FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD
April 23-24, 2014
Room 7C13
441 G Street NW
Washington, DC 20548

Wednesday, April 23, 2014

Administrative Matters

- ### Attendance

The following members were present throughout the meeting: Mr. Allen, Messrs. Bell, Dacey, Granof, McCall, Showalter, Smith, and Steinberg. Mr. Reger was present for most of the meeting and during his brief absences, Ms. Kearney represented OMB. The executive director, Ms. Payne, and general counsel, Mr. Marchand, were present throughout the meeting.

It was announced that Mr. Reger, having been detailed to OMB from Treasury, would be representing OMB. Mr. Bell would be representing Treasury.

- **Approval of Minutes**

The minutes of the March meeting were approved at the meeting.

Agenda Topics

- **NAPA Study Results**

Overview

The Board discussed the National Academy of Public Administration's (NAPA) report, *Financial and Related Information for Decision-Making: Enhancing Management Information to Support Operational Effectiveness and Priority Goals.* FASAB contracted with NAPA to help the Board learn more about the financial information needs of executives and managers as well as preparers' needs for resources to guide financial information development. The research would inform the Board on: the availability of good financial and related information; the effective use of financial data by senior managers; the current and desired role of the Chief Financial Officer (CFO); and, if gaps exist, what options are most likely to be helpful in closing those gaps. The NAPA team consisted of the following members:

NAPA Panel

G. Edward DeSeve, Chair

David Mader

Barbara Wamsley

NAPA Staff

Joseph Mitchell

David Treworgy

Jonathan Wigginton

The NAPA team conducted a series of discussions with 27 federal executives and senior managers with operating responsibility for agencies, bureaus, offices, divisions, or comparable organizational units and, to facilitate the conversations, the team used a discussion guide that included both multiple choice and qualitative questions. The following are excerpts of their principal findings:

> **Availability of information**: Data generally are highly accurate and granular, but federal agencies face challenges in analyzing and transforming data into readily understood, actionable information for executive decision-making— especially the linking of budget, costs, and performance.

Use of information: The degree to which financial data are effectively used for decision-making is heavily driven by each organization's revenue source and operational approach. Agencies tended toward one of two general camps: 1) user fee-based revenue and/or production-oriented, direct operations agencies, where external pressure for transparency fosters the creation and use of financial and cost analysis for decision-making by executives and senior managers; and 2) appropriations-based revenue and/or regulatory, policy, and grant-making agencies, which generally have fewer needs for detailed financial and cost analysis. Both types of agencies can utilize financial data more effectively if leadership instills a culture that pays attention to costs and performance by creating structures and incentives that encourage employees to carefully examine these issues.

Role of the CFO organization: CFO organizations will increasingly need to offer valuable decision-making support to executives and senior managers. They should continue to evolve from a legacy core focus on transaction processing and compliance to a more modern approach that features sophisticated cost and performance analysis tailored to the decision-making requirements of agency leadership.

To address the gaps observed and meet the decision-making needs of executives and managers, NAPA discussed six recommendations:

1) increasing the ability for CFO staff to act as business partners to agency program leadership;

2) emphasizing development of CFO staff skillsets;

3) linking budgeted resources to costs, outputs, and performance;

4) developing financial and programmatic dashboards specifically tailored to the decision-making requirements of executives;

5) enhancing existing reporting systems; and

6) creating specific legislative and regulatory catalysts, such as the 2009 American Recovery and Reinvestment Act reporting requirements.

Mr. DeSeve opened the panel discussion by noting the importance of the topic. The alignment of financial information and management information has never been perfect. The thrust of GPRA to create a performance framework needed to have integrated with it the budget information on a timely basis and on a continuing basis. The recent improvement of GPRA to create quarterly reviews, and to have the chief operating officer of the department, typically the deputy secretary, conduct quarterly reviews creates an even greater demand for financial information. To some extent in some agencies it will be balance sheet information. In other cases it will just be budgetary information. But to pull that information forward so that it can be considered at the same time, if not combined with, as performance information is considered.

The study found that there continues to be a disconnect in managers' minds between the financial information (which they view as very accurate and very granular) and information useful to them as they managed their departments. The key question before FASAB and before OMB and GAO is how do we improve the utility of the financial data and make it meaningful to managers at all levels? I always talk about from the shop floor to the top floor. How do we make it meaningful at the shop floor, and then how do we make sure that it gets up to the top floor?

Particular matters discussed during the Board meeting are presented below.

Success Stories

Mr. Treworgy noted that there were some pockets of success. For example, at one agency, the chief operating officer developed the information that they felt was lacking. They found a relatively junior person, skilled in Microsoft Excel, and they developed a series of analyses and dashboards that actually connected human resources, finance, and operational information and created a whole series of management information charts for the agency administrator. Although this was a somewhat informal effort, it was very effective. Also, there was a user-fee funded agency that was heavily data driven and integrated cost and budget information. Although they had “wish list” items, most agencies would be glad to get where they were.

