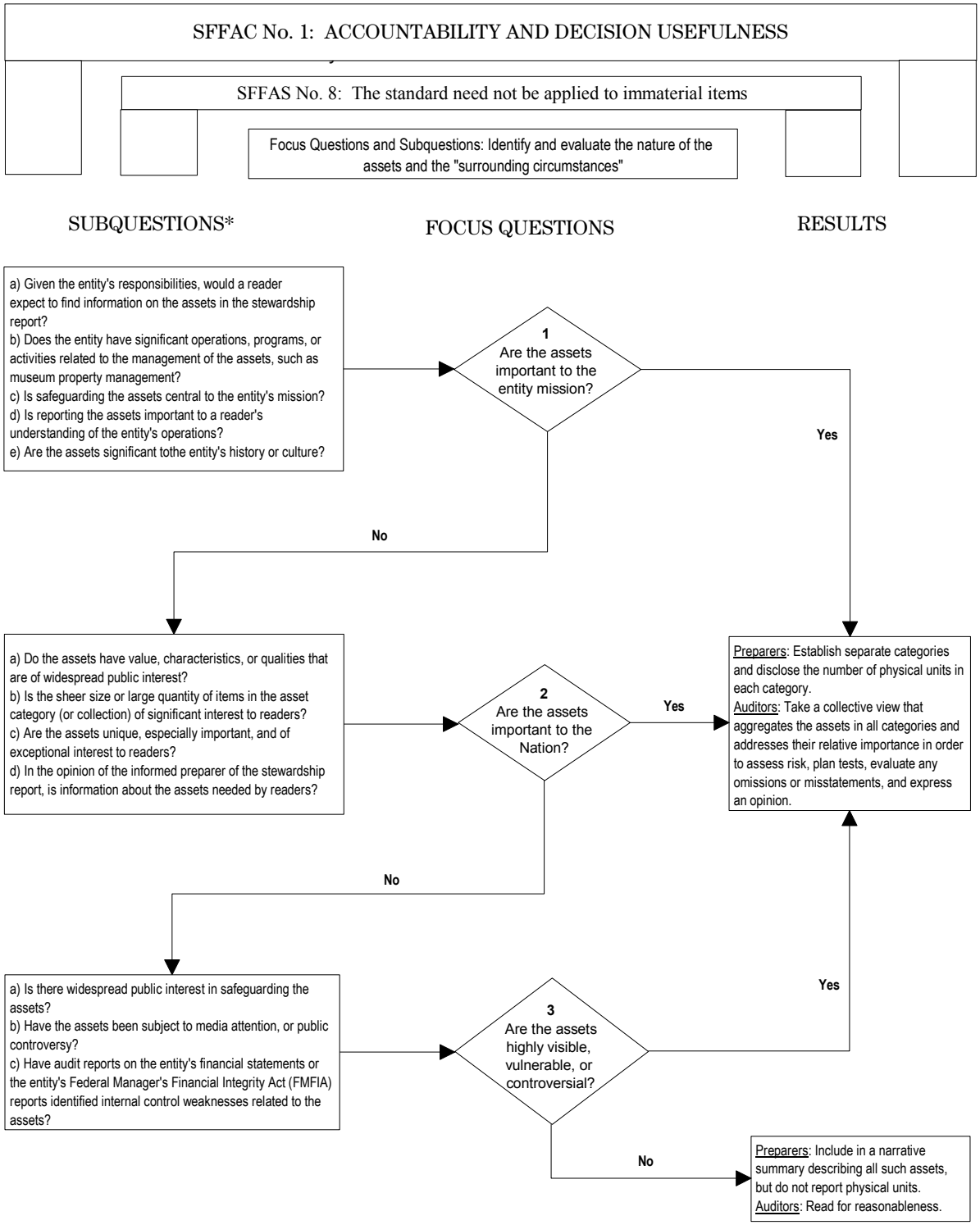
The questions are *not* intended as criteria for excluding assets from the stewardship report. SFFAS No. 8 clearly requires that an entity’s SL and HA should be reported, and the completeness assertion is inherent in such reporting. To that end, answering the questions helps preparers to identify *meaningful levels of aggregation* for reporting. Based on their answers, preparers can follow the corresponding flowchart in Figure 2 for an indication of the appropriate reporting treatment. Similarly, answering the questions helps auditors to independently assess the relative importance of the entity’s SL and HA, and they can then follow the flowchart for an indication of the appropriate audit treatment.

