

FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD
December 10-11, 2003
Room 7C13
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Wednesday, December 11, 2003

Administrative Matters

• **Attendance**

The following members were present: Chairman Mosso, Messrs, Calder, Farrell, Patton, Reid, Schumacher, Zavada, and Ms. Cohen. Mr. Anania attended by phone for the following sessions: fiduciary activities and rules of procedures on Wednesday and all sessions on Thursday.

The general counsel, Jeff Jacobson, and the executive director, Wendy Comes, were present.

- **Update on Activities**

Ms. Comes confirmed cancellation of the discussion of the proposed AAPC technical releases 3 and 6.

The Board agreed to plan a public hearing on the exposure draft on earmarked funds, with the understanding that if comment letters did not indicate a need for a hearing, it could be canceled. Mr. Patton noted that if there were only a few comment letters, it might be desirable to solicit presenters for a hearing.

Ms. Comes previewed the new website design for members. The new website will be available the first week of January. She indicated that up to date Volumes I (Original Pronouncements) and II (Current Text) would be posted to the website during January 2004.

Agenda Topics

- **Concepts – Objectives**

Comparative advantage, cost accounting, and related issues

Mr. Bramlett introduced the discussion on objectives. He noted that Board members had been given three background documents:

1. A memo from him dealing with the concepts of comparative advantage and legal mandate. As an introduction to the Board's next topic of discussion, the memo also explained the role of elements of financial statements in FASB's conceptual framework. He suggested that each of these concepts could provide tools to help address what he perceived to be two of the Board's primary objectives for the concepts project:

- A desire to articulate more explicitly the linkage between objectives and standards, thus providing members more guidance in setting standards, and
- A desire to define and delimit more precisely the role of GAAP-basis financial reports in addressing the objectives of federal financial reporting, thus showing how these reports fit in to the larger federal performance and accountability reporting framework.

2. A memo from Ms. Comes dealing with antecedents to the CFO Act and with the dual focus in SFFAC 1 on internal and external users.

3. A memo from Ms. Comes dealing with budgetary integrity.

Mr. Mosso said that he would like to see if the Board could agree on how to proceed regarding the budgetary integrity objective and the operating performance objective.

Mr. Patton said that FASAB is an accounting advisory board, which might have implications for its comparative advantage. He would link to that consideration of the kind of products the Board might produce. We produce financial reporting standards, which leads naturally to thinking of the accountability report, of which the financial statements are a part. He would like to think about whether it would be useful to ask whether we have products to serve the various components of accounting, or whether we have basically one product to serve those objectives. Also, he would consider whether that one product is really an appropriate vehicle for the variety of accounting guidance that an accounting advisory Board might produce. For example, there might be something less than a standard that would provide information or suggested guidance, but would not establish GAAP. He thinks FASAB should not set GAAP for managerial accounting. If FASAB were to deal with managerial accounting at all, it would best be done in some vehicle other than standards.

Mr. Mosso directed attention to pages 21 and 25 of Mr. Bramlett's memo. Page 21 presented the "Information Spectrum" as portrayed by FASB in its 1980 Invitation to Comment (ITC), *Financial Statements and Other Means of Financial Reporting* (a revised version appears in FASB's *Statement of Financial Accounting Concepts No. 5, Recognition and Measurement in Financial Statements of Business Enterprises*, 1984). Page 25 presented figure 1, "How Accounting Contributes to Information Used by Citizens, Congress, Federal Executives, and Program Managers," from FASAB's SFFAC 1. He asked whether Mr. Patton was thinking of something like them. Mr. Patton said that was correct.

Mr. Patton noted that FASB had indicated its area of interest; he asked whether FASAB's area of interest was marked. Mr. Bramlett said that he thought the Board had not been prepared to define its area of interest with great specificity when SFFAC 1 was published. The Board realized that the federal reporting model was still evolving. The CFO Act referred to performance information years before GPRA was passed. The term "accountability report" did not yet exist, much less today's basis for Performance and Accountability reports.

However, the fact that solid arrows in the diagram pointed to the two central boxes, with dotted arrows to the others, was intended to suggest a primary focus on the two central boxes [i.e., general purpose financial information plus one type of special purpose financial information: budget execution reports]. Budgetary reports were included, not to suggest that FASAB would establish budgetary principles or standards, but rather because it was contemplated that information on budget execution would be an essential part of a complete set of the basic financial statements to be prepared and audited pursuant to the CFO Act.

Mr. Mosso suggested that it might be time to reconsider the figure in SFFAC 1 in light of subsequent developments.

Cost Accounting

Mr. Patton asked whether cost accounting would be part of operating efficiency, and whether FASAB should set cost accounting standards. Mr. Mosso said that question could be related to the background material on why the Board was created. Ms. Comes said that the background paper on antecedents to the CFO Act provided an indication of concerns at that time. The paper does not focus exclusively on cost information. She has a hard time imagining where one would draw the line between financial accounting and cost accounting. As far back as ARB 43, accounting standard setters noted that it would be unusual not to assign indirect cost to inventory, but did not specify what methods should be used to do this.

The cost accounting standards that she worked with in the private sector dealt with what costs were allowable charges. She could not envision FASAB delving into that type of issue. On the other hand, she could imagine FASAB discussing what full cost is (as it did in SFFAS 4), and providing some guidance on how it should be displayed, e.g., in the Statement of Net Cost. She is puzzled by how one would draw a line between cost accounting standards and financial accounting standards. Further, she is struck by the structure of the federal government being different than is the case for other entities covered by other GAAP.

The Federal Financial Management Improvement Act (FFMIA) requires the auditor to report on whether the preparer's systems comply with accounting standards at the transaction level. This ratchets up the effect of SFFAS 4 on the preparer. It goes beyond what GAAP would normally require. The paper was not intended to provide the basis for a discussion of questions like (1) the difference between managerial cost accounting and financial reporting standards, and (2) what would be the impact of asserting that we have a different product, or of explicitly excluding cost accounting from the Board's role.

Mr. Calder said the discussion was pertinent because SFFAS 4 is a strange duck. It is part concepts statement, part standard, but the standards and concepts are interwoven. FASAB delved into management with SFFAS 4. People not on the Board recognized a need for cost accounting and there was pressure on the Board to do something about it. The Board reacted with SFFAS 4. In effect, FASAB said, "we will go beyond the traditional standard setters' role, and get into efforts to force management to do things we or others think is good." The discussion is relevant to the question whether we want to pull back from that.

Mr. Patton asked, "Is a GAAP standard from FASAB the best way to improve federal cost accounting?" Mr. Mosso noted that FASAB's standards do call for a Statement of Net Costs. Mr. Calder said a standard might be a convenient way, in the absence of anyone else doing it. He noted that the government-wide and departmental financial statements focus on cost by organizational unit rather than by program. Ms. Comes said that one does see some breakdown by the goals of an organization, with creativity by some preparers to show something more than organizational cost.

Elaborating on Mr. Calder's comment about pressure on FASAB to do something regarding cost, Mr. Bramlett said that, in particular, Vice President Gore's "National Performance Review" directed the Board in 18 months to develop standards that would report the "true cost" of the Government's activities. His concern is that in the governmental arena, where one reports to a wide range of potentially interested parties—including many who are not trained as accountants—there seems to be a common notion that there is such a thing as the "true" cost.

His objective regarding cost accounting would be that FASAB do what it can to assure clear communication about the "right" cost for a given decision rather than the "true" cost.

Mr. Schumacher said it is not quite clear to him where the role of the Board ends and others such as OMB come in regarding cost accounting.

Congressional concerns

In response, Mr. Mosso noted that, in passing the CFO Act, Congress focused primarily on internal users, coupled with concern about assuring the integrity of federal accounting. FASAB was to some extent created to set standards in that context. We set standards for any agency that is required to prepare financial statements, which now includes almost all federal agencies. He does not see a big difference between internal and external reporting, except for cost accounting. Reporting for a given bureau within a department, for example, is for the people who supervise that particular bureau. Reporting for the department is for those who oversee it, including people in OMB and Congress, and so on. There is a layering effect, with FASAB setting standards for every layer. In that sense, it is almost all external reporting.

Mr. Zavada asked whether the emphasis in the legislation was on managerial accounting, or more specifically on systems and control?

Mr. Mosso said that the overarching concern seemed to have been "fraud, waste and abuse," with some references to management as well. The things Mr. Zavada had mentioned could be related to that concern.

Mr. Zavada said he thought the primary emphasis had been on systems and control, and that as a by-product of improved systems and control one would have information for management. Mr. Mosso suggested that was why the Board had included the "systems and control" objective.

Mr. Reid said that action to address the systems and controls objective was now coming; it is very likely that agencies will have external certification on controls. Between the legislation and policies, that is something pretty well addressed. He would therefore rank that objective as a low priority area for the Board to devote energy. He is not a fan of reporting cost of functions, because the answer needs to be tailored to the question. For example, some elements of cost are relevant if one is expanding an

operation, but may not be relevant if it is contracting. Those matters require management's judgment.

Ms. Comes noted that the things Mr. Reid mentioned are addressed in SFFAS 4. Mr. Bramlett suggested that some of the concerns about internal versus external focus and about reporting relevant cost might be resolvable when FASAB gets to the "communication methods" part of its conceptual project. Today's technology makes it possible for preparers to permit users and analysts ready access to customizable databases, rather than predefined, once-a-year reports on paper. He cited an article that envisions a future in which the audited general purpose report "serves as a benchmark, upholds information credibility, maintains information comparability, and satisfies users' common information needs while the added customization meets users' different information and presentation requirements."

Comparative Advantage

At Mr. Mosso's request, Mr. Bramlett introduced the discussion of whether the idea of comparative advantage could be relevant to the Board's concerns. He said "comparative advantage" might refer to different things in this context, such as:

- Attributes of accounting as a practice rooted in the processing of financial transactions, or
- Attributes of financial reporting as a practice mandated by the CFO Act and other laws and conducted in the context of Government Auditing Standards, or even
- Personal attributes of Board members, such as their individual experience, expertise, and perspectives.

For him, comparative advantage seems to include consideration of at least three factors:

- (1) Core data inherent in the financial transaction processing system,
- (2) Mandated periodic public reporting (not necessarily limited to core data) that is potentially independent of the budget, and
- (3) Potential for regular audit.

He thought that the initial FASAB members focused on the role of the financial transaction processing system as the beginning of the kind of financial reporting on which they would focus primary attention.

Mr. Mosso said he thought the three factors were relevant to developing the objectives FASAB will focus on and follow. They may help orient people as to why we have particular standards. Other factors might be considered. He noted that the budgetary accounts are built into the agencies' accounting systems at the transaction level.

Mr. Zavada said the second factor seemed on point. It is even more fundamental than examples that had been cited, such as information on deferred maintenance. It relates to establishing a body of accrual-based information that is available to demonstrate accountability and for decision making.

Implications of Antecedents to the CFO Act and the Dual Internal/external User Focus

Mr. Mosso directed attention to three questions posed on pages 4 and 5 of Ms. Comes' memo on events leading to development of the CFO Act and the question of dual internal/external user focus. She asked whether that was an area the Board wanted to explore further.

Mr. Reid said that the environment had changed, including new laws. We need to look at the objectives in light of the perceived effectiveness of new requirements. Just because a law has been passed does not mean that it is effective. If we perceive those things to be effective to satisfy an element of need, it is appropriate for us to back away. We looked at a history of legislation that has been passed, but we have not done an analysis or assessment of the effectiveness of the legislation.