The Need for Data Analysis and Enhanced Skillsets

Mr. Mader noted that he has experience in both the federal and private sectors and noted that the report validates that the federal community has made great strides in the accuracy and timeliness of data. Now, the issue is how to take that data beyond just the CFO and to integrate it with another silo? There are many legacy systems that do not talk to each other and because we are not going to invent new databases or create new systems, we need to leverage the skills and the technology that is available - to extract and integrate that data. The staff are expected to do something more and we have not necessarily recognized that as a core requirement for the CFO to provide to the rest of the organization. There should be a way to identify what that skill set is; start recruiting for it; and start developing the expertise that is sorely needed. The business analytics tools are available and are being used. It is a matter of identifying the number of staff you need within an organization and going out and recruiting.

Ms. Wamsley noted that training is also needed.

Mr. Treworgy noted that program managers indicated that they struggled with the hiring process. The private sector is able to hire their candidates with greater agility because the government’s hiring process is lengthy – it can take four months to make an offer.

Linking Budget, Cost and Performance

Mr. Treworgy noted that agencies appear to be at different stages with respect to developing cost information and linking budget cost, and performance. Some are further along than others and different agencies have different needs. Some might acknowledge that they have different places to spend the money, and if they knew how to allocate it better, they could perform better. However, others might say that, although they have not performed the analysis, they have an idea of conditions and additional analysis would not necessarily help lead to improvements. One agency was able to list their major programs and attempt to describe in words, and in as much quantitative detail as possible: the amount that went into the programs; and what were the outcomes. While that sounds basic, it did take a fair amount of time and it was a departure from what they had done before, which is just to have the regular financial statements. In addition, one agency mentioned that while we have accounting codes to track costs, we do not have a way to track the benefits derived from those costs. Mr. Simms agreed that agencies were at different stages and noted that perhaps the key would be finding some guiding principles that all the agencies could look to achieve.

Mr. DeSeve noted that incentive structures in the federal government do not create a pull for the kind of information we are discussing. In general, Congress has not asked to have information presented in a manner where there would be a clear attribution of outcomes and costs.

Mr. Treworgy also noted that one department felt that they were relatively unique among departments in discussing the benefits achieved for the money provided. They felt that in their discussions with the administration and Congress they actually did a good job articulating the linkage between appropriations and outcomes and they felt some other departments were kind of passive and not taking the time to lay out the benefits that were achieved from the spending.

Regarding whether reliable systems are in place to allocate overhead, Mr. DeSeve noted that the Census Bureau has many independent projects contracted to them from other organizations such as the Department of Labor, and they have to be able to cost those projects so that they can bill for the services. Accordingly, they would need to have an allocation mechanism for overhead. When there is a need, the entity would have good systems, but if it is only an internal initiative and the need is not as great, the systems may not be as good.

Concerning the level for linking performance information, Mr. DeSeve suggested the Treasury Account Fund Symbol level. If a Treasury Account Fund Symbol has been established, you ought to be able to link that or a couple of them to a particular performance. He noted that this was the approach used for the Recovery Act reporting.

Accuracy and Completeness of Data

Mr. Treworgy noted that there was concern regarding data overload rather than data quality. Survey participants did not have the sophisticated tools necessary to array the data in a useful manner. Mr. DeSeve noted that there was some concern with timeliness in some organizations.

Common Information Needs

Mr. Dacey noted one agency that built a large information repository, but found that it was not being used to the extent expected because the managers did not know how to effectively utilize the information . As a result, the agency designed template forms of reports that managers could use to help them array the data into something that was useful to their particular needs.

Regarding whether there were clear views on what information the survey participants sought but could not access, Mr. Treworgy noted that a lot of the participants indicated that it is not just a matter of having analysts who know how to make the right reports, but it is about having the managers and executives who know how to ask the right questions – how to “kick the tires.”

Also, with respect to whether there are some common information needs, Mr. Treworgy noted that it would be a challenge to get to one-size-fits-all in the program area because many of the information needs are unique.

The One-Year Appropriation Cycle

Mr. DeSeve noted that some agencies are already receiving two-year appropriations and there may be some case studies where two-year money or, in some cases, no-year money will be available more routinely as appropriators get comfortable with that activity.

Recommendations to Others (non-FASAB Recommendations)

The NAPA report included recommendations to organizations such as the President's Management Council and the Chief Financial Officer's Council and the NAPA team is considering making presentations to those groups.

The Role of FASAB

Mr. DeSeve noted that FASAB should develop and publish a model, recognizing that some may not use it or use it right away, and educate the community on how to implement it. Also, the Board should try to get Congress to understand the importance of aligning cost data and performance data. The question is how much are we putting in, not necessarily how much are we getting out? In addition, FASAB voices a view and could say that there is another step that can be taken with the data that was created as a result of its initial standard setting. Thus, FASAB could frame the questions and the principles around which analytics should be created, not only within the agency but also from an accountability perspective at the level of the President's budget and at the level of congressional review.

Mr. Mader added that once a model is created, point to best practices and say this is what is in the art of the possible.

Ms. Wamsley noted that third parties are involved in delivering program outcomes and program performance is not accomplished or services delivered when expenditures occur. This presents a big problem that people have struggled with for a long time. Whenever third parties are involved, how do you set standards to facilitate consistency in the accounting systems and link finance to specific program outcomes? Accordingly, concentrate on what is doable today, the programs that are involved in direct operations, and move forward. Programs that are involved in direct operations generally have more of an immediate output.