Most of the questions below refer to SL and HA in the plural, to emphasize reporting on asset categories. A “yes” answer to *one or more* of the main focus questions suggests that the assets are material and should be disclosed in a separate category that will be subject to examination. In contrast, a “no” answer to *all three* of the main focus questions suggests that the assets need not be disclosed in a separate category, and instead, should be included in a narrative summary that will be read for reasonableness.

As indicated by the flowchart in Figure 2, the subquestions should be considered first to help determine the answer to the related main focus question. A “yes” or “no” answer to a single subquestion does not automatically mean that the related main focus question should be answered yes or no. When evaluating the answers, certain subquestions may be given greater or lesser weight than others.

Figure 1. Focus Questions and Subquestions for Considering Materiality for Stewardship Land and Heritage Assets
Focus Question 1. *Are the assets important to the mission of the entity?* a. Given the entity's responsibilities, would a reader expect to find information on the assets in the stewardship report? b. Does the entity have significant operations, programs or activities related to the management of the assets, such as museum property management, realty management, etc.? c. Is safeguarding the assets central to the mission of the entity? d. Is reporting the assets important to a reader's understanding of the entity's operations? e. Are the assets significant to the entity's history or culture?
Focus Question 2. *Are the assets important to the nation?* a. Do the assets have value, characteristics, or qualities that are of widespread public interest? b. Is the sheer size or large quantity of items in the asset category (or collection) of significant interest to readers? c. Are the assets unique, especially important, and of exceptional interest to readers? d. In the opinion of the informed preparer of the stewardship report, is information about the assets needed by readers?
Focus Question 3. *Are the assets highly visible, vulnerable, or controversial?* a. Is there widespread public interest in safeguarding the assets? b. Have the assets been subject to media attention or public controversy? c. Have audit reports on the entity's financial statements or the entity's Federal Manager's Financial Integrity Act (FMFIA) reports identified internal control weaknesses related to the assets?

Figure 2. Flowchart for Considering Materiality for Stewardship Land and Heritage Assets



* Answer these subquestions first to help determine the answer to the related focus question.

Staff Analysis/Comments

Materiality as it is applied to HA and SL (as well as in other applications) is a matter of professional judgment and materiality has both quantitative and qualitative characteristics. Considering that HA and SL are not reported and measured in dollars as other traditional financial information, qualitative factors will play a major role in judging materiality.

Staff notes that the AAPC Draft guide-- Reporting and Assurances Guide for Stewardship Land and Heritage Assets—contains detailed focus questions and sub-questions for consideration in determining materiality for HA and SL. Staff believes the discussion, focus questions and flowchart would be a useful tool to preparers in determining material categories for presentation. Staff believes that once the proposed standard is finalized, the AAPC Workgoup will be revitalized to finalize this Guide. Staff believes that the guide is an excellent starting point for addressing certain issues. The Guide could ultimately be issued as a Technical Release through the AAPC or at minimum Staff Implementation Guidance.

Questions for the Board

- Does the Board still agree with the current wording of the proposed standard that states "Entities with significant heritage assets/ stewardship land…"?
- Does the Board believe the language included in SFFAS 8 ("The determination of whether an item is material depends upon the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement") should be included in the proposed standard?
- Does the Board believe the proposed standard should be expanded to include a discussion of materiality and how it applies to HA and SL?

Audit Cost Issue

(**NOTE**: Staff had planned to present this at the March Board Meeting. However, due to the length of discussions at the public hearing, staff was not able to present the results and summary of the round table at the March Meeting.)