Ms. Comes said this sounded like a global study of federal financial management. Mr. Reid said he would focus on things that have changed. He thinks the President's Management Agenda (PMA) has been particularly effective, at least in financial management. It raised the bar for agencies from just getting a clean opinion to "what's really going on there." This forced agencies to take a broader financial management view. The Integrity Act has taken on more significance in recent years because there are other things going on like the PMA, so that it is not just an internal assessment of controls. There is a synergy that has improved effectiveness of things like the Integrity Act. That is the kind of analysis that he thinks would be helpful in deciding where we want to place emphasis and priority.

Mr. Mosso said that other things could be related to that. For example, the budget is being transformed to bring in more performance measures and to have appropriations more logically related to programs.

Mr. Reid said the discretionary portion of the budget is so small that it is necessary to manage over multiple years. We have moved to a 10-year focus, with 75-year projections for some things. Some economists don't think 75 years is enough. The budget is taking on a longer view, which reduces the impact of accrual differences in financial statements.

Ms. Comes said pieces of such an assessment of developments are available from GAO, the Mercatus Center, and similar sources such as the PCIE/CFO Council study of an opinion on internal control. Mr. Reid said he was not thinking of a global assessment and that these pieces may be useful to the Board.

Mr. Mosso noted that we currently don't see positive assurance on internal control, as is now required in the private sector. Mr. Schumacher said that the Sarbanes Oxley Act

(SOX) calls for the CEO and CFO to sign off on the controls, and for the external auditor to opine on them. Mr. Reid said that an opinion on internal control would be costly, but assuming we go that way, internal control will be pretty well nailed down.

Mr. Farrell said there have been studies on added cost. He saw speculation when SOX was passed that added cost might be as much as 30% or 40% higher.

Mr. Zavada said it is necessary to look at both sides: the incremental costs and the incremental benefits. Mr. Farrell noted that an opinion on internal controls in general could be much broader than an opinion on controls related to financial reporting. He also noted that existing internal assessments seem to indicate that there are a lot of material weaknesses; adding a requirement for external opinions on control would not make the weaknesses go away. Mr. Reid noted that this was an objective of the PMA. Over time we can make the weakness go away and start mirroring things going on in the private sector.

Budgetary Integrity

Mr. Mosso directed attention to the third background paper related to objectives that had been sent to the Board, Ms. Comes' memo on budgetary integrity. She said it was a response to some members' request to link the federal reporting model more closely to the Budgetary Integrity objective. The memo included an expansion of a matrix Mr. Bramlett prepared for the October meeting and excerpts from GAO report GAO-01-43 Federal Accounting and Reporting: Framework for Assessing the Reliability of Budget Execution Data Is Not Yet Fully Implemented. GAO-01-43 October 6, 2000.

Mr. Reid said that Treasury prepares an annual report of receipts and outlays. It is known simply as the Annual Report. The receipts and outlays are matched against allocations in the budget. The information is available very quickly, and the report stays open indefinitely. The sum of changes to the report are infinitesimal. Whatever goes on with respect to controls over the process, which is the backbone of whether one stays within the budget or not, must be working well.

Mr. Schumacher said the material made the link between the objective and the financial statements clear to him. He thinks the objective is still a very clear objective.

Mr. Mosso asked whether it was safe to assume that budgetary integrity should remain an objective. Mr. Reid said he would like to take it to a different level. In the state and local governmental arena, comparisons between budget and actual are done in two different ways: by program or function and by natural account, such as salary, fringe benefits, rent, travel, etc. He found this very helpful from a management standpoint. Unless one sees how much is being spent on overtime, it is hard to assess adequacy of staffing, for example.

Ms. Cohen agreed that it is hard to control what is not seen. She noted a recent article in the New York Times about the difficulty of controlling overtime in the New York City government.

Mr. Mosso said that nothing currently in FASAB's standards calls for object class information. He asked if object class information was still produced. In response to his question, Mr. Kilpatrick said that object class information is published, not in the program and financing schedule, but in a supplementary table for each expenditure account and a separate publication.

Mr. Reid noted that the standard general ledger drives how information is collected and reported. Systems drive the answer at a program level; at Treasury they don't have any granularity, in the form of disaggregated data, as to the type of expense that was incurred.

Mr. Calder said it was an interesting discussion: that kind of thinking is how we got SFFAS 4, i.e., it reflected the belief that managers should have cost information. He asked whether FASAB should require that kind of information, or should someone at the agencies say they ought to have this kind of information?

Mr. Reid said that the District government uses the same object class system that the federal government does, and that District managers use the information, together with other information. Part of the reason the system was set up to produce information that way is that, in order to pass the annual audit, it is necessary to be able to present the information both ways. The accounting requirement is a plus for managers in state and local government. Based on what he hears from federal managers, he doubts that they all have ready access to such information.

Mr. Zavada said that he thought the information is available within an appropriation; he is not sure how timely it is. It does not appear on the Form 133, but it is available.

In response to a question from Mr. Patton, Mr. Reid explained that the Annual Report (Combined Statement of Receipts, Outlays and Balances) is the "actual" spending side, at the level at which it was appropriated. It is the source of the "actuals" in the President's Budget. Mr. Patton asked whether it showed the source of spending authority and how much was left. He inferred that we could tell whether financing and spending were in accordance with authority from a report that is already available. Recalling Mr. Mosso's question whether it was safe to assume that budgetary integrity should remain an objective, Mr. Patton suggested that this report goes a long way toward achieving that objective, and that perhaps FASAB had no comparative advantage in producing additional rules regarding it.

Mr. Jacobson pointed out that the compliance report mostly addresses the use of the appropriation as to amount, not purpose. Mr. Reid agreed. He explained the process OMB and Treasury follow of apportioning and warranting appropriations. Mr. Patton concluded that providing assurance regarding "purpose" was an aspect of budgetary integrity that might not be addressed by the Annual Report.

Mr. Jacobson mentioned past problems in this regard at the Department of Defense. Mr. Bramlett reminded the Board that in October Mr. Kilpatrick spoke to a related point, when he noted that audits had revealed problems.

Mr. Kilpatrick said that people at OMB had found the audit of the SBR useful in bringing some facts to light despite the fact that the SBR is presented on a very aggregated basis for an agency as a whole. They have also found having the SBR useful in working together with people at Treasury to improve definitions and in other ways.

Mr. Reid noted that there is a group of people who maintain the Standard General Ledger (SGL) and develop related accounting guidance.

CONCLUSION: Mr. Schumacher observed that the notion of financial condition is a forward-looking notion and should not be confused with financial position. Mr. Mosso agreed that this would be a topic of discussion. He concluded that the discussion seemed to indicate little need for major changes to the first two objectives – Budgetary Integrity and Operating Performance. Further analysis of the current environment would be provided, as requested by Mr. Reid. In addition, the Board will discuss the remaining two objectives – Stewardship and Systems and Controls – at future meetings.

- **Concepts - Elements**

Approach

Ms. Wardlow opened the discussion on phase II of the conceptual framework project by describing her memo, which had been provided to the Board. This memo contained two main sections. The first section described the approach taken by the FASB and other standard setters to defining assets and liabilities. She asked whether the FASAB would tentatively adopt that approach, without prejudice to potential future modifications, if the need for them becomes apparent upon further discussion. She explained that by “approach” she meant both:

(a) The notion that assets, liabilities, and other elements of the financial statements should be defined based on their essential characteristics—i.e., those features that are so fundamental that an item lacking those features could not be considered to meet the definition, and

(b) The notion of the conceptual “primacy of assets,” to use the FASB’s term—i.e., the idea that elements of financial statements other than assets should be defined in relation to assets. For example, the element “liability” may be defined in terms of an obligation to pay or transfer assets to someone else or to consume something of value to provide service to them. This does not mean that information about assets the Government holds is considered more important than information about the Government’s liabilities and other commitments, nor does it mean that the Balance Sheet is considered more important to users than the Statement of Net Cost.

The second section of the memo discussed the three essential characteristics that the FASB and some other bodies believe that all assets have, and the belief that there are no other characteristics that all assets share. Questions for the Board would include:

1. Does the Board believe that the three essential characteristics defined by the FASB also are essential characteristics of federal government assets?
2. Do federal government assets have any essential characteristics that are not present in private for-profit or not-for-profit assets?

She explained that part of the approach was the distinction between definition and recognition; i.e., the idea that an item might meet the definition of an element, yet not be recognized for some reason (e.g., because it is not reliably measurable).

Mr. Patton agreed that elements should be defined in terms of essential characteristics. The APB approach seemed circular.

Mr. Reid agreed, but expressed concern about the notion of “primacy of assets.” Governments may be more defined by the commitments they make than by the assets they hold. Another party does not necessarily recognize those commitments as assets. There are many commitments not currently quantified on the balance sheet.

Mr. Schumacher asked whether that was not just a timing difference? To him, it is just a frame of reference to define the other elements, a building block, not an assertion about what is most important. Ms. Cohen observed that one could say that a government’s primary asset is its power to tax and to confiscate resources.

Mr. Mosso suggested that the “conceptual primacy of assets” was not so much a concept as recognition of the fact that one can’t define a liability or revenue without reference to an asset. There is no implication that information about the asset is more important. Historically the idea was discussed because FASB was trying to change the APB approach that defined assets as a residual debit on the balance sheet: “whatever we say is an asset is an asset.” It was an issue in the context of the debate between the “revenue/expense” view of accounting and the “asset/liability” perspective. We probably don’t even need to debate it today. He agrees that in setting standards we often start with the liability side.

Mr. Patton said that there is a possibility we might define new elements of financial reporting, e.g., “commitments.” He asked whether we could define “commitment” by starting with assets. Ms. Wardlow said that she thought one could: as with a liability, one would be making a commitment to transfer an asset, or to use up a service potential in providing a service, etc. Without wanting to look too far ahead, other factors might distinguish a commitment from a liability, such as the event that created it and whether some other event would need to take place, etc.

Mr. Bramlett asked whether elements reported on the Statement of Budgetary Resources could be defined in terms of assets? Ms. Wardlow suggested that from an agency’s perspective, an appropriation could be seen as an asset, but FASB’s definition

of an asset would need to be modified. Mr. Reid asked whether it might be possible to turn it around and define it in terms of a commitment to do something. Mr. Mosso noted that two of the three characteristics of an asset listed by FASB relate to a particular entity.

Essential Characteristics

Mr. Mosso directed discussion to “essential characteristics.” Ms. Wardlow reviewed FASB’s conclusions, including the idea that “asset” is better defined in terms of ability to receive or control benefits rather than in terms of legal ownership. She noted that the idea of “control” had been an issue for some standards setters. It implies that the entity has access and/or the ability to control others’ access.

Ms. Wardlow observed that for governments and not-for-profit entities, not all assets contribute to future net cash inflows. Mr. Patton said he particularly liked the notion that an asset helps to achieve an entity’s mission. Accountability is such a big issue and part of the mission in government that we might be able to use it to justify including fiduciary resources.

Mr. Calder said that the federal Government is unique in its ability to take or control assets, and in its ability to abrogate commitments. He also observed that one could have different forms of ownership and rights to different, severable benefits from assets. For example, if I own a building I can use the building and take its benefits through use, or I can lease the building. Someone else then has “ownership” of the right to use the building (and thus an asset), but not the right to sell the building, which I retain.

Mr. Patton asked, “what about ownership of fiduciary resources?” Mr. Calder said, “That is a question, who owns the assets? If we own the assets, what is the fiduciary duty? I say they are not our assets.” Mr. Reid said, “If you conclude that we have custody but we don’t own them, then they should not be recorded, contrary to our draft.” Mr. Mosso asked, “How would you account for a trustee in a separate free standing trust operation?” Mr. Calder said, “if I own the assets, but have an agreement to provide resources back, I have a liability; if I don’t own them but am holding them, I am accountable for them, but they are not mine.” Mr. Zavada asked, “Doesn’t the fact that they are held in a fiduciary capacity mean that the assets are their assets [not the trustee’s]?” Mr. Mosso suggested they own a claim on the trustee. Mr. Calder said that fungibility of assets, as with money, adds a complication.