With respect to performance reporting, Mr. DeSeve noted that he believes a statutory basis already exists for the unification of financial and performance information. The Government Performance and Results Act (GPRA), the CFO Act, and the GPRA Modernization Act include the idea that program information and financial information should be unified. Thus, a basis exists that GASB likely did not have because of the different constitutions of the states, the different charters of the cities and so on. We need to associate the financial information that is created with the performance information that is required.

Mr. DeSeve also noted that the performance information does not necessarily need to be audited, but the two (financial and performance) have to stand side-by-side. Beginning to audit performance information is a slippery slope. So, he would stay away from the auditing of performance information. The Inspector General will inform you about the performance information; or Congress will tell you whether they think it is useful; or OMB will ask questions again and again about it. Also, while placing performance information under an audit rubric is a mistake, being able to associate financial information with program information is something that you have the capacity to do.

- **Reporting Model**

During the reporting model discussion, each Board member presented their individual views regarding an ideal reporting model. Staff will summarize the presentations, indicating common themes, to facilitate discussion in June 2014. During this portion of the meeting, Messrs. Allen, Showalter, Smith, McCall, and Steinberg presented their views. The remaining Board members presented their views the following day.

Mr. Allen

Mr. Allen noted the following guiding principles for his ideal model:

- The Consolidated Financial Report (CFR) needs to be more intuitive and understandable and focus on decision useful information for citizens.

- The CFR needs to better report the Federal government's financial position (condition) and changes in that financial position (condition) during the reported fiscal year.

- All financial reporting needs perspective and context. Financial trend information is necessary for context at the CFR level and performance information, budget information, etc. provide perspective and context at the agency level.

- Agency reporting should be structured to best provide information to their intended users.

- Agency reporting should also provide audited information necessary to prepare the CFR.

- Agency reporting should provide disaggregated CFR information and disaggregated information useful for program managers and other internal users. However, the financial statements need not be structured in the same manner as the CFR.

At the government-wide level, Mr. Allen's model would include a Statement of Financial Trends showing key measures of interest to citizens; and a statement of net cost trends that would present cost by function and multiple years of cost information. Also, users would be able to link from the government-wide statement to the agency statement of net cost showing cost by function and program. Agency level reports would only include other statements as necessary. For instance, not all agencies would have a balance sheet or Statement of Significant Assets and Liabilities.

Details of Mr. Allen's presentation are attached.

Comments/Questions

Members discussed the possibility of reporting cost by budget function and Mr. Allen noted that the key is that the ideal model should start with what users want to know without regard to the constraints at this time.

Mr. Bell noted that the proposed Statement of Financial Trends basically shows information that is being presented today in the Management's Discussion and Analysis (MD&A) and Mr. Allen responded that the proposed statement provides about 95 percent of the information needed to answer citizen's questions.

Regarding whether the Board should consider redefining financial position, Mr. Allen noted that the Board has conceptual guidance and he would not look to revisit that issue. However, he would start with the existing concepts and move to a broader discussion of financial 'condition.'

<u>Mr. Showalter</u>

Mr. Showalter noted the following guiding principles for his ideal model:

- The project should provide guidance about the type of information included in government-wide vs. component reporting
- Determine financial statements and other information required for government-wide vs. component reporting
- Align reporting objectives with the applicable financial statements and other disclosures
- Determine whether financial statements should articulate among each other
- Financial statements are not the only source of information
- Financial statements would include reporting on 'key' programs – which may vary over time

As part of his ideal model, Mr. Showalter noted the possibility that only government-wide financial statements would contain a "full-set" of financial statements and agency/component statements should primarily focus on operations. In addition, there should be a closer linkage between costs, outputs, and performance and encourage, but not require electronic reporting.

Details of Mr. Showalter's presentation are attached.

Comments/Questions

Mr. Showalter clarified that agency information could be different from the government-wide information and, essentially, the government-wide model is not simply a replication of what is in the agency model. However, the agency could provide more detail than the government-wide.

Mr. Steinberg noted that both Messrs. Allen and Showalter indicated that perhaps agency-wide balance sheets may not be needed. Accordingly, how would the determination be made regarding which assets and liabilities would be reported? Mr. Showalter noted that he was focused on ‘reporting’ rather than ‘auditing,’ which are two different topics. Also, the reason we focus on the balance sheet is that we need the cost data. There could be a requirement to audit and internally report a balance sheet, but not part of the external financial statements. If there are items that are not significant to the performance side, why spend time auditing it? Members were concerned about what would be FASAB’s role with respect to the financial information gathered and maintained internally but not reported externally.

Mr. Dacey asked whether the statement of changes would show the changes in assets not reported. Mr. Showalter noted that he was focused on bringing about some new ideas, to think about things differently, and then the Board could evaluate what is actually feasible. Assets and liabilities would still be presented at the government-wide level.

With respect to Mr. McCall’s question about performance measures, Mr. Showalter noted that he was considering the need to inform citizens about commitments and noted that a good government-wide performance measure would be the one Mr. Allen discussed – are we better off today than yesterday?

Mr. Reger noted that the presentation appeared to be oriented toward information reporting and strengthening the agency reporting activities rather than actual accountability reporting. Mr. Showalter agreed that there might be less detail at the government-wide level and more robust information at the agency, but he emphasized that the information is about accountability.