Another issue brought up by respondents to the ED as well as conveyed by participants at the public hearing, was the additional audit costs that will be incurred implementing the proposed standard. Accordingly, the Board had expressed an interest in learning more about potential audit costs of implementing the proposed standard from the audit community. Staff queried Offices of Inspector General and CPA firms responsible for financial statement audits to solicit their views on the cost issue. Staff held a Roundtable meeting in February 2004.

Purpose of Roundtable with OIG and CPA Firms

The purpose of the Roundtable was to solicit input from the audit community on specific issues raised by respondents on the ED entitled *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information.* As part of its deliberations, the Board had asked staff to obtain additional information on certain issues raised by respondents. Specifically, the tentative Board consensus (as detailed in the ED) is to reclassify heritage assets and stewardship land information as basic information, except for condition information, which would be classified as required supplementary information. Several

respondents commented that the cost of auditing this information may exceed benefits obtained. The Board believes it should consider the cost of its standards relative to the benefits. Since some of the items currently reported as RSSI ultimately might be audited at examination level, staff consulted with the audit community regarding estimates of the audit costs of this proposed action.

Participants

Curtis Crider, DOI OIG	Ron Smith, DOD OIG	Barbara Sauls, DOD OIG
Nick Christopher, LOC OIG	Jay Miller, LOC	Joe Cummings, USDA OIG
Chike Gardner, DOC OIG	Amanda Windsor, DOC OIG	Kim Geier, OMB
Mark Connelly, GAO	Walt Fennell, PwC	David Cotton, Cotton & Co.
Jeff Norris, KPMG	Philip Peters	Dan Kovlak, KPMG
James Maynor, Kearney & Co	Wendy Comes, FASAB	Melissa Loughan, FASAB

Questions provided to participants for consideration

(NOTE: The following questions were provided to participants in advance of the round table to facilitate discussion.)

Considering the current proposed standard Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information reclassifies heritage assets and stewardship land information as basic information:

- Has there been an attempt to estimate the potential audit costs?
  If so- Please describe the methodology or basis for the estimate, including the following:
  - What were the estimated costs?
  - Was this estimate based on a particular agency's heritage assets and stewardship land information? Which agency? Is this agency your current audit client?
  - What would you describe as the most costly audit procedures (for example, site visits) in the estimate?
  - Did you base this estimate on providing assurance only on the required information (versus what agencies are currently reporting, which often includes additional information)?

- If not, could you provide an estimate for the costs of your current audit clients?
  - How long will it take to determine an estimate? For which agency? Is this agency your current audit client?
  - Are there any particular issues that make estimating the costs difficult?
  - What would you foresee as the most costly audit procedures (for example, site visits) in the estimate?

- Would you expect a significant increase in audit costs for only the first year that the information is audited? In other words, would the cost of audits subsequent to the first year be comparable to audits prior to the change in classification?

- Are there any other factors specific to the potential audit costs of the proposed standard that you believe should be considered by the Board during its deliberation?

Discussion Summary

- The DOI OIG representative and the representative from the CPA firm (KPMG) currently auditing DOI both conveyed that there would be a significant increase in audit costs, as well as an increase in costs for the accounting and program offices. Although considered a "swag" DOI OIG suggested that the accounting and program offices potentially could spend $2 ½ to $3 million in the initial year to implement the standard. KPMG suggested that audit fees for the initial year could be approximately $5 million, with subsequent years approximately $2 million. (NOTE: All estimates are considered very soft numbers and no detailed methodology for determining the amounts were provided.) KPMG explained the challenging aspects of the audit at DOI include:
    - Designing methodologies to test for completeness
    - Availability of historic records to demonstrate ownership
    - Multiple locations (estimated at 600 federal and 1,100 non-federal facilities)
    - Significant deficiencies in the internal controls over Stewardship Land and Heritage Assets, including:
        - DOI does not consistently follow its established procedures and controls
        - DOI does not consistently maintain and approve source documents for additions and deletions to stewardship assets
        - DOI does not consistently perform annual inventories and verifications for stewardship assets
    - Use of specialists, such as attorneys and surveyors

- No estimates of potential audit costs were provided by other participants.