Ms. Wardlow observed that similar issues came up in accounting for state and local governments (SLG). For example, some pension plans are trusts for multiple employers’ plans. Some have questioned which assets “belong” to each individual employer’s plan. However, the trust assets are fungible and not associated with any particular individual plan; rather, each employer’s individual plan owns a share of the trust’s total assets. In SLG accounting, neither the trust assets nor the assets of individual employers’ plans are considered or reported as assets of the employer entity.

Mr. Mosso noted that the Board would discuss fiduciary activities in more detail after lunch. Clearly, he said, the ideas of ownership or control needs to be dealt with in the explanation of essential characteristics.

Mr. Patton asked whether ownership would mean there would be no intangible assets? Mr. Calder said no, we need a way to recognize intangibles. Mr. Patton asked, "Would research and development R&D be a possible asset not eligible for recognition?"

Mr. Calder mentioned a situation for consideration: the Corp of Engineers builds dams on someone else's river. Ms. Wardlow noted that similar situations arise for states. One can make a case that what matters is not the legal title but the right to the benefits that flow from the use of the asset. FASB was concerned about legal enforceability, which is normally part of ownership. That may not be what we mean here.

Mr. Mosso said that Mr. Patton's point about R&D would be an issue. FASB concluded that R&D can meet the definition of an asset, but it is not recognized because the relationship to future cash flows is too tenuous. Mr. Bramlett noted an entity/control difference: in the private sector context R&D involves expenditures intended to enhance future benefits accruing to the reporting entity. In the federal context, R&D typically involves expenditures intended to benefit the society at large.

Ms. Wardlow said that this relates to the community asset idea, where the flow of the benefit need not be exclusively for the benefit of the entity. As she discussed in her memo, FASB acknowledges that the problem of "noncontrolled benefits" arises in the not-for-profit and governmental sector.

Mr. Mosso noted that under FASB's standards, assets for not-for-profits need not directly be related to future cash inflows. There may well be unique aspects regarding R&D for the federal government as compared with the private sector and even with state and local government.

Mr. Patton asked whether we could discuss probability. Ms. Wardlow agreed that it would need to be dealt with, in connection with "characteristics" as well as with "recognition" and "measurement" issues. As her memo explained, FASB included a footnote about the word "probable" in the asset definition, suggesting some concern about how the word might be interpreted, and distinguishing its use in defining an asset from its use in FASB's Statement No. 5 [defining which contingent liabilities should be recognized].

Some other standard setting boards have not included "probable" in their definitions of "asset," perhaps because of how they worded the definition. For example, the word "potential" in the phrase "service potential" may convey the notion of probability, so definitions that include that phrase may contain the idea of probability without using the word. Coupled with that, concerns have been raised about what probability means and how to measure it in a definitional sense compared with measurement in the context of recognition.

When asked about his views, Mr. Patton quoted from Ms. Wardlow's memo:

[FASB's] explanation suggests that the FASB believes that uncertainty about an asset's existence (i.e., whether future benefits exist) is something different from uncertainty about the value (or other measure) to be used to report the asset in the financial statements.

He thinks there is an existence probability issue that needs to be incorporated into the definition. If we don't, there will be inferences made about how probable existence needs to be, so we might as well face up to it, even if we substitute "rights." We have discussed before whether "rights" implies 100% certainty or something else. The idea [of probability] is lurking there, so not to bring it into the actual definition is to invite trouble.

Ms. Wardlow asked, "whether one uses the word or not, are you comfortable with the notion that you don't have to be fully certain in order to say 'yes, I have an asset'." You don't always know. Hopefully you have enough evidence to convince yourself that it is your asset before you determine whether you can measure it for whatever you are measuring in the financial statement.

Alternatively, do you want to be stricter about a barrier between whether you have an asset or do not? FASB tried to leave it as an evidential thing, an everyday, person-in-the-street notion. FASB ran into some problems with that, probably because probability is a statistical notion that is used in accounting standards in a more specific way. If the basic notion is acceptable that you don't need to be 100% certain that something is an asset, then we can talk about whether to use the word probable or get the idea across in some other way.

Mr. Mosso asked whether members knew of any assets unique to the federal government that should be dealt with? There being no response, he asked whether there were any characteristics of assets unique to federal assets?

Mr. Jacobson said that when the CFO Act was debated there was much discussion in Congress about whether human capital was an asset. Mr. Mosso noted that the concept had two facets, one in context of the Government's own activities, and the other in the broad context of promoting the general welfare. SFFAS 8 refers to human capital in the second sense as "stewardship investments." Mr. Bramlett observed that the earlier discussions Mr. Jacobson mentioned were focused specifically on the second, broader meaning. "Like education programs," Mr. Jacobson added. He explained that some members of Congress were concerned that potential bias in budgeting that might arise if accounting standards implied that expenditures on tangibles like weapons systems produced assets but expenditures on intangibles like education did not produce assets.

Ms. Wardlow said that other boards have debated the first or narrower question of whether an employer has an asset in its workforce. Probably most people will say yes, but it can't be measured. Also, what is the transaction: is it hiring the employee, completion of training, or something else? Does it meet the three essential characteristics listed by FASB?

She referred to the earlier discussion about the Government's ultimate asset being the power to tax. It falls down on measurability, but when you separate definition and measurement, it might be regarded as an asset. However, it is also necessary to consider the third essential characteristic, the transaction or event. It may be necessary to consider whether the private sector's definition needs to be modified in order to get a definition that is useful.

Mr. Patton asked whether human capital fits the control criterion. Ms. Wardlow said that is an issue. Employers do limit or regulate others' access to that benefit, so it might meet the definition, but the transaction would also need to be considered.

Mr. Farrell asked whether Mr. Calder was proposing that the word "ownership" be included as an essential characteristic in the definition of asset. Mr. Calder indicated that he was suggesting that some form of ownership, or some word or words that would convey a similar meaning, be included. "Or ownership of some aspect," Mr. Reid said. Mr. Calder agreed.

Mr. Calder noted that the FASB used the term "economic benefits." To some the phrase implies a monetary inflow, and would seem too limiting. Mr. Bramlett recalled that Mr. Holtz-Eakin had said that economists use the term more broadly, but he also had said that he would not object if the Board wanted to use a different term to assure clear communication with others.

Ms. Wardlow noted that the Board would need to explain whatever words it uses. Some other boards, including GASB, have also had problems with that term. Referring to her memo, she explained that for some time GASB had used the following working definition of asset:

Assets are rights to service potential (economic benefits) controlled by an entity as a result of past transactions or other events.

GASB staff had regarded the terms "service potential" and "economic benefits" as synonymous. Later, a Board member objected to the terms "service potential" and "economic benefits" because that member perceived them to be "jargon." The working definition therefore was modified, shortly before GASB suspended work on its elements project. The revised working definition was:

Assets are an entity's rights to goods, services, or cash flows as a result of past transactions or other events.

Mr. Patton recalled that Mr. Anania was eager to include "service potential." Ms. Wardlow explained that some people at GASB understood "service potential" to be related only to capital assets, which was a narrower meaning than had been intended. Different people have different ideas about what terms mean.

Mr. Mosso noted the difficulty that arises from using common words. The word "probable" still gives FASB problems, and FASB defines "reliable" in a way different than some people commonly use it. Using common words with special meanings may

sometimes be unavoidable, but it is difficult to get words that will be universally understood in the way one intends.

CONCLUSION: Mr. Mosso asked what Ms. Wardlow proposed to do next. Ms. Wardlow said that we might explore the concepts of ownership and control, and how they fit the federal environment. Then we might consider further whether federal government assets have any fundamental characteristics other than the three characteristics identified by FASB as fundamental to all business and not-for-profit assets. Ms. Wardlow indicated that she would prefer to obtain the Board's agreement on what the essential characteristics of federal government assets are before attempting to deliberate possible definitions of asset. This is because, in her view, those definitions should be more succinct expressions of the essential characteristics identified by the Board.

- **Fiduciary Activities**

The Board discussed staff recommendations on the issues developed from respondents' comments and from the public hearing.

Issue A. Should non-Federal assets be reported on Federal balance sheets? and

Issue B. Does the phrase "held in the name of" need clarification?

The staff explained that a respondent had objected to reporting non-federal assets on a federal balance sheet and staff asked the Board whether in light of the elements discussion earlier in the day the Board preferred to table the issue temporarily. Mr. Mosso responded that the Board should discuss the issue.

Mr. Mosso noted that certain additional comments had been received from the Interior Department on December 8th that staff had not had time to analyze. An analysis would be provided but until then discussion of the Indian trust fund issue would have to be postponed.

Mr. Reid indicated that it would be helpful to him to understand how the fiduciary funds actually flow through the Government and how much of the Indian funds are within the Government itself at any point in time versus how much is out in a more traditional trust account. He said he could envision some similarities between what goes on at a bank. Clearly the trust department uses the accounts of the bank to do business in terms of making deposits and transfers to other places etc. without tainting the trust relationship. They use the demand deposits and facilities of the bank for a small period of time for the funds on their way in or on their way out. He wanted to find out how close does the trust situation at Interior mimic that kind of a situation where the funds come through Treasury and then go out to Bankers' Trust or wherever they are invested and in some cases they may be invested within the Government in Government securities. He wanted to get a sense of the order of magnitude of the holdings, to know, for example, how much of the Indian trust funds were invested in Government securities versus other means of investment. He

wanted a sense of how commingled this is, or are the funds held by the Government briefly as deposits in transit to other accounts. He said the substance of the Government's role may make a difference in the accounting treatment: transit accounts may be best left off the balance sheet while commingled funds would be different.

Mr. Jacobson noted that the tribal and individual funds flow through the Government in multiple ways. They can go straight to the Treasury, or to the Federal Reserve, or a depository bank because some of these monies are collected in the field where they do not have a Federal Reserve Bank near by and it's local bank will be designated a depository institution and Federal monies can be deposited there. BIA then does the paper work to credit the account of the intended beneficiaries.

Mr. Reid agreed and noted that, after the monies are deposited, there are several options. In some cases it goes to the beneficiary directly and in other cases it is invested. He said with respect to the individual Indian monies that the bulk of it is invested in a trust account with the Bankers' Trust in New York. He didn't know how long it was held in Treasury accounts and what accounting goes on there. He noted that in some cases Interior gets a receipt for money to be credited to many accounts, e.g., an oil royalty payment might need to be divided among a hundred individuals that participate in that particular allocation. He said there are some standing provisions for the Indians to direct the Government to either keep the money and invest it or send it to the tribe or individual Indian.

The staff will provide more detail on the flow of these funds.

The staff asked the Board whether it had changed its position with respect to the principle of reporting non-federal assets on federal balance sheets, even if labeled "non-entity". Mr. Mosso said the question involved the issue of consolidated reporting rather than the asset element per se. He said no one was questioning the existence of an asset. A Federal trust entity would hold assets and be liable for certain obligations. The question would be whether to consolidate those assets and liabilities on the federal entity's general purpose balance sheet. He noted that in the past the FASAB had required certain non-Federal assets and liabilities to be so consolidated and labeled as "non-entity assets", e.g., seized assets. He said that preparing a consolidated balance sheet containing both federal and non-federal assets would not present definitional issues.