Mr. Reger noted that Mr. Allen’s presentation appeared to raise the issue of whether the financial statements represent the United States Government as an entity or something broader than simply the financial position of the government and he wanted to clarify Mr. Showalter’s focus. Mr. Showalter noted that he focused on the government as an organizational entity.

Regarding the reporting objectives, Mr. Showalter noted that the federal government should be achieving the stewardship objective, but there are items of information that help achieve stewardship that are not addressed by the other objectives (budgetary integrity, operating performance, and systems and control) such as sustainability reporting.

<u>Mr. McCall</u>

Mr. McCall began with the reporting objectives, suggesting changes to them and noting how they might be achieved. He also noted that the ideal would include: a budget-actual statement; the same basis of accounting for budget and financial statement reporting; service effort and accomplishment information; and sustainability information. Mr. McCall called for a task force to assist in defining the term “program” and research be initiated to decide whether stewardship also includes the term “sustainability” or whether SFFAC 1, Objectives of Financial Reporting, should be expanded to also include sustainability as an additional concept or include within stewardship.

Details of Mr. McCall’s presentation are attached.

Comments/Questions

Mr. McCall clarified that he is fairly comfortable with the existing set of financial statements and believes that citizens will likely review the government-wide Citizen’s Guide rather than agency financial statements and there should be some key government-wide performance measures.

Mr. Smith

Mr. Smith compared the components of the existing model to the reporting objectives and determined what modifications were needed. Accordingly, his model would address some of the needed changes and would include financial statements such as:

- Statements of Comparison of Cost and Accomplishments to Budget - Presents the expenditures incurred compared to the budget for the current year and a discussion on the progress of the major priorities.

- Statements of Progress on Major Priorities - Presents the expenditures for the current year by term specific funding and ongoing expenditures, next year and five years of expected expenditures to achieve goals of major priorities, and the percentage of total expenditures incurred to percentage of goal accomplished for major priorities.

Also, Mr. Smith noted that the statement of net cost should show the cost of major programs in priority order. Accordingly, citizens could see the greatest priorities for the entity.

Details of Mr. Smith’s presentation are attached.

Comments/Questions

Regarding the focus of the model, on the government-wide or agency, Mr. Smith noted that he hoped that the type of model he is proposing would create a public dialogue on priorities. We need to determine our priorities and decide when we can afford to do them. Also, if we are trying to achieve a goal and it is not being achieved, we need to ask why that item is still being funded. To understand the priorities, a structure would need to be in place at the agency level because the agency level provides the detail. The government-wide level is a snapshot of where we are as a nation. Accordingly, the balance sheet is important at the government-wide level, a consolidation of the agencies.

Mr. Steinberg

Mr. Steinberg noted that the focus should be on the agency level flows statement. He proposed a statement that would present the strategic goals of the agency, budgetary resources, obligations, outlays, and accrued costs. The statement would replace the current budgetary resources statement. Also, Mr. Steinberg believes that performance information needs to be included in the report to enable users to ascertain the outputs and outcomes received for the incurred costs and thereby be able to assess whether the outputs and inputs are worth the costs. Mr. Steinberg stated that he would have a separate disclosure in which an agency reports the same information for the five to ten programs the agency believes are its most important and in which there is the most interest. Requiring the reporting of costs for five to ten programs would stimulate the determination of costs for all of an agency's programs, and thereby provide for the implementation of SFFAS 4, *Managerial Cost Accounting Standards and Concepts*, which has long eluded the financial management community.

Also, the Board should develop qualitative characteristics for performance information and encourage electronic reporting.

Details of Mr. Steinberg's presentation, along with his outline for a proposed concept statement and his article, *The Federal Financial Reporting Model: Where To, Now?* are attached.

Comments/Questions

Mr. Steinberg noted that the Government Performance and Results Act requires strategic planning, managing by strategic goal, and information on what it is costing to pursue that strategic goal.

Regarding why he focused on agency level reporting, Mr. Steinberg noted that the concerns and studies set forth have tended to focus on the agency-wide statements. Also, at the agency level, the more important information are the performance information and where does the agency stand with respect to its budget. The government-wide level provides the financial information, our future commitments, assets, the deficit, etc.

Members acknowledged the results of the CFO Act 20 year study which noted that the value of the financial statements are that they have improved the accountability to the public; that the federal government and its agencies can prepare financial statements and have them audited; and the financial statements have improved the accuracy of financial data.

Ms. Payne noted that our focus group discussions included analysts from think tanks and they were heavily into determining program costs. Analysts provide value by helping others understand the financial information.

The Board concluded the presentations for the day and will continue on April 24, 2014.

- **Reporting Entity**

Ms. Loughan directed the Board to Tab C, Reporting Entity, and explained that the Board would be considering the last of the technical issues raised during due process. As discussed in the memo, the Board will see the document with all changes at the next meeting. Ms. Loughan explained that of the issues for discussion, the first two issues relate to items discussed at the March meeting.

Staff explained the first issue regarding the component reporting entity misleading to include provision was presented in March. Staff explained that the proposal provided that in rare instances, it also may be misleading to include an organization that is administratively assigned to a reporting entity based on the principles provided. In such cases, the organization may be excluded. Based on the responses, a majority supported the proposal but a few suggestions were identified.