- Several participants commented that there are limited funds available to agencies and there are other pressing priorities that should be considered in relation to the benefits obtained from the proposed standard. In addition, several participants raised other concerns that should be considered that affect the audit costs. Participants who did not support the proposal discussed the following:
    - Difficulties with accelerated reporting dates (USDA)
    - Agencies will reduce the information being reported (DOI)
    - Only unit information being reported (USDA)
    - No baseline inventories (LOC)
    - Count information is not as important as other factors, such as the preservation of the information (LOC)
    - Materiality issues are complex with this type of information
    - There are internal control weaknesses in this area which would naturally lead to more substantive type testing and result in more audit costs (DOI and USDA)

- Several participants commented that there are very important benefits obtained, especially considering that there are stakeholders who are very interested in this information. Participants discussed the following in support of the proposal:
    - For accountability and control, it is very important to know what heritage assets an agency has and where they are located
    - The public is concerned about these types of assets and how they are being safeguarded
    - This information is essential for prudent management of assets

- Value added may not necessarily be in the number themselves, but actually results from reporting the information and having it subject to audit implies sound management
- Providing the information and the audit may be difficult, but it is important
- Discussion resembles the same type of arguments against implementing the CFO Act over 10 years ago, but we now know how it has lead to better financial management and accountability

- Several participants suggested that if the Board moves forward with the proposed standard, certain actions could be taken by the Board to reduce costs, such as:
  - Develop an incremental approach for implementation of the standard
  - Provide language in the standard that would provide some flexibility or relief as to what would be sufficient documentation for support. One participant noted the Board provided relief in SFFAS 23 as it recognized that some historical records may not have been maintained.

<u>Staff Analysis/Comments</u>

Several participants at the round table echoed concerns noted in the comments letters and the public hearing. However, although the obstacles to the audit were discussed, potential audit cost information was not available. Also, most participants did recognize that for management purposes—especially as it relates to accountability and control, it is important for agencies to know what assets they have and where they are located. The participants did believe that the public is very interested in these types of assets and that they are safeguarded.

The participants did offer valid concerns regarding the ability to locate documentation to support ownership. Staff does agree that there could be some additional language in the standard that would provide some flexibility or relief as to what would be sufficient documentation for support. One participant noted that the Board provided relief in SFFAS 23 as it recognized that some historical records may not have been maintained and perhaps something similar could be provided in the proposed standard.

SFFAS 23 Eliminating the Category National Defense PP&E, provided implementation guidance as follows:

> 11. This standard recognizes that determining initial historical cost may not be practical for items acquired many years prior to the effective date of this standard in an environment in which the historical records were not required to be retained and may therefore be inadequate.
> 12. If obtaining initial historical cost is not practical, estimated historical cost may be used. Other information such as but not limited to budget, appropriation, or engineering documents and other reports reflecting amounts expended may be used as the basis for estimating historical cost.
> 13. Alternatively, estimates of historical cost may be derived by estimating the current replacement costs of similar items and deflating those costs, through the use of price-level indexes, to the acquisition year or estimated acquisition year if the actual year is unknown. Other reasonable approaches for estimating historical cost may also be utilized. For example, latest acquisition cost may be substituted for current replacement cost in some situations.

Staff notes that SFFAS 23 does recognize that historical records for items acquired long ago may not have been retained. However, the relief provided in SFFAS 23 relates to the valuation of the assets as it allows for estimating historical costs and suggests reasonable approaches. The proposed standard on reclassifying heritage assets and stewardship land does not require a valuation or dollar values for heritage assets and stewardship land. Therefore the specific relief provided in SFFAS 23 would not apply.