Mr. Reid said that one of the primary reasons that the Board undertook the trust accounting project was to clear up the confusion about Government "trust funds", and one of the things about the proposed treatment that concerns him is that we have a situation where, if this were a bank in the private sector, the accounting would clearly be done differently. He was concerned that, after having clarified the accounting for dedicated collections, the proposed treatment of fiduciary activity would introduce confusion on the fiduciary side.

The Board discussed the nature of the Government's relationship to the Indian funds. Mr. Mosso said that more information was needed about how the Indian monies were held in order to assess the correlation with the Thrift Savings Plan. In the latter case, the TSP authorizes certain investment companies – banks and others -- to manage the beneficiaries' funds, and then the individual employee puts the money with that managing fund and the TSP administrative entity is finished with it at that point, although there may be some incidental TSP administrative accounts. He said he did not know if that were true in the Indians' case. If the Indians were merely telling Interior to do this or do that, then he said the analogy was to a bank deposit.

Mr. Reid suggested that the Board not get out in front of the litigation regarding the Indian trust funds since the court will rule on factual situations, including the extent of legal relationship. Mr. Mosso indicated that he did not understand what the accounting has to do with the litigation issues – we're operating on principle. Mr. Reid said that apparently there is an issue regarding the use of individual Indian monies for the benefit of the Government with the plaintiffs asserting that the monies should have been treated more like a separate trust operation. The Government is saying it does and has treated it as a separate trust operation. The court will be examining the facts of the case to make a determination. It will be a factual determination. Mr. Reid did not want the FASAB to be in a position to force that determination on the court. Mr. Mosso said the accounting would be based on principle. Mr. Reid said he was impressed by the notion that the Indians can withdraw their funds because that is a characteristic of control; and if the Indians do control the funds then information would be disclosed in the notes. Mr. Zavada opined that the Indian trust funds situation is like the TSP situation.

The Board discussed the nature of the assets held by the Library of Congress. Mr. Calder said the example of the Library raises an issue. The Library's balance sheet (page 26 in Tab C) shows \$1.1 billion in assets but the Library doesn't own them all. He said the notion of "non-entity assets" was an anomaly to him.

Mr. Reid noted that the Library's fiduciary copyright fees are invested in "market-based Treasury notes and bills," which are securities the Government issues to itself which earn a calculated interest rate (an average of certain Treasury securities with maturities of more than four years). Treasury creates them each July 1st. In effect you've got a security that's not available to the general public. If this were off the Government's books and out with a private investment company or trust at a bank, such securities could not be purchased. The law setting up the fiduciary activity allows the Library and other Federal entities to make such investments. If the fiduciary activity were off the balance sheet and disclosed in a note, then you have the issue of what they can invest in as a "non-Federal entity". You might run afoul of the law that created the relationship. Mr. Reid said that this was an issue with respect to eliminations because if someone outside the Government owns these securities, then they would be "debt held by the public" and probably shouldn't be

eliminated. Mr. Calder opined that they are debt held by the public. Mr. Reid said that that was how they are currently handled in the CFR; they're not eliminated.

Mr. Phaup asked whether the non-marketable market-based securities are subject to market fluctuations in price. Mr. Reid said they were, when they mature. There are different maturities to them and a new price is calculated every year. Mr. Phaup asked what the Library of Congress owed with respect to the copyright holders "custodial liability" [\$658 million per the balance sheet on p. 26 of Tab C]. He asked whether they owed them whatever rate of return has been earned on these market-based securities or do they owe them some fixed amount independent of that. He said that would matter for Mr. Holtz-Eakin's argument because ownership entitles you to, in his view, all – but only – the return on those assets and also any loss thereon. He said that, since these securities fluctuate in price, it would be helpful to know whether the liability fluctuates in lockstep with the value of the assets, as it does in trust accounts for example. Mr. Reid said there was no market risk with these securities, no risk of loss of principal. They are all bought and sold at par. There are some securities that have provisions that allow them to fluctuate but, for the most part, if they want to redeem them the Federal entities get par value plus whatever accrued interest is due. There is no premium or discount on them.

Mr. Anania (speakerphone) suggested that the Board defer a decision with respect to Interior's concerns since there is not enough information. He also suggested that the term "non-Federal assets" not be used since non-Federal assets by definition should not be on the balance sheet. Instead he suggested using the term "assets held as a fiduciary."

Mr. Anania concluded by saying that the definition of "asset" has a bearing on all of this. He said the fiduciary activities project is one that emphasizes the difficulty of reaching a conclusion on individual projects with the Board still unsettled on the asset definition. The notion of benefits and to whom the benefits flow and the notion of control and other notions all seem important in the fiduciary activity discussion. He noted Mr. Mosso's memo in the briefing material that discussed the notion that benefits could be as broad as the benefit the Federal entity could get in meeting performance requirements. He hadn't thought about benefits as broadly as that before. He said that, in the private sector, benefits accrue to the entity and shareholders. In the Government there are benefits to an agency, which ultimately become benefits to the citizens. But he hadn't thought about benefits being as broad and intangible as helping the Federal entity meet its goals and objectives. He suggested the possibility of seeing if there was agreement on that point because it may qualify some things as being assets that he hadn't thought about, even though they may not meet the recognition and measurement criteria.

Mr. Anania said he agreed with the staff conclusion that the accounting for fiduciary activity by private sector entities is a mixture of approaches and not based on settled conceptual principles. He suggested that worrying about what is done in bank trust departments might not be the best use of the Board's time. He didn't think this was a parallel situation or that the bank trust accounting concepts arose out of any deep

conceptual discussions. He suggested spending less time trying to find parallel tracks that might match up with something else and look at this conceptually with the facts at hand. That might result in answer that is like TSP or maybe not but it should be based on the facts and circumstances that the Board sees and not be bound by what has been done before.

The Board did not object to staff recommendations with respect to Issues C-G. The Board discussed the following issues individually:

Issue C.1 Should the standard provide guidance on the Foreign Military Sales program?

The staff concluded that in substance foreign military sales activity represented fiduciary activity. Both Mr. Reid and Mr. Farrell suggested that the standard should include language that requires the substance of the transaction be determinative – not the form.

Issue C.2 Should the standard provide guidance on the U.S Corps of Engineers (USACE) and Civil Works Construction in Progress (CIP) program?

This was determined to be something other than a fiduciary accounting issue and the basis for conclusions will reflect this determination.

Issue C.3 Are seized Iraqi assets “fiduciary assets”?

The Board agreed with the staff recommendation that SFFAS 3 was applicable.

Issue E.3 Should Treasury securities be eliminated for the CFR?

The Governmentwide consolidated financial statements should not “double count” assets and liabilities. The Board tentatively decided that Treasury securities in fiduciary accounts should be eliminated against debt held by the public. A liability for fiduciary activity and any related asset would be presented on the balance sheet.

• **Rules of Procedure**

Ms. Comes indicated that the rules had been revised since the last meeting. She requested member comments on the revisions. Members raised and resolved the following issues:

- Page 5, lines 15 to 17 – Provides that the Chairperson confer with the Board prior to issuing individual Discussion Memoranda and Research Reports. However, line 31 contradicts this by saying “if the Board elected to issue a preliminary document.” This suggests an affirmative action by the Board. The Board agreed that the sentence beginning at line 31 should read: “For any preliminary documents soliciting comments (e.g., discussion memorandum,

invitation to comment, or preliminary views), the Board members receive all comments as well as a staff summary.”

- Page 7, Eligibility to vote - Mr. Anania is concerned that a new member – who had not been privy to deliberations on an issue - could still vote on the issue. He is concerned that individuals may not have all the necessary information to support voting. In addition, he found the phrasing confusing. The Board agreed that the section could be clarified. Mr. Anania remains concerned about permitting new members to vote. However, the Board consensus was to allow new members to exercise judgment in this area.

- Mr. Calder asked that the rules be consistent throughout regarding “majority” votes. For example, he found:

- Page 2, line 34 – “General consensus”

- Page 7, line 13 – “A majority of members serving”

- Page 20, Technical Bulletins and Technical Releases “A majority of members”

Ms. Comes indicated that she would conform the terminology or clarify the intent based on governing documents such as the Memorandum of Understanding.

- Page 15, line 17 – Mr. Patton requested and the Board concurred that the statement “A majority of the Board may request a meeting” should be changed to “A meeting will be called if a majority of the Board requests a meeting.”

- Page 30, section 16 -- Mr. Patton inquired about the desirability of having the Chairperson seek input from the sponsors regarding a recusal. Mr. Jacobson advised removing the provisions since it is ambiguous and unnecessary. The Board concurred.

CONCLUSION: Ms. Comes noted that the AICPA Rule 203 review is not complete. If the review results in proposed changes to the rules, the Board would review those changes at its March meeting. If no other changes are proposed, Ms. Comes anticipates providing the rules -- with the changes identified at this meeting -- to members in early February for approval before submission to the sponsors for final clearance.

- **Steering Committee Meeting**

The committee received an update on FASAB’s recruitment efforts. With respect to the entry-level vacancy, the committee members expressed concern that an internship program may be administratively burdensome relative to the contributions by interns. The committee preferred that Ms. Comes pursue a full-time staff member to fill the entry-level position but remained open to the internship if positive results were attained quickly.

Ms. Comes advised the committee that the Accounting Research Association had named a new member to the Appointments Panel. Mr. Harold Monk replaces Nita Clyde on the Panel. In addition, a meeting of the panel will be scheduled for February. In the meantime, the registry will be updated. When the panel convenes, the registry will be available and the panel will be asked for recommendations on the reappointment of Messrs. Mosso, Farrell and Patton for an additional term following the end of their current terms on June 30, 2004.

Adjournment

The meeting adjourned at 3:45 PM.

Thursday, December 11, 2003

Agenda Topics

- **Veterans Affairs Health Benefits Issue**

Mr. Mosso noted that the briefing materials included issue papers from the General Accounting Office (GAO) and the Veterans Affairs (VA). Ms. Comes explained that this issue was raised in Mr. Calder's October 8th memorandum requesting Board action. She reminded the Board that this issue earlier led the Board to revise the preamble to the Basis for Conclusions (BfC) to clarify that the BfC could not override a standard. She requested Board comment on the proposal from GAO that the Board consider whether a liability should be recognized for veterans' health care benefits.

Mr. Reid notes that SFFAS 5's BfC is very clear. He read for the Board the material related to VA Health Care Benefits:

184. The Board believes that VA medical benefits, for both mandatory and discretionary programs, are best measured by the annual cost incurred rather than by actuarially determined charges during the veteran's military service. Medical care for veterans does not satisfy the probability or reasonably measurable criteria in this standard at earlier dates, and therefore future medical benefits do not constitute a long-term liability to be recognized in the Balance Sheet. The Board believes VA medical benefit liability and related expenses should be recognized in the period medical care service is rendered. The entity should consider, however, what disclosures would be appropriate for these costs under the contingency standard.

Mr. Reid opined that it would be difficult for a preparer or auditor to ignore this unambiguous Board conclusion. Thus, he believes Board consideration is warranted. Further, he noted that there are also serious measurement issues. The benefits available in any year are based on funding for that year. VA determines benefits annually.

Mr. Mosso indicated that the BfC is not authoritative and we don't know what the prior Board had in mind. However, the issue of measurement may be the critical issue to take up.

Mr. Schumacher asked what was meant by the assertion in GAO's position paper that OMB, Treasury and VA officials believe recognition of a liability would be controversial. Mr. Zavada indicated that it was likely the nature and composition of the benefits. Some veterans receive benefits due to service-connected disability while other veterans receive discretionary benefits based on their financial need and available funding. He indicated that VA had recently cut back on care for some groups.