As discussed at the last meeting, PBGC (while supporting the provision) had contacted staff in an effort to clarify certain language. Also, some wondered how the language may affect the Offices of Inspector General. Therefore, the Board asked staff to research the item and make the necessary revisions to paragraphs 62-63 to ensure the PBGC example was covered while also cautioning against unintended consequences that may affect organizations such as the OIG.

Ms. Loughan explained staff recommended removing the example in paragraph 62, and also editorial changes to paragraph 63. Staff also included additional language to the Basis for Conclusions for the Board's consideration. Staff opened the discussion for questions and comments from members.

Mr. Steinberg asked if staff could explain how the proposed changes to paragraph 63B relate to the PBGC issue. Ms. Loughan explained that the changes were proposed because staff believed it would be clearer to suggest net costs versus liabilities. Mr. Steinberg explained that he still did not understand it. Staff explained the original wording may have misleadingly implied that the larger entity is responsible for the liabilities of the smaller entity despite the fact that a bureau usually settles its own liabilities. Therefore, staff believed it would be confusing to have that as an example and revised it to focus instead on whether consolidating the cost information relates cost to a shared strategic goal or to shared objectives or programs. Further, it is highly unlikely in these misleading to include cases that there is some alignment closely in the strategic plan or in the programs. Also, as a reminder, these are just examples.

Ms. Payne suggested staff clarify with editorial changes to remove the negative statements.

Mr. Steinberg suggested that PBGC and the Labor Department both have the shared goals of worker and retiree security. He asked if it was necessary to have the phrase no shared strategic goals or objectives. Ms. Payne agreed and stated that it could say the consolidated cost information for the new component would not be meaningful, something to that effect.

Chairman Allen asked if any of the members objected to the change and no members objected. Therefore, it was agreed staff would incorporate the change.

Mr. Showalter explained that he suggested the word ‘meaningful’ was not appropriate because it is not defined and he suggested using ‘misleading.’ Staff explained that they believed it was a good change and planned to incorporate that in the document. Staff explained that editorial changes will be included in the full document at the June meeting.

Mr. Dacey explained he had some editorial comments but he also had a question. He asked what changes were made to address the Inspector General issue discussed at the March meeting. Ms. Loughan explained that the example listed in paragraph 62 had been deleted (specifically, “in such cases, for example an organization may have been legally established…”). Mr. Dacey explained he generally supported the change but he thought there may be enough concern or confusion that the OIG could be perceived as a separate organization. He suggested explaining in the Basis for Conclusions that the Inspector General would be expected to be included with their respective entities. Mr. Dacey noted there have been a few questions regarding whether the OIG’s operations should be included within the entity. The response has been that it is part of the entity.

There was a brief exchange among members. Members agreed that the Basis for Conclusions should say OIGs would be included and would not be excluded under the misleading to include criteria.

Subject to the modifications discussed, members agree to the component reporting entity language to address the concerns with the misleading to include provision.

Mr. Granof noted some confusion regarding the meaning of paragraphs A18 and A19. Ms.Loughan noted that she would clarify A18 to refer to implementation guidance for the administrative assignments. Ms. Loughan explained the one-time review was referring to the first year of implementation that it is anticipated the component reporting entities will go through a lengthy process to determine the administrative assignments. The central agencies will provide guidance to ensure consistency. Mr. Granof explained that A19 does not make it clear as to what one is supposed to review. Ms. Loughan explained that it referring to the three areas identified, but staff can add language to make it clearer. Staff agreed to make it clearer that it is a one-time review of the administrative assignments.

Ms. Loughan directed members to the second issue- Organizations Partially in the Budget-Museums. At the March meeting, staff had presented the issue of Organizations Partially in the Budget and explained that certain entities, such as museums, are partially on budget--meaning a substantial portion of their funding is from federal appropriations included in the budget and the entity receives private support (such as donations) not included in the budget. Staff explained these types of entities include the Smithsonian Institution and the US Holocaust Memorial Museum.

Staff explained these entities currently present the budgeted portion as ‘federal’ or ‘appropriated funds’ and present the other funding as ‘non-appropriated,’ or ‘trust funds’ in their stand-alone reports. However, only the budgeted portion is included in the US Government-wide financial statement. Generally, the component reporting entity financial statements are presented using the FASB’s non-profit formats. The statements present federal funds, donor funds, and total funds (consolidated) in columns. Amounts are identified for restricted and unrestricted funds.

Although staff had met with representatives from the US Holocaust Memorial Museum prior to the March meeting to discuss their comment letter and concerns, the Board requested that staff also reach out to the Smithsonian Institution prior to finalizing this area. Staff understood that most members continued to support including the organizations as a whole (that is, not “splitting the baby”) and approved language in the Basis for Conclusions to explain that the funds from dedicated collections would prevent misleading presentation of funds not available for general purposes. Thus, the only open issue is whether the standards are sufficiently clear that all funds would be included. Ms. Loughan explained that staff met with the Smithsonian and summarized the results of the meeting but there is a clarification.