However, as the Board has recognized that historical records for items acquired long ago may not have been retained, it may be helpful to include language to this fact within the proposed standard. In addition, the Board may want to include language encouraging preparers, program offices, and auditors to develop other reasonable approaches and methods for satisfying the specific audit assertions that would rely on historical documents as evidence and support. Staff believes that this is another area that the AAPC Workgroup (which includes representatives from the audit and preparer side) could address in their guide. Meaning the workgroup could discuss the specific problem areas where there is a lack of support and determine reasonable approaches or best practices.

Questions for the Board

- Does the Board agree that additional explanatory language recognizing that historical records for items acquired long ago may not have been retained should be added?
- Does the Board agree that language encouraging preparers, program offices, and auditors to develop other reasonable approaches and methods for satisfying the specific audit assertions should be added?
- Does the Board have any questions about the Roundtable Meeting with the auditors?

Possible Phased Implementation Methods

After the Public Hearing on the Heritage Assets and Stewardship Land ED, the Board directed to staff to determine if there were alternatives that would provide for a phased implementation of the proposed standard. The Board hoped that some sort of phased implementation would provide time for the entities to address some of the issued identified, especially for consideration of the constrained resources facing most agencies.

Staff determined the following possible phased implementation methods:

- Based on proposed required reporting disclosures
- Based on audit assertions
- Based on entity

Included below is a brief description of the possible staggered implementation approaches for the Board's consideration.

Based on proposed required reporting disclosures

The current proposal includes the following for required reporting disclosures:

> a. A concise statement explaining how significant heritage assets are important to the overall mission of the entity.
>
> b. A brief description of the entity's stewardship policies for heritage assets. Stewardship policies for heritage assets are the goals and principles the entity established to guide its acquisition, maintenance, use, and disposal of heritage assets consistent with statutory requirements, prohibitions, and limitations governing the entity and the heritage assets. While not all encompassing, the policies may address

preserving and maintaining condition, providing public use or access, and enhancing the heritage assets' value over time.

c. A concise description of each major category of heritage asset. For each major category of heritage asset the following should be reported:

1.) the number of major collection or non-collection type heritage assets for which the entity is the steward as of the end of the reporting period;

2.) the additions and/or withdrawals from the category during the reporting period; and

3.) a description of the major methods of acquisition and withdrawal of significant heritage assets. This should include disclosure of transfers of heritage assets between Federal entities and those acquired through donation or devise, if material. In addition, the fair value of heritage assets acquired through donation or devise, if known and material, should be disclosed in notes to the basic financial statements in the year received.

d. Entities should report the condition of the heritage assets (which may be reported with the deferred maintenance information) as required supplementary information. Entities should include a reference to the condition and deferred maintenance information if reported elsewhere in the report containing the basic financial statements.

e. Entities should disclose that multi-use heritage assets are recognized and presented with general PP&E in the basic financial statements and that additional information for the multi-use heritage assets is included with the heritage assets information.

Based on the Public Hearing presentations, it appears that most entities concerns are with the reporting requirements (that would be subject to audit) that relate to the unitization and substantiation of reported unit amounts.

Therefore staff determined that another potential phased approach could be based on required disclosures. For instance, the phased approach could be as follows:

For periods beginning after September 30, 2005—disclosure requirements in a, b, d, and e above are required.

For periods beginning after September 30, 2007—disclosure requirements for those required in previous year and disclosure requirement c1 for ending balances is required. NOTE: *Once the ending balances were substantiated in this year, those balances would then become the beginning balances the following year. For years thereafter, all required information, including additions and withdrawals, would be basic information and subject to audit.*

For periods beginning after September 30, 2008—disclosure requirements for all of the above are required.

The above phased-in implementation offers additional time for agencies to address determining the proper level of aggregation for major categories, as well as determining the appropriate physical unit of measure and documenting their reasoning for such. This additional time will also allow for the AAPC to update and issue their Guide in ample time for consideration before implementation. FASAB could request that AAPC finalize the guide by January 2006 or perhaps within one year of the issuance of the proposed standard, which would be over a year and a half prior to the implementation of the required reporting by major categories.