Mr. Farrell agreed that this is a complex issue. However, he indicated there were other programs that are contingent on funding but where we recognize a liability. Mr. Mosso indicated that funding should not affect liability recognition.

Mr. Zavada indicated there is no guarantee from year to year regarding the level of care provided. However, he agreed there was some core group that would receive care on a continuing basis.

Mr. Patton opined that this issue is central to our work on elements. He expressed reluctance to rush to a solution. However, it seems that putting this project on a parallel track with our broad liability project is a sensible approach.

Mr. Calder indicated GAO believes a liability should be accrued for some amount. GAO believes there is a reasonably firm commitment in some cases despite the discretionary nature of the program. It is a prime example of the need for a definition of liability. It may be a good case study for the liability project.

Ms. Cohen asked about changes to the VA program since SFFAS 5 was issued.

Mr. Campbell, Chief Financial Officer (CFO) at Veterans Affairs, and Mr. Ed Murray, Acting Deputy CFO, joined the Board for its discussion and responded to Ms. Cohen's question.

Mr. Campbell explained that at the time SFFAS 5 became effective, VA was providing medical care only to those veterans with service-connected disabilities. The Enrollment Act directed the Secretary to annually determine how many veterans would be treated. This year, the Secretary determined that VA had to stop treatment of certain categories of veterans. [A system of categories numbered one through eight is used to prioritize access to care.] No new enrollees in category eight are permitted this year. Mr. Campbell believes it is possible that some category eight enrollees may be disenrolled in coming years.

Therefore, Mr. Campbell does not believe that a meaningful measurement of any liability under the program is possible.

Mr. Mosso asked what "enrollment" entails.

Mr. Murray explained that each year the Secretary reviews funding and decides who can be enrolled in a given year. Enrollment is necessary before care can be provided. Veterans remain enrolled unless a decision is made to remove from the rolls veterans in certain categories.

Mr. Campbell noted that the projections by VA actuaries have not been very accurate due to the many factors that influence use of Veterans health care.

Mr. Reid asked what VA would have to do to obtain a reliable estimate.

Mr. Campbell indicated that at least a year's work by the actuaries would be needed to develop projections. The cost may be as much as \$2 million . Another 6-9 months would be needed to work with the auditors. However, he is doubtful that the auditors would find the actuarial results sufficiently reliable. The population changes dramatically. For example, companies doing away with health benefits would influence the population of veterans seeking care because as veterans lose coverage from employer sponsored programs they seek care from VA.

Mr. Farrell asked how VA determines how much to ask for in each year's budget submission. Mr. Campbell indicates that VA puts together the best budget it can but that the budget process is not a rational process of assessing requirements --- it is a political process.

Mr. Mosso asked how VA health care differs from DoD health care.

Mr. Campbell indicated that some veterans have served only a little time and do not have a service-connected disability. Military retirees have a contract providing lifetime health care as part of the exchange for 20 or more years of good and faithful service.

Mr. Patton asked about the issue VA raised regarding assigning the liability to DoD since they are the employing entity.

Mr. Campbell notes that this liability is incurred because of the enlistment of soldiers, sailors, airmen and marines. The cost of this is appropriately recognized by the entity receiving their services. The main point is the government recognizing the liability. A secondary point is that the cost should be associated with the Department of Defense so that full cost is captured by the employing entity.

Mr. Patton indicated that the liability should be transferred to the entity responsible for settling the liability in the end.

Mr. Campbell suggested that the Board create a general construct for liabilities. The Board should answer the question of "how does the government incur a liability?"

Mr. Mosso indicated that we have three alternatives regarding this issue. He polled members on their preferred alternative. All members agreed that the issue would be taken up with a broad project on liabilities; the liabilities project is integrated with the concepts project.

Mr. Anania asked whether the VA would make disclosure of the contingency. He asked if there was a role for FASAB with respect to disclosure on an interim basis? Mr. Calder referred to the disclosure presented on page 1 of the briefing materials. This disclosure was included in the FY 2003 report and shows good progress on the issue. He did not see a need for FASAB to address the disclosure issue on an interim basis.

Mr. Campbell asked that the Board provide a period for implementation if a liability is to be recognized due to the cost and time involved in determining a liability.

Mr. Mosso indicated that the effort would go through our normal due process and include consideration of an appropriate effective date.

CONCLUSION: The Board will consider the issue of liability recognition for Veterans Health Care Benefits as one component of a broader project on liabilities.

- **Social Insurance Assumptions**

Ms. Comes explained this issue was raised in Mr. Calder's October 8th memorandum. However, the issue was identified through the efforts of the AICPA task force. Mr. Calder indicated that the issue relates to adequacy of disclosure. The task force has indicated that the assumptions are a necessity for complete disclosure – complete understanding by the reader. He explains that our standards recognize the importance of this information but the standards are ambiguous. Auditors working on the audit guidance believe the information must be disclosed. They would like FASAB to clarify that assumptions are a required disclosure.

Mr. Reid indicated that the standard is clear that the assumptions must be included in the required information. He is concerned that the auditors would focus on the accuracy of each assumption and assess materiality relative to individual assumptions. For example, that the appropriate interest rate is 6.2% versus 6.1% would be an issue. He believes materiality would be applied directly to the assumption rather than as it impacts the total net present values. He does not believe it would be value added to audit individual assumptions. He believes the assumptions are relevant as they relate to the amounts presented in the statement but that the accuracy of the forecast of an individual assumption is irrelevant apart from its impact on the amounts shown on the statement.

Mr. Mosso indicated that you are auditing the statements and the assumptions that back it up. Mr. Farrell indicated that – in concluding on SFFAS 25 - we looked at the current notes associated with the statement and found them to be voluminous. He recalled reviewing the notes and concluding the statements and assumptions were required disclosure. The Board determined that the rest of the required information should be Required Supplementary Information (RSI).

Mr. Calder noted that right now – if the preparer does not want to put RSI in the report – there is a small price to pay. If the preparer omits RSI, the auditor simply notes its absence.

Mr. Farrell explained that the auditor has indicated that absent the assumptions there would be a qualification. Mr. Farrell asserted that there is an assumption that the notes must be appropriate to the circumstances. There is not a standard for every situation.

Mr. Patton indicated that he believes SFFAS 25 says assumptions are RSI.

Mr. Schumacher asked if this proposal would change the level of the audit scrutiny of the assumptions. Mr. Calder indicated that it did not change the audit scrutiny. Thus, the issue is one of geography.

Mr. Reid argued that the issue goes beyond that. If you present a list of items in a note – particularly if they are percentages or something other than dollars – then the auditor must make a determination with respect to each one of those items. As SFFAS 25 is currently written, the assumptions are assessed only as they relate to the statement. If the assumptions are RSI, then they are evaluated only as they relate to or impact the statement. If the individual pieces are disclosed, then each individual piece has more importance. You are not saying how the assumptions impact the statement. Thus any one of the assumptions can be challenged as a stand-alone item.

Mr. Patton recalled that putting the additional information in as RSI was intended to give the auditors a break with respect to the amount of work done on other information. He was surprised the auditors are now arguing the opposite.

Mr. Mosso recalls thinking only of the numerical disclosures. He expressed surprise at the question because he believes the assumptions are an integral part of the statement. He considers it an oversight.

Mr. Reid suggested that if you were computing a pension liability then all the supporting assumptions would be presented in the notes.

Mr. Farrell recalled that we were simply trying to accomplish not putting 17 pages in the notes. It's nice information but not necessary to fair presentation.

Mr. Calder asked how clarity could be provided by the Board on this issue.

Ms. Comes indicated that the decision to use an amendment or an interpretation was up to the Board but she believes an interpretation would be appropriate. This was based on her recollection that the Board focused on a list of information in SFFAS 17 and that the requirement to display assumptions precedes the list of information. The requirement to display assumptions appears with the valuation date requirements. These are underlying requirements related to each of the items of information in her view. If the issue is controversial enough to require an amendment, she suggested that a longer basis for conclusions is generally needed and a longer exposure period is warranted.

Mr. Reid opined that the current standard is unambiguous with respect to the assumptions. Paragraph 25 indicates that all information is stewardship information -- the only SFFAS 25 change was to present the statement of social insurance as a basic financial statement.

Mr. Patton said that if the assumptions were wrong in some way – this would show up in the statement. So, if the auditors were concerned about a significant error in an assumption, the auditors could take exception with the amounts on the statement.

Mr. Calder indicated that the assumptions are very powerful. He believes that if a reader could not access the assumptions then the statement is defective. Thus, if the auditor finds the assumptions are not presented, he or she should be able to say the statement is defective. If the assumptions are RSI and not presented, the auditor may not qualify his or her opinion.

Mr. Farrell agrees that there are important assumptions but asked if the average reader was going to assess the appropriateness of mortality rates by type of individual. He doubts if the readers are able to question such complex assumptions. He believes some should be basic but not all.

Mr. Calder said we were not talking 26 pages of assumptions. Just key assumptions would be disclosed. The sensitivity analysis would not be presented as a disclosure but as RSI.

Mr. Farrell agreed but wondered what the key assumptions would be.

Mr. Fontenrose, the project manager for SFFAS 17, joined the Board. Mr. Pat MacNamee, the chairman of the AICPA task force on social insurance, also joined the Board.

Mr. Anania indicated he preferred to amend the standard instead of interpreting it. He indicated that each time we reclassify an item of RSSI we face this issue. We need to be fairly specific about which parts are basic and which remain as RSI. We need to be cautious of these issues in other RSSI reclassification projects. He is inclined to want to do something about this issue.

Mr. Mosso asked Mr. Fontenrose whether in par. 25 regarding the best estimate of assumptions we spelled out what assumptions should be presented. Mr. Fontenrose indicated that we left it to the preparer and auditor to determine what significant assumptions are. For the sensitivity analysis, we did provide a list of assumptions for which sensitivity should be addressed.

Mr. MacNamee indicated the issue was precipitated by the audit guidance the task force is preparing. The task force researched other accounting literature – related to pensions and health care plans. In these cases, GAAP requirements included disclosure of significant assumptions. Testing the assumptions is an important part of what the auditor does with respect to these amounts. If assumptions were presented as RSI, the auditors would do a significant amount of work with respect to assumptions since the assumptions support the basic financial statement. The auditors report would be inconsistent with the level of work and assurance provided regarding assumptions. The auditor disclaims an opinion with respect to RSI in a standard auditor's report. Alternatively, the auditor could parse out the opinion but ultimately a clear indication of

the level of assurance with respect to information should be conveyed in the auditor's report.

For the presentation as a whole to be considered fair and for the auditor's report to be clear, the assumptions should be included in notes (not RSI). This is consistent with audit standards regarding adequacy of disclosure. Ultimately, if preparers have the option of presenting the assumptions as a note or in RSI and elect to present them as RSI, the auditor would have to take exception on the basis that disclosure was inadequate.

Mr. MacNamee indicated that if FASAB had asked the task force which items should be basic the task force would have indicated that the assumptions should be basic.

Mr. Farrell said he felt you would end up with assumptions in disclosures without FASAB acting. GAAS would demand the disclosure.

Mr. MacNamee indicated that if you read GAAP as FASAB SFFAS 17 and 25, the significant assumptions appear to be RSI but that management may elect to disclose assumptions. However, GAAS regarding adequacy of disclosure means the assumptions must be disclosed.

Mr. Calder asked if there was any literature to support that position? He supports where the task force is going but not how they are getting there.

Mr. Mosso indicated that not all GAAP is written in a standard. Some GAAP is so fundamental it goes without saying.

Mr. Fontenrose indicated that social insurance programs are so unique that the Board may not want to apply some generic GAAP.