Ms. Payne explained that Ms. Loughan and she met with the Smithsonian representatives to clarify that they understood that if the Smithsonian were included it would be included in its entirety- both donated and appropriated funds. She explained that staff left the meeting with shared impressions that they understood that. During the course of the discussion, we also discussed whether they would be consolidated or disclosed, and that is mentioned in the memo. The Smithsonian was contacted by their auditor. Smithsonian asked it be clarified that Smithsonian did not agree with two statements in the staff summary. Therefore, they did not concur with these two statements:

> “However, it was agreed that the funds are managed by the federal government because generally there is an authorization for the contributions and there are federal officials that have oversight of the private or donated funds.”
>
> “The representatives were comfortable with the proposal, even with the understanding that they might be a consolidation entity and understanding that GAAP may allow for presentation alternatives that display restrictions on certain funds in the consolidated government-wide financial statements through existing standards.”

However Ms. Payne noted she did confirm the Smithsonian representatives understood that it is clear in the standards that it would be the total organization included, not just the appropriated money, no matter how they are classified.

Chairman Allen confirmed that this would not change the way they reported the agency themselves and that is a point we tried to make to them. Ms. Payne agreed but noted that they did not agree with a point in the summary that indicated the “funds are managed by the federal government because generally there is an authorization for the contributions and there are federal officials that have oversight of the private or donated funds." Ms. Payne explained they were also uncomfortable with the second sentence that implied they were a consolidated entity by stating they might be a consolidation entity. They simply want the minutes to reflect that they do not agree with the staff memo.

Mr. Bell explained that he noticed staff highlighted some concerns with respect to collection of information through the GTAS system of Treasury. His understanding from checking with the Fiscal Services is that there is not a major concern about the ability to get at this information. Staff explained the concern was cited by the Smithsonian representatives and related to whether GTAS would be able to accept the information for the donor funds as it was Smithsonian's impression the system would not be capable of doing so. Staff believed this to be a system issue and followed up with the appropriate personnel at Treasury, who were very responsive to the inquiries. Staff communicated this concern with the appropriate Treasury /GTAS specialists. They followed up on the matter and we were informed that GTAS accepts all valid treasury account symbols (TAS).

Ms. Payne reiterated the primary reason for the meeting with Smithsonian was to confirm their understanding that both appropriated and donated funding would be included if they meet the inclusion principles. We also discussed with them the applicability of the dedicated collection standards so that it would be clear that those funds are not available for general use.

Mr. Steinberg explained he had a concern. His concern is that what we are looking for, which is that they report the entire entity to the Treasury Department, and that the Treasury Department reports the entire entity either as a consolidation or disclosure entity; is in the basis of conclusion and not in the standard. He explained that the Board should write standards to say what they should be. He explained the auditor had said to him that he thinks it should be in the standard so that there would not be any question when they do the audit. Mr. Steinberg explained that at the last meeting, it was suggested he provide a paragraph or a sentence for the standard. Mr. Steinberg explained that if the Board believes an entity should be reported in its entirety, then we should say that in the standard. His proposed language is:

> [The first paragraph, which addresses that the museums are "in the budget" he proposed to go right after the current paragraph 22.]
>
> Certain organizations created by Congress as museums or performing arts organizations are in the budget, but are also authorized to receive donations, either directly or through affiliated entities, from persons and organizations outside the Federal government. Although these organizations are often characterized as "partially in the budget," the entire organization should be included in the government-wide GPFFR, that is both the portion funded through the budget process and the portion funded by donations.
>
> [The second paragraph is intended to assure that these organizations are reported in their entirety. It would go right after the current paragraph 53.]

> The GPFFR, in reporting entities considered "partially in the budget," should include, either through consolidation or disclosure whichever is applicable, the entire entity, and not just the portion considered "in the budget."

Chairman Allen explained he thought the standard called for that. Ms. Loughan explained that the Board discussed the issue before, and decided the standard did not need to address it, instead a footnote was added--footnote 35 to paragraph 64. The Board also previously determined to add the detailed explanation to the basis for conclusion. The discussion is referenced in the minutes that is included in appendix.

Mr. Steinberg explained that he believes if we have a standard, it should be in the standard not in the footnote. Mr. Showalter suggested he was not sure he understands Mr. Steinberg's point. Paragraph 64 and footnote 35 appear clear. Mr. Steinberg explained that the standard should say what we expect to happen. Mr. Showalter explained that he believes paragraph 64 does. Mr. Steinberg explained that paragraph 64 addresses consolidation entities. He explained that some of the partially-in-the budget organizations may be disclosure entities so there needs to be some clarity for those.

Ms. Payne suggested that one person's clarity is another person's rule instead of principle. She explained that what if there is a museum for which there is a listing as we have had with things like Howard University and they list the name, they appropriate money, but it otherwise does not meet the inclusion principles and we have provided an out for that. Ms. Payne explained that she did not see the need for the specificity because it is more like a rule than like a principle and has the potential to be confusing.

Ms. Loughan explained that we met with two museums and those meetings indicate that they read it and understood it. The wording appears clear and there is the explanation in A-19 in the basis.

Chairman Allen suggested it may be something we have to vote on and he appreciates Mr. Steinberg writing language. He thought some of that language could go in the basis of conclusion.

Mr. Steinberg asked if you want something to happen and this is something different than current practice, why would you put it in the basis rather than in the standard. Mr. Steinberg explained we are setting a bad precedent if we try to establish standards in either footnotes or in the basis for conclusion. Mr. Steinberg explained that he believed it was important to address in paragraph 22.