Based on audit assertions

FINANCIAL STATEMENT ASSERTIONS—See **Exhibit 9** for additional detail regarding assertions and evidential matter from AU326.

Assertion	Description
Existence or occurrence	Assets or liabilities exist at a certain date and recorded transactions occurred during a given period.
Completeness	All transactions and accounts that should be included in the financial statements are included.
Rights and obligations	All assets are rights of the entity and all liabilities are obligations at a given date.
Valuation or allocation	All assets, liabilities, equity, revenues, and expenses are shown at the appropriate amounts.
Presentation and disclosure	Financial statement components are properly classified, described, and disclosed.

As staff attempts to formulate a plan based on this, staff finds it a bit difficult to do, as FASAB's role is to determine what information is essential to fair presentation in accordance with GAAP. Staff also recalls that Board members have requested that language specific to audit requirements be taken out of the ED.

However, if the Board wishes, the proposed reporting requirements could be reconsidered in light of the above assertions. Therefore, staff prepared a chart analyzing the proposed reporting requirements against each assertion (see **Exhibit 10)**. The Board may consider that certain reporting requirements may not be necessary when reviewing in conjunction with the audit objectives.

Another potential phased implementation method (which was recommended to FASAB) would be a phase-in of assertions that the auditors would actually test. For example, the first year of implementation of the proposed standard may only require testing for Existence and Presentation and Disclosure. In the following year, the auditor would test for those assertions and Completeness. Meaning, additional time is allowed because it may be more difficult from an audit perspective to assure the completeness of the stewardship land versus the existence. Staff notes that this type of phased implementation would be difficult to provide for in an accounting standard. Instead, this would have to be accomplished from audit guidance and that could only be possible by designating the information as Required Supplementary Information. *AU 558 Required Supplementary Information* provides for the procedures that an auditor must consider when information is required by FASAB (also FASB and GASB). Among other

procedures, it includes "Apply additional procedures, if any, that other statements, interpretations, guides, or statements of position prescribe for specific types of required supplementary information."

Considering this, additional guidance would be developed that states which assertions or tests should be performed and this could be done in a staggered fashion.

Based on entity

Another possible approach would be based on entity. Looking at Stewardship Land—DOI, DOD and USDA administers almost all of the Federal Government's Stewardship Land. However, staff believes that utilizing this sort of phased approach would not be logical as it would make most sense for the agencies with the largest amounts of heritage assets and stewardship land (such as DOI) to be required to implement first. However, it is the agencies with the largest amounts of stewardship land and heritage assets that will face the most difficulty and cost.

Staff Analysis/Comments

Staff believes that the phase-in approach based on the proposed required reporting disclosures would be the best alternative for the Board's consideration. It allows agencies additional time—approximately 4 years-- to address the implementation issues related to determining appropriate categories of assets and units. The additional time will also allow ample time for the AAPC Workgroup to update and finalize its guide.

Questions for the Board

- Does the Board agree with staff recommended approach to a phased implementation—based on a phase-in of required disclosures? If so, does the Board agree with the time frames?
- Do Board members wish to offer other alternatives for a possible staggered implementation approach?

High-level questions for the Board and Staff Recommendations

As noted at the beginning of this paper, it may be appropriate to ensure the Board's position on the current proposal. Meaning, after review of the Binder materials and discussion at the Board meeting, does the Board still want to move forward with the current proposal? More specifically:

- Does the Board agree with the disclosure requirements in the proposed standard?
- Does the Board agree that the heritage asset and stewardship land information should be classified as basic, except condition information, which is RSI?
- Are there Board members that wish to present alternatives for consideration?

Considering the staff analysis and comments throughout this document, the Board has gathered that staff recommends moving forward with the current proposal. However, as also noted in the analysis there are several areas of the proposed standard that will need to be expanded upon

and clarified. In addition, staff foresees a lengthy Basis for Conclusions that will address many of the areas as well.