Mr. Schumacher asked if the Board should articulate specific assumptions that should be in the notes? Mr. MacNamee indicated that SFFAS 17 lists some assumptions as being more important. However, each of the five social insurance programs is unique. He believes it would be problematic to have a generic list.

Mr. Mosso polled members regarding their views on whether the assumptions should be basic or RSI.

Mr. Anania agrees with the task force's analysis of the standards and the ambiguity. There is a mechanical adjustment needed to the standards since you can't read SFFAS 17 and 25 together to require disclosure. He believes an amendment is in order. We should try to get the best answer now.

Mr. Patton referred to the criteria for determining whether something is basic or RSI. He does not know what the answer would be. He would like to revisit all the assumptions to determine which assumptions go in which category. He indicated that the AICPA seems to need a list but Mr. MacNamee objected. He noted that each program is different and a single list would not be useful. There has never

been a view that we need a list. The view has been simply that we need GAAP to require disclosure of the assumptions. Mr. Patton noted that the Board consciously put items of information in one bucket or the other and should consciously do the same for assumptions. Mr. Reid opined that we would be doing that with the liability project and that would be a better vehicle for addressing this. Mr. Patton noted the sense of urgency. However, Mr. Reid said the task force seems to have made a decision to qualify the opinion if assumptions are not disclosed. Mr. MacNamee agreed. Mr. Patton noted that we can't resolve this before the task force goes to press. We have a number of critical issues.

Mr. Schumacher indicated that he had believed the significant assumptions went along with the statement when he agreed to SFFAS 25 and believes they should be disclosed.

Mr. Calder believes we should require disclosure of significant assumptions.

Mr. Zavada has no objections to moving the key assumptions. However, he appreciates that this will work out in practice.

Mr. Reid does not see us fixing anything – this information is being presented. There is no abuse here. He would prefer to wait until we delve into social insurance liability issues.

Ms. Cohen believes the assumptions should be basic.

Mr. Farrell agreed the assumptions should be basic but is not in favor of determining what is significant.

Mr. Mosso favors correcting the ambiguity.

Mr. Mosso indicated that there are two remaining questions – categorizing the assumptions and whether we do this as an amendment or interpretation.

Mr. Anania indicated that we could list a minimum set of assumptions that should be disclosed. He also favors an amendment.

Mr. Patton would list the minimum. He believes an amendment is required.

Mr. Schumacher asked whether we could do an interpretation if we list minimum assumptions. Ms. Comes responded that an amendment would be required and it would require more time. Mr. Calder noted that a single list doesn't work well for all programs. Mr. Schumacher indicated that he would simply require significant assumptions. If we do a list, he believes it becomes problematic and thus prefers generic language.

Mr. Calder asked about the time frames and recalled that there was not much of a time difference. Ms. Comes indicated there was only about 45 days difference

between an interpretation and an amendment in her initial estimates. The Board has a greater difference of opinion on this issue than she anticipated and the time difference would be greater based on that. Mr. Calder prefers an interpretation but would pursue an amendment if necessary. He believes the last item on any list would be “any other significant assumptions.” However, he would prefer to simply stick with “significant assumptions.”

Mr. Zavada prefers an amendment that requires significant assumptions be disclosed. He would not list specific assumptions.

Mr. Reid prefers significant assumptions to a list. There is too much variability among the programs. He believes an amendment is required. There is nothing ambiguous about SFFAS 25.

Ms. Cohen prefers significant assumptions to a list. She believes an interpretation would be better if it can be done.

Mr. Farrell prefers simply significant assumptions. He is willing to support an interpretation. The broader project on liabilities will give us another opportunity to consider these issues.

Mr. Anania asked whether a proposal relying on “significant assumptions” would generate a request for a list? Mr. MacNamee indicated that he would not request such a list. No issue has emerged yet regarding the ability to identify significant assumptions. In addition, the more detailed requirements for sensitivity analyses aid the auditor in identifying significant assumptions.

Mr. Mosso indicated he supported “significant” and an interpretation. Thus, we are five to four in favor of an interpretation.

CONCLUSION: Staff will prepare a draft interpretation for the members to consider as soon as possible.

- **Natural Resources**

Staff, Rick Wascak, led the discussion. Staff noted that the objective was to obtain approval of the proposed disclosures. Before discussing the proposed disclosures, staff reviewed information requested by board members on various other topics at the October Board meeting.

Staff explained that the Minerals Management Service (MMS) 2000 national assessment for oil and gas resources was emailed to members and that it was also contained in their binder. In regard to the national assessment, staff noted that the MMS did not track the cost of the assessment. Staff added that MMS representatives would not even attempt to estimate a range for the cost, nor did it prepare a separate budget for it. Other information reviewed with the Board included a brief overview of the FASB’s “expected cash flow” approach and the SEC’s “full cost” method for extractive

industries. Mr. Mosso added that the SEC's "full cost" method does not help us here because it is used by producers and not by lessors.

Staff referred the Board members to a 2-page paper pertaining to oil and gas resources, which had been provided to them earlier in the morning. Staff noted that the paper contained 3 questions and that each question was followed by staff's views. Staff explained that the paper was prepared based on information that had been gathered about the oil and gas resources and the initial "elements" concept paper discussed the previous day. Staff stated it wished to determine if Board members agreed with staff's views before discussing the proposed disclosures. The following 3 questions were discussed:

1. Are Federal government oil and gas resources an asset?

Staff explained it believed the oil and gas resources are assets because they meet the initial characteristics of an asset discussed the previous day.

2. Do Federal Government oil and gas resources meet the recognition criteria?

Staff stated that it believed the oil and gas resources did not meet the recognition criteria because they cannot be reliably measured. Absent quantity information traditional current value approaches cannot result in a comprehensive valuation of oil and gas resources.

3. Can an expected value for leases be derived from anticipated revenue with sufficient reliability to be capitalized?

Staff stated that it believed oil and gas proved reserves cannot be reliably measured or estimated in total. Absent quantity information, an expected value for leases cannot be estimated. Staff explained producers are required to disclose, as RSI, information about the quantity of proved oil and gas reserves and its estimated discounted net cash flow. However, the Federal government doesn't have information on proved reserves and it would have to get the information from the producers.

Staff explained that its views with respect to these 3 questions led to the proposed disclosures provided for discussion.

Mr. Patton asserted that it was not correct to say that oil and gas resources can't be reliably measured. He stated that it depends on what you are trying to measure. If you are trying to measure its cost, then the statement is too broad. The outcome for this project may not change because the costs appear to be immaterial; and, you don't put an asset on the balance sheet if it is immaterial. He noted, however, that he didn't want to anticipate the outcome of the "elements" study by saying things couldn't be measured at market value. He added that if there were better systems, the assessment cost could be measured.

Ms. Comes stated that the cost of assessing the resources has no effect on the cost or value of the resources. It is not a cost of acquiring or improving oil and gas resources. A comprehensive cost of acquiring and improving oils and gas resources cannot be determined.

Mr. Patton said if we were buying oil and gas resources, part of the cost of obtaining them would be the front-end cost of scoping out what there is. He added that, even though we are not buying oil and gas resources, he believes the front-end cost is part of the cost of resources the Federal government has. Staff asked if the statement were changed to indicate that the “quantity” cannot be reliably measured and that costs were immaterial, would he agree with the statement. Mr. Patton responded that it was a step in the right direction.

Mr. Anania stated that for the assessment stage and the leasing stage he is pretty well convinced that oil and gas resources would probably fail the recognition and measurement test. However, he was not convinced that in the production stage there isn’t a revenue stream that could at least be considered for some sort of reasonably, reliable measurement for an asset to be recorded. He added that it might require getting information from the producers, which the Federal government may not be getting today. Mr. Mosso added there were 2 revenue streams—a leasing stream and a production stream. However, the production stream is more estimable. Mr. Mosso asked if staff had discussed estimating anticipated revenue with representatives from the MMS. Staff noted it had and that the estimated anticipated revenue would be speculative, hard to obtain, and very soft. He also noted that the MMS did not say it couldn’t be done, but it was working on an alternative proposal. Mr. Mosso asked the Board’s reaction to trying to capitalize the production revenue stream.

Mr. Reid noted that from history one could argue we have a resource and from time to time it generates revenue. He explained that one technique to estimate what the resource is worth would be to look at historical records to see what production revenue flows were generated for the past 20 years. Then, consider if the existing resources that we have are as plentiful as the resources that generated the revenue flows over the last 20 years and decide if it is likely for the revenue flows to recur in the future. He noted that the assessment would be part of that judgment process in determining how likely it is for the revenue flows to recur. He added that something on the balance sheet is better than zero. Mr. Farrell noted that the amount recorded would be limited by the estimate of the future production revenues and would not represent all the resources in the ground.

Mr. Calder asked what important information is the Board trying to tell people. He said the Board is currently dealing with oil and gas. But, there are a lot of natural resources that we have available and can’t value. He said oil and gas is only one piece. Mr. Anania suggested that there might be other natural resources that have a production stage similar to oil and gas.

Mr. Reid suggested approaching the issue as though it were the sale of an asset and not as revenue earned. He added that the Board should take a look at what Mr. Anania

is suggesting. Staff noted that the federal government was not selling the oil and gas. It was selling the rights to explore, extract, and produce oil and gas; and, in return the Federal government receives a share of the value. Mr. Anania suggested that the Board be careful. He said that the Board should try to look at all opportunities even handedly, whether it is for an asset or liability. He noted that he was looking for the best balance sheet presentation as of a certain date. He added that you could almost say if you present enough in disclosures you don't need to record anything on the balance sheet. Mr. Anania also stated that, since this is the first of the natural resource items, he would like to spend some time to pursue ideas in order to be able to objectively say whether an asset could be recognized or why it is not..

Mr. Mosso stated that we would not be trying to get the total value of the proved reserves for oil and gas; only the value of the anticipated revenue stream we know exists for producing leases. Mr. Reid agreed that the amount of proved reserves would not be needed. He said the forecast could be over 50 years, or for a number of years deemed reasonable, discounted to present value, and recorded. Mr. Reid noted that collections could be made against the booked value. Ms. Comes noted that this approach would result in recognizing lease revenue year by year, but total production revenue in the year production began (at the expected net present value for all years of production). There could be unexpected changes to the production revenue that would appear to impact operating performance. For example, producers could decide to discontinue producing for some reason – such as a drop in oil prices - or improved technology could increase production. Mr. Anania responded that individual wells could have an effect on the collections; however, in aggregate, it should not. He added that the anticipated revenue could be trued-up every 6 months or so.

Ms. Comes remarked that she believes the Board should consider whether it is misleading to recognize significant anticipated revenues without showing any indication of the cost of what is being given up in exchange. Mr. Anania stated that it is really a question of what statement is more important. He asked if they are all important or does the Board want to look at certain statements and list the statement being most important. Ms. Comes indicated she was looking at it from the perspective of completeness. She explained her attempts to link this concept to the conceptual framework project are to show that there may be ramifications for making decisions to recognize the expected present value of a contract to dispose of something. She said she believes this concept, and its revenue aspect, should be linked to the conceptual framework project. Mr. Anania noted that he wasn't arguing hard for capitalizing anticipated production revenue. He said he just wanted the record to show that the Board considered the aspect of asset recognition for oil and gas; and, that it was not just dismissed. However, based on its findings, the Board decided to go with disclosures because that is what the rest of the world is doing and that is all the Board needs to do.

Mr. Anania suggested that staff do a search within and outside the Federal government to determine if others were recognizing something similar to anticipated revenue. Staff noted that it had researched how other countries reported natural resources and there

was no evidence of recording anything on the balance sheet. Mr. Mosso noted that, based on FAS 69, producers disclose expected cash flows.