Ms. Payne explained paragraph 22 is about organizations included because they are in the budget. However, Mr. Steinberg's addition talks about things that are partially funded, and identifies them as museums or performing arts, certain organizations created by Congress but we have not tested "created by Congress." We have not tested to see are there many other things besides museums and performing arts that are partially funded. This is a very complex standard, and it is difficult to see the value to adding this to paragraph 22.

Mr. Steinberg suggested this is a principle-based standard and we are not writing for individual things. However, museums and performing arts partially in the budget is something we have been concerned about from the beginning of the project, but have not addressed in the standard. Staff believed it had been addressed in their view in the standard, and that is why they object to adding more wording that has not been tested, and could be confusing. However, staff noted this is an issue the Board needs to decide.

Mr. Dacey asked if the concern was how the term “organization” is defined, that some people might perceive that term in Smithsonian’s instance, to be just the federal portion as an organization?

Mr. Steinberg explained it is “organization” and then it goes on to say where their funding will come from, and the same with the Holocaust Museum. Mr. Dacey asked if people will clearly understand we mean the entire organization. Mr. Steinberg stated he believed that the language he wrote was pretty clear. Mr. Dacey explained, although he understood the concept, he had some concerns about the specificity and limitations to these particular types of entities. Because the Board is saying that “organization” means the entire organization, even if part of it is funded through other sources. If we did add something, it should be at a very high level as opposed to specific programs. He explained he had some concern for footnote 35 being applied only to the consolidation entities, and maybe it should be applied to “organization” when we first start the process of determining organizations to include.

Mr. Dacey suggested clarifying how “organization” is defined and that it means the entire organization and put it up front, perhaps in footnote nine where organization is initially defined. He explained that is where the decision is made to include or not. Mr. Showalter agreed and explained it would cover bother consolidation and disclosure. Mr. Dacey agreed and stated it would clarify that it meant the whole entity.

Ms. Payne confirmed that it benefits from having that wording associated with footnote nine to clarify. Instead of the wording that Mr. Steinberg introduced, staff will use similar language to that in footnote 35 that it is already relatively settled. The Board agreed to put something short and to the point in footnote nine and footnote 35 should remain and tie back to nine accordingly. It was agreed the changes to footnote nine and 35 would be considered editorial and reviewed at the next meeting.

Chairman Allen asked if the Board agreed with staff’s proposed language to the Basis for Conclusions to explain organizations partially in the budget. He noted by seeing no objection, the Board is in agreement with the language and that staff will add language to footnotes nine and 35.

Ms. Loughan explained the next issue for discussion would be related parties. She explained that the Board proposed a definition of related parties and disclosures for related parties where the relationship is of such significance that it would be misleading to exclude disclosures about the relationship. To recap the response, the Board asked respondents if they agreed or disagreed with the related parties definition and requirements. Nineteen respondents generally agreed with the proposal and one disagreed (19 respondents did not answer the question). The Board also asked respondents if they agreed or disagreed with the list of the types of organizations that generally would be considered related parties. Nineteen respondents generally agreed with the proposal and one disagreed (19 respondents did not answer the question).The Board also asked respondents if they agreed or disagreed with the list of exclusions. Eighteen respondents generally agreed with the proposal and one disagreed (20 respondents did not answer the question). The Board asked if there were additional exclusions that should be considered. Staff notes the Board discussed the universe of entities the federal government may have relationships with and where significant influence may exist as there could be countless relationships considered. The Board agreed the best approach would be to develop parameters – certain classes of relationships and specific types of entities that would generally be excluded. The Board spent time discussing government sponsored enterprises and multi-lateral development banks and determined these to be types that may be related parties.

Ms. Loughan explained that there was a series of issues to review related to the topic, but staff could discuss them individually.

Ms. Loughan explained the first question appears on page 15, and that one is Treasury's suggestion to insert the word 'certain' in paragraph 85B. Staff believes the word 'certain' should be inserted in front of multi-lateral development banks so as not to make the presumption all would be related parties. Though staff believed the word 'generally' would cover it, it may be a good idea to add this as well. Therefore, staff recommends paragraph 83b. be revised as follows:

> 83b. Organizations governed by representatives from each of the governments that created the organization, including the United States, wherein the federal government has agreed to ongoing or contingent financial support to accomplish shared objectives (for example, <u>certain</u> multi-lateral development banks).

Mr. Steinberg asked what is meant by certain. Mr. Showalter stated 'not all.'

Ms. Loughan explained that as the memo noted, the proposed language has 'generally' and even though it seemed like that might have covered it, staff did not see any harm in adding the word certain based on the response. This request came from departmental Treasury staff, and the request was that they did not want it to appear that all multi-lateral relevant banks are now and forever considered by the Board to be related parties. And we did not intend that either. We are fairly cautious with making examples.

Mr. Reger asked if a multi-lateral development bank met the other criteria, then that would be the determinative factor. Ms. Payne agreed and nobody gets out because of the word certain. Mr. Reger so if there were a multi-lateral development bank which did not meet the criteria by the reference here; it would not have to be, so there is no foul?

Chairman Allen asked if any Board members object to adding the word ‘certain’ and seeing none, he noted there was agreement.