If the Board is in agreement, the goal will be for staff to provide the revised proposed standard for the Board's discussion at the December 2004 Board Meeting.

If the Board agrees to move forward with the current proposed standard, staff will work towards finalizing the proposed standard by incorporating the following, and any additional changes agreed to by the Board at the meeting:

Areas for revision, additional language and clarification in the proposed standard:

Effective Date/ Phased-In Implementation—The effective date will be revised to reflect a staggered implementation (based on a phase-in of required reporting disclosures that are classified as basic).

For periods beginning after September 30, 2005—disclosure requirements in a, b, d, and e above are required.

For periods beginning after September 30, 2007—disclosure requirements for those required in previous year and disclosure requirement c1 for ending balances is required. NOTE: *Once the ending balances were substantiated in this year, those balances would then become the beginning balances the following year. For years thereafter, all required information, including additions and withdrawals, would be basic information and subject to audit.*

For periods beginning after September 30, 2008—disclosure requirements for all of the above are required.

Statement explaining how HA/SL are important to the mission of entity (Par 28a & 44a)
Expanded to include compliance with laws and regulations because Congress has determined certain classes of assets to be nationally significant regardless of the mission.

Categorization and Unitization—
Additional language added to reiterate that categorization and unitization is determined by the preparer and the preparer should document the reasoning for major class determinations.
Additional language added to clarify that reporting is at the majpr category level, to ensure that readers do not interpret this to mean an item-by-item count.
Additional explanatory language in the Basis for Conclusion that conveys the information included in the Categorization and Unitization section above to explain why the Board is not prescribing categories.

Supporting Documentation
Additional language recognizing that historical records for items acquired long ago may not have been retained and language encouraging preparers, program offices, and auditors to develop other reasonable approaches and methods for satisfying the specific audit assertions that would rely on historical documents as evidence and support.

Additional Guidance
Additional language stating that the AAPC Stewardship Guidance Workgroup will be revitalized and commissioned to update and finalize their Draft Guide by January 2006 or within one year after the issuance of the proposed standard. The Draft Guide could ultimately be issued as a Technical Release or Staff Implementation Guidance. The Draft Guide is an excellent starting point on many of the issues raised. In addition to the areas already addressed in the guide, we could recommend that an area on suggested reporting categories, including different levels of potential aggregations and unit reporting be included. We could also recommend that the guide

discuss specific examples or case studies that involve cases where there is a lack of supporting or historical documentation. The guide could discuss the development of other reasonable approaches and methods for satisfying the specific audit assertions that would rely on historical documents as evidence and support.

Basis for Conclusions

Basis for Conclusions will be drafted accordingly to include explanatory language about all of the above items and the Board's reasoning for making certain revisions and not making other revisions. In addition, it will contain the results of the comment letters and public hearing.

Other issues for consideration:

- Based on the decisions made at the Board meeting and the resulting revisions to the proposed standard, the Board will have to determine if the proposed standard will have to be re-exposed for comment.

- Ensuring that the AAPC Task Force is revitalized and on track for updating and finalizing the Draft Guide by January 2006 or within one year after the issuance of the proposed standard.

Heritage Assets and Stewardship Land, Tab H
Exhibits

Museum Reporting Summary	**Exhibit 1**
President's Federal Real Property Management Initiative	**Exhibit 2**
Executive Order 13327 Federal Real Property Asset Management	**Exhibit 3**
Executive Order 13287 Preserve America	**Exhibit 4**
Advisory Council Guidelines on Implementing Preserve America	**Exhibit 5**
Excerpt from *Becoming Better Stewards of Our Past*	**Exhibit 6**
Excerpt National Historic Preservation Act	**Exhibit 7**
Heritage Asset Categorization Project Report	**Exhibit 8**
AU326 Evidential Matter	**Exhibit 9**
Analysis of Reporting Requirements Against Audit Assertions	**Exhibit 10**