Mr. Mosso stated that the Board should not dismiss looking at capitalizing the anticipated production revenue stream. He asked the Board members how they felt about pursuing this. Mr. Farrell said he believes there is the potential to have an asset associated with the production phase of the lease. But, he was also thinking about the vast accounting literature that deals with long-term contracting and leasing. He added that he was contemplating all the measurement criteria and hurdles that have to be met before there is income recognition. He suggested that the Board look at that literature to make sure that if it is an asset, there is something there to measure and recognize. He added there should be some set of established criteria for taking producing leases and recording a present value for them. He said it was worth pursuing. Messrs. Anania, Mosso, Patton, Reid, Schumacher, and Zavada agreed that it was worth pursuing.

Ms. Cohen said she believes there is an asset for oil and gas. However, she didn't believe there is a reliable measurement to recognize it and to use the anticipated production revenue stream is misleading. Mr. Calder said he was largely in agreement with Ms. Cohen. He commented that the Board is looking at a small piece of all natural resources and giving some recognition to this small piece in a very nebulous way. Mr. Reid asked if recognizing the anticipated revenue stream could be a precedent for other areas. Mr. Calder responded that he would like to see where we come out on this project first. Mr. Mosso asked staff to pursue the capitalization of the anticipated production stage revenue stream.

Mr. Reid asked if it was possible to get an order of magnitude of the revenue streams for other natural resources. Staff noted it would gather the information.

Staff described the proposed disclosures. Mr. Mosso observed that the proposed disclosures are probably relevant regardless of what may happen regarding capitalization. Mr. Calder questioned the disclosure requirement related to the collection process. Staff agreed that the language wasn't clear and would be made more descriptive. Mr. Calder asked if it would be possible to present the individual amounts collected for each type of natural resource on one schedule. Staff responded that it was. Mr. Mosso asked staff to prepare an example for the next Board meeting.

Mr. Farrell asked if the proposed disclosure for projected volumes and collections be classified as required supplemental information (RSI). The Board agreed not to decide the classification of projections since this item will be addressed during discussions regarding capitalization of the anticipated revenue stream. Mr. Anania commented that he believes the proposed disclosures present more detailed information than is needed. He said he believes a narrative describing the collections and distributions would suffice. Mr. Mosso asked staff to take account of the comment. Mr. Mosso asked what the next phase of the project would be. Staff noted it would address the recognition of revenue.

CONCLUSION: Staff will: 1) pursue capitalization of the anticipated production stage revenue stream, which will include researching accounting literature that deals with long-term contracting and leasing in relation to measurement and recognition criteria; 2) gather information pertaining to the revenue streams for other natural resources and develop a sample schedule presenting their magnitude in comparison to each other; and 3) revise the proposed disclosures, specifically, to make the proposed narrative requirements more descriptive and to remove the detailed collections and distributions information.

- **Stewardship Land/Heritage Assets**

Ms. Loughan opened the discussion by explaining that the Exposure Draft, *Heritage Assets and Stewardship Land: Reclassification from Required Supplementary Stewardship Information* was issued on August 20, 2003. Comments were requested by November 10, 2003. Staff explained that 12 comment letters had been received prior to the distribution of the Board binders and those were included in the binders and part of the staff analysis. Staff stated that one additional letter (from the AGA) had been received and staff distributed a copy of that letter to the members during the Board meeting.

Ms. Loughan explained that the staff objective for the meeting was to discuss the comments received and the staff prepared analysis and recommendations. Other goals for the meeting were to determine if a public hearing should be held on the ED and related comments and to determine any significant changes or areas for improvement to the proposed standard.

Staff directed the Board to the Staff Analysis and Recommendations at Tab 1 for discussion. Staff explained that based on the comments, 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 for periods beginning after September 30, 2004.
- Most respondents agree that the preparer should be allowed to exercise professional judgment in determining if the heritage assets and stewardship land are significant.

Staff explained that it would be best to discuss each of them separately and then determine if the Board agrees with the staff recommendations that follow each issue. The Board agreed with this approach for discussion of the issues.

Staff explained that 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. Staff further explained that this centered around three main reasons cited by respondents:

1. There is a need for more specific guidance, such as categories and reporting standards, on reporting for heritage assets and stewardship land information.
2. The Board should consider audit implications of the proposed standard, including the additional audit costs by classifying the information as basic.
3. The proposed standard would result in less useful information presented by agencies and/or information being disjointed when presented in different sections of the report.

Staff stated that the respondents that did not agree with heritage assets and stewardship land information being reported as basic information, recommended that it be classified as required supplementary information (RSI) or remain as RSSI.

Staff also explained that it looked at each of the 3 arguments and noted the issues raised by the respondents for the most part, echo issues raised since SFFAS 8 became effective September 30, 1997. Additionally, staff discussed that the issues identified by respondents had been discussed by the Board on several occasions. Specifically, staff provided the Board an excerpt of a more detailed timeline that had been included in the February 2003 Board Binders. The timeline detailed several Board discussions specific to audit issues, round table discussions with the AICPA, and discussion of work by the AAPC on specific guidance for heritage assets and stewardship land.

Staff briefly discussed the three staff recommendations related to this issue:

1. Request the AAPC to revitalize efforts of the Stewardship Guidance Work Group and work towards finalization of the Reporting and Assurance Guide for Stewardship Land and Heritage Assets, which may ultimately be published as a Technical release. The Draft should be expanded where necessary to cover the issues identified by respondents in the comment letters. The work group should also consider work done by other groups such as the Heritage Assets Categorization Team and include work efforts of the AICPA (see next point.) FASAB staff will work closely with the work group with the goal of finalizing the guide in advance of the effective date of the proposed standard.
2. FASAB staff be available to work closely with the AICPA on accounting issues related to heritage assets and stewardship land as it provides appropriate guidance for the audit profession.
3. Add additional language to support / reiterate the ability of agencies to have flexible reporting within the context of the proposed standards and also that the AAPC has commissioned a Work Group to finalize a guide.

The Chairman requested the Board's input on the above recommendations and other information presented on the issue.

- Mr. Farrell asked if the Board has considered that perhaps the respondents are right and this information should be considered RSI instead of basic. Mr. Farrell further explained that with the number of respondents that opposed the Board's proposal, that perhaps the cost-benefit issue is a valid concern. Mr. Farrell suggested that the Board should at least listen to the Board's constituents. Mr. Farrell suggested that perhaps audit costs in this particular area would be better served looking at the controls in this area, which would address accountability. The Chairman questioned if the Board's requirement for a line item in the proposal would make sense with the accompanying information as RSI.
- The Chairman requested staff to provide more information about the AAPC Stewardship Guidance Work Group (SGWG) and their work. Staff explained that the SGWG was formed in 1998 with the intent to perform research and collaboration on how to report and audit stewardship land and heritage assets. Staff further explained that the SGWG did finalize and expose for comments its draft guidance, *Reporting and Attestation Guide for Stewardship Land and Heritage Assets* that addresses asset identification, materiality considerations, condition reporting, and auditing issues. In January 2002, the AAPC SGWG decided not to finalize the Guide on HA & SL until FASAB work was completed. The AAPC decided it would re-evaluate the comment letters previously received once the necessary revisions have been made to the Guide as a result of the actions of the FASAB on its RSSI projects. Staff discussed that along with the recommendation that the AAPC SGWG be revitalized, staff believes that all the comment letters should be forwarded to that group, along with the work of the Heritage Assets Categorization Team for consideration by SGWG.
- Mr. Anania stated that he believed that there were legitimate concerns raised in the comment letters and perhaps the Board should consider not disturbing RSSI. However, Mr. Anania noted that the Board has decided to eliminate RSSI, so a decision must be made with regard to the items. The Chairman explained that the decision was not simply just to eliminate RSSI, but also to reclassify all existing RSSI elements within the current accounting classifications within the profession. The Chairman noted that when RSSI was created, the Board intended that it be subject to audit. The Chairman also added that the Board wants to get the Balance Sheet complete with all assets and liabilities that it can and in this particular instance, there is no question if these are major assets, but there are measurement issues.
- Mr. Schumacher noted the concern of several respondents regarding the increased audit costs. He stated that he believed there would be a one-time significant cost, but after the first year, the additional costs should not be major and would eventually level off. The Chairman added that once the balances such as land are determined, it would be fairly straight forward as the balances don't change much as the land remains there.

Ms. Cohen asked if the Board has additional information on what the added costs would be to audit the information. The Chairman commented the Board must decide what is best for financial reporting and most often with comment letters, the Board will have more negative comments to consider.

- Mr. Schumacher discussed his concern about the fact many respondents indicated that entities would present less information if the information was reclassified as basic. He questioned whether the Board should pause and reconsider the potential effect on financial disclosure.

Mr. Patton explained that the information being reclassified as basic is very fundamental (description and physical units) and the agencies could continue to report additional information in another part of the report. Mr. Patton explained that getting some audit assurance on the physical units for stewardship information is a very important step. The Chairman further explained that the additional information that agencies may wish to include does not necessarily have to be in a different part of the report, as long as the information is clearly labeled. Mr. Schumacher commented that he has seen unaudited information within the body of footnotes. Mr. Patton noted that respondents did comment that it would be awkward to present information in different places. Staff commented that the proposal does not eliminate any reporting requirements, so agencies will still be required to report the same information and also have the flexibility to report additional information as it has in the past. Mr. Farrell added that although the requirements are the same, it appears that the agencies are saying they probably won't provide much more than the minimum requirements. Mr. Patton commented that the Board didn't require the additional information before and the agencies chose to provide, so they may continue to provide the information to tell their stories.

The Chairman discussed that normally one would expect the financial statements to be concise, so boiling the stewardship information down to a piece that is appropriate to the financial statement would be what the Board would prefer. Mr. Reid stated that for the consolidated government-wide financial statement, the information must be boiled down. In addition, looking at the size of the reports and the amount of information included in the stewardship section, a little less information may not be a bad thing. Mr. Reid also discussed that he believed that agencies would still continue to provide the stewardship information, as he believed that they would want to continue reporting the information if it is essential to the interests of the agency. The Chairman also commented that the financial statement is a part of the Accountability Report and other information could be presented within the Accountability Report.

The Executive Director suggested that perhaps the Board should consider whether a public hearing should be held. The Executive Director explained that the hearing would offer an opportunity for the Board to hear more information about the issues, especially

the cost factor. The Board members agreed that a public hearing should be held and it would be helpful.

The Chairman requested that Board take a moment to review the staff recommendations specific to the issues that surrounded the respondent not agreeing with the stewardship land and heritage assets being classified as basic. A majority of the Board agreed with the staff recommendations, but reserved final decisions for after the public hearing.

Staff directed the Board to the next issue on page 6 of the Staff Analysis and Recommendations which summarized that most respondents agreed with the Board's new disclosure requirements and did 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. Staff did note that one respondent did not agree with the disclosure for an explanation of how heritage assets and stewardship land are pertinent to the entity's mission because the respondent stated that agencies may have heritage assets as a result of their compliance with laws and regulations and that Congress has determined certain classes of assets to be nationally significant regardless of the agency mission. Staff recommended that adding additional language to include how heritage assets are required and/or fulfill mandates promulgated in laws, regulations, and executive orders to paragraphs 28a. and 44a. The Board agreed with the staff recommendation.

Staff directed the Board to page 7 of the Staff Analysis and Recommendations for the next issue, which summarized that most respondents do not agree with the proposed effective date for periods beginning after September 30, 2004. Staff explained that the key reasons cited for the delay of the effective date included the following:

1. There is a need for additional time to address issues noted in their arguments against classifying the information as basic.
2. Time should be allowed for agencies to include additional funding in their budgets for the additional work, including the additional costs to be included in audit contracts.

Staff further explained that most of the respondents suggested that the effective date be for periods beginning after September 30, 2005 and two respondents recommended for periods beginning after September 30, 2006. Staff also pointed out that the updated project plan shows the standard not being final until August 2004. Staff explained that its recommendation would be the proposed standard effective date to be changed to periods beginning after September 30, 2005 because staff believes the agency budgets and audit contracts are strong arguments for delaying the effective date. Staff further explained that the additional time (which would in effect be over a year before implementation) would be sufficient time for agencies to address some of the issues noted.

The Chairman requested the Board's input on delaying the effective date as proposed by the staff. Mr. Calder commented that the agencies have been reporting this information for a long time and there is no reason to delay. He explained that all

indications are that the agencies are reporting good information, so it should not be much additional work. He further explained that there are no real major issues, other than perhaps audit issues and he does not see them as major enough to delay the effective date. Mr. Farrell also agreed that no delay in the implementation would be necessary. Mr. Patton suggested that he would agree with the staff recommendation considering the current timeline shows it being issued in August 2004. All other Board members agreed with delaying the effective date for one year.

Staff directed the Board to the bottom of page 7 of the Staff Analysis and Recommendations, which summarized that most respondents agree that the preparer should be allowed to exercise professional judgment in determining if the heritage assets and stewardship land are significant. Staff explained that one respondent did not agree and the respondent noted that the current definition of heritage assets already includes the words “significance,” “importance,” and “significant” and by including “significant heritage assets” is redundant, and implies creation of a multi-tiered system.

Mr. Patton explained that he had a slightly different read of the comment letters regarding this issue. Mr. Patton explained that everyone would agree that the preparer should be able to exercise significant, professional judgment, but it is more of a matter of with respect to what. Mr. Patton further explained that he thought it was also the wrong frame of the question. Mr. Patton discussed that six of the respondents commented that “significant” was an ambiguous term. Mr. Patton explained that the letters indicate that the word “significant” is being interpreted in different ways. Mr. Patton suggested that it appears that some interpret it to mean material, and if people are going to interpret “significant” to mean material or something else, the Board should be clear in what it means. Mr. Patton explained that the question should have been more focused on whether the term significant as it is used in the proposed standard is sufficient. Mr. Patton further discussed that he believes if the Board is going to use the term significant, it should define it. The Chairman commented that the term significant is used widely throughout accounting literature and it clearly means something more than material. The Executive Director added that it normally also implies more of a qualitative connotation versus quantitative.

Staff commented that in earlier versions of the proposal, the term material was used instead of significant and the Board decided to change it to significant. Mr. Patton discussed that there should be some sort of explanation of the difference between materiality and significance or people will be using widely different criteria.

Mr. Anania suggested that the word “amounts” be removed from the beginning of par. 28 and 44 where it reads “Entities with significant amounts of...” Mr. Anania commented that some may think of dollars with the word “amounts” which may also lead to confusion. Mr. Anania also commented that he does understand Mr. Patton’s point on the term significant, but he does not believe the issue of when to use the term significant and when to avoid it can be addressed in this project, especially considering this project is dealing with units versus dollars. Staff suggested that “significant amounts” could be removed from the beginning of par. 28 and 44 since the last sentence the last sentence of those paragraphs does state: “The note disclosure related

to significant heritage assets/stewardship land should provide the following.” The Board agreed with the staff recommendation.

Mr. Patton reiterated that he believed the Board should provide additional information regarding what is meant by significant. Mr. Patton explained that he thought of significant as something that is important for political or other types of reasons. He suggested that setting standards where words can be used or defined in different ways leads to different types of implementation. The Chairman explained that in areas such as this where there are many different variables, it may be best to leave it up to professional judgment.

Mr. Farrell asked if the public hearing would be open for everything or would the Board try to focus the speakers on certain questions. The Chairman explained that the hearings are normally open for any discussion for people to back up their comment letters. Mr. Patton asked if it would be possible to pose questions when the Board solicits for testimony. The Executive Director explained that it is possible to contact respondents to let them know the Board is interested in hearing more about the issues raised in their letters. In addition, the Board is also permitted to emphasize areas that the Board would like to hear testimony, such as cost-benefit issue and the meaning of the term “significant”. Mr. Farrell suggested that the Board should alert the potential presenters that the Board has tentatively agreed to delay the implementation by one year. Mr. Patton explained that he would like to reframe the question on the use of the term significant for consideration when the Board sends out the notice for the public hearing. The Chairman agreed that both of these items could be covered in the notice.

One Board member questioned the need for the public hearing considering many decisions have been made. The Chairman explained that nothing is final until a final ballot and the public hearing is an opportunity to learn more and have a better understanding of the issues behind the comment letters, which could affect the Board’s actions. He explained, that after the public hearing, the Board could decide to move forward with the decisions made today or they could totally change their decisions and have to re-expose the document for major changes.

The Executive Director explained that it would be best to focus on encouraging respondents to testify at the public hearing and to defer any plans to finalize a pre-ballot until after the public hearing.

Mr. Farrell asked if it would be possible to ask respondents what they think the actual costs would be to audit the information. The Executive Director asked Board members if they would be interested in having staff query audit firms to solicit their views on the cost issue. Mr. Farrell explained that it would be interesting to hear from some of the agencies with large amounts of heritage assets, such as Interior, and find out if they have researched the costs—specifically for the first year and then years thereafter. The Board agreed to have staff follow-up on this with the audit firms.

Staff directed the Board to page 17 of the Staff Analysis and Recommendations, which included other comments (outside of the specific responses to the questions posed in

the ED) received from respondents. Staff explained that there really were no changes or staff recommendations based on these comments other than forwarding these comments to the SGWG for consideration in their guidance. The Board agreed with the staff recommendation.

CONCLUSION: A Public Hearing will be held at the March Board Meeting. Staff will update the proposed standard for changes agreed to in the meeting, which included delaying the effective date one year and adding additional language as noted in the staff recommendations above.

- **Stewardship Investments**

Ms. Loughan opened the discussion by explaining that this project relates to the reclassification of Stewardship Investment information that is now currently classified as RSSI. This project evolved as part of the Board's overall project of reviewing and re-categorizing the stewardship elements to fit the categories identified in the traditional auditing model. The Stewardship Investments category (which includes Nonfederal physical property, Human capital, and Research and Development) covers the remaining RSSI elements. Staff explained that the objective of the meeting was for staff to provide an introduction to the project by discussing the background information, current requirements, and sample reports. Staff also hoped to obtain initial thoughts from the Board and confirm the scope of the project and approve the working project plan.

Staff discussed the various background information included in the Board binders, which included the Staff proposed Stewardship Investments Project Plan, Summary Chart of RSSI Elements & Status, Summary of Remaining RSSI Elements & Requirements, Pertinent Excerpts from SFFAS 8 *Supplementary Stewardship Reporting Related to Stewardship Investments*, and Sample Stewardship Report Excerpts for Stewardship Investments.

Staff also explained that the staff's preliminary recommendation would be to reclassify the information as Required Supplementary Information. Staff further explained that if the Board did approve the project plan, staff would develop a more comprehensive analysis and recommendation. Staff reiterated that the intent was to introduce the topic and gather the Board's initial thoughts on the project. The Chairman requested the Board's thoughts on the project, project plan, and initial staff recommendations:

1. Mr. Schumacher asked if it would be accurate to say that the Stewardship Investment information is auditable and it is more a question as to whether the information is necessary for fair presentation. Staff explained that there have not been any major audit issues other than the ability to obtain information from the state and local governments for shared contribution amounts. Staff also discussed that the information is being reported on the Statement of Net Costs as part of expenses. Mr. Calder explained that there is an audit issue with

respect to human capital investments in that there should be evidence that the investments contribute to the well-being of the nation.

2. The Chairman questioned if the agencies were providing trend data. Staff explained that in the earlier years there were problems with providing prior year data, but considering the agencies have been reporting the information for several years now, the trend data is available.
3. Mr. Farrell asked if the Board is aware if this information being produced anywhere outside of the financial statements. He also questioned the purpose of reporting this type of information. The Chairman explained that it goes back to the Stewardship Objective and relates to the well-being of the nation, rather than the federal government. The Executive Director explained it was also part of an attempt to balance the varying types of investments. Mr. Farrell asked if the information is useful to the public and if it is fulfilling the objective. The Chairman commented that agencies are encouraged to report outcome measures that show how the investments improve the well-being of the nation. Staff commented that the outcome measures are not part of the required minimum reporting, but are described in the measurement section and the standard provides that agencies should be able to provide information on the outcomes of the programs reported.

Mr. Farrell explained that he believes that staff should not only pursue if the Stewardship Investment information should be reclassified as basic or RSI, but also consider if the information is actually necessary and whether the Board should continue to require that it be reported. The Executive Director stated that the National Science Foundation might be a good agency to contact and discuss this with as they do disseminate their report widely.

The Chairman explained that some of this information, especially specific to outcomes, is now required by GPRA. Therefore, it may be a good idea for the Board to reconsider if this information is still necessary as part of the financial statements because the information may very well be reported in other means. Staff noted that in reviewing the reports, many agencies refer to the performance report section in the Stewardship Investments information.

Mr. Reid suggested that the Board could include a question in the Exposure Draft asking respondents if they believe the information should be retained.

4. Mr. Anania asked staff if the sample reports included in the binder were the most extensive or best practices. Staff explained that the reports included in the binders were considered good examples because they included most of the different types of stewardship investments and were therefore more extensive than some of the other reports.

5. The Chairman commented that the Board would be considering the Stewardship Objective and the Systems and Control Objective at the March Board meeting and the Board should tie this into that discussion.

The Executive Director asked the Board for confirmation that as of this point, there are no Board members that believe the Stewardship Investment Information should be classified as basic. Mr. Patton explained that he believed the information about investments in human capital is one of the most important things the Government does and considering that the Board is unlikely to show anything on the Balance Sheet about this, it is extremely important information and fundamental to in reporting what the Government has done. Mr. Patton further explained that if the human capital investment information is auditable, that it is essential and should be basic. Mr. Anania stated that his preliminary thoughts would be to classify the information as RSI, but he has not reached a final conclusion. His main reason for not making the information basic is because much of the reporting is soft information and much of it is qualitative, especially the outcome reporting.

The Chairman asked for the Board's position on next steps and whether the Board agreed with the staff recommendation on the project. The Board agreed with the staff recommendation of reclassifying as RSI, except the Board would like staff to research the area further to determine if the information is still necessary, especially in relation to the Board's reconsideration of the Stewardship Objective. Mr. Patton explained that in the process of supporting an RSI classification, the staff must present an argument against the information being reported as basic. Mr. Zavada explained that even if the Board eliminated the requirement, agencies would still be permitted to include the information in their reports. He further explained that agencies could include the information in the MD&A, which may make most sense for reporting. Mr. Farrell explained that some agencies are probably reporting this information as a separate segment on the Statement of Net Cost. He added that as financial statements have evolved, this information is probably being reported in better ways. The Chairman commented that these are other ideas or alternatives for the Board's consideration for MD&A or perhaps a line item on the Statement of Net Cost .

CONCLUSION: Staff will continue research and develop alternatives for classification of Stewardship Investment information, which may include eliminating the reporting requirements, reclassifying as RSI, reclassifying as basic, or a combination of these alternatives. Staff research will also include determining if the information currently required for Stewardship Investments is being reported by other entities.

Adjournment

The meeting adjourned at 2:30 PM.