Ms. Loughan explained there was an inconsistency with some of the language. Staff recalls that earlier versions (see June 2012) of the proposal had “financial and operating” in both par. 79 and 80. The change was a staff edit based on internal discussion of the types of policy decisions that would be both “financial and operating.” Some staff believed capacity to make significant operating policy decisions would almost always be linked to also making financial policy. Others believed the requirement that there be both financial and operating policy decisions would be limiting. That is, a decision maker could be solely involved in operating policy and have “significant influence” but not be considered a related party. Staff concluded that the adjectives were not meaningful given the difficulty in applying them and the potential that the form of decisions may vary but not the substance. (Staff recognizes that conforming changes to paragraph 79 were equally warranted based on this logic, and these words will be removed from paragraph 79.) So that is what we are recommending in paragraph 79, a conforming change.

Chairman Allen noted that it appears the Board has already agreed to this, so it should not raise any concern. If there are no objections we will move on. There were no objections.

Ms. Loughan explained the next issue relates to an NSF request that the exclusions paragraph be modified so that the standard clearly denotes that NSB members as individuals, or the entities they are affiliated with, are not in related party relationships with NSF. [Staff notes paragraph 84c) indicates that “key executives of the federal government and organizations owned or managed by key executives, other employees of the federal government, or members of their families” are not related parties.] NSF and NSB suggested that “FASAB explicitly add in 84c) “Presidentially appointed agency board members” to the list of exclusions. Alternatively, paragraph 84b) could be expanded to state “This exclusion also applies to management and board members of institutions that jointly serve on the board of a federal agency. This occurrence does not result in a related party relationship between the federal government and the individual or the federal government and the affiliated institution.” Furthermore, NSF requests that FASAB add the term “that may or may not” to paragraph 84 b) as: “Organizations with which the federal government transacts a significant volume of business that may or may not result in economic dependence such as….”

Staff noted in the public hearing discussion, it appeared the concern was more with the term “related parties” based on private standards and that transactions may not be arms length. The discussion conveyed that the NSF currently discloses information and is very transparent about the award amounts and so forth and describes them as affiliated with board members. Staff noted that certain FASAB Board members noted concern with excluding them all together and some hesitation with the additional language because there could be situations where you have members of your board receiving material amounts of grants, it would be relevant to disclose that.

Staff's review of the NSF FY2013 financial statements found that NSF includes disclosures related to these types of relationships under Note 15: Awards to Affiliated Institutions. The note provides the total amount of the award and a high level description. It also provides a brief description of the conflict of interest rules and other framework. An appendix (not part of the audited financial statements) to their report provides a table listing the institutions affiliated with members of the National Science Board and awards obligated. A footnote to the table describes the purpose of the table is to provide open and transparent reporting. It also describes the framework that the NSF and the NSB operate under.

Staff explained while it appreciates the NSF concerns, staff does not believe it would be appropriate to add language to fit the specific circumstances they identified. It appears the proposed standard provides the proper exclusions and it may be more of a concern that NSF has with how its presentation may be interpreted. However, FASAB agreed that 'related parties' is a generally accepted term and though it does not apply in the same way in the federal government, it was preferred to define it in our context versus developing a new term or making a definitive statement that we do not believe there are related parties to the Federal reporting entity.

Staff explained that once the standard is issued, 'related parties' in the federal environment will have its own benchmark and the auditors will audit based on the federal standards. As for other concerns that items listed as related parties may be interpreted by outside parties to lead to other than arms length transactions, the proposed standards do not prevent an entity such as NSF from labeling the related parties as "Affiliated Institutions" as they have done in the past and explaining the conflict of interest rules.

Staff explained if members believe that relationships such as the NSB do not warrant consideration for related party disclosures, staff believes the reasoning would be similar to that applied for key executives (par. 84c). That is, conflict of interest and other ethics requirements (such as financial disclosures) address the significant influence concerns associated with related parties. If a broader approach is needed, staff believes par. 84c could be revised to acknowledge that generally those "individuals covered by conflict of interest regulations such as key executives, organizations owned or managed by key executives, other employees of the federal government, or members of their families" would not be related parties.

Therefore, staff explained the Board has two options and should vote on the best approach—

Option A- Address in the Basis for Conclusions

The option would be if the Board believes it would not be appropriate to add additional language to the standard. Instead, the basis for conclusion would include the following additional paragraph:

AXX. During its due process, the Board considered a request that 'related parties' language be modified to clearly denote that members appointed on boards as individuals, or the entities they are affiliated with, are not in related party relationships with the departments or agencies. The Board did not believe additional language was necessary for several reasons. Most Board members believed the appropriate broad classes of exclusions were provided. Certain Board members also noted concern with excluding all such members because there may be situations where disclosures would be appropriate. Further, based on current practices it appears much of this type of information is being reported. However, the Board understood the concern with the understanding of the term 'related party' as commonly used in financial reports to imply less than arms-length transactions. The Board believes once federal standards are issued, the term 'related parties' in the federal environment will have its own implications - that is, a focus on exposures to risk of loss or potential gain as a result of the relationship. The proposed standards do not prevent an entity from labeling the related parties as "Affiliated Institutions" or any other term appropriately descriptive. When doing so, it may be important to explain the relationships by including information such as conflict of interest rules and other frameworks they operate under.

Option B- Revise paragraph 84c.

This option would be used if the Board believes relationships such as NSB do not warrant consideration for related party disclosures. Staff believes the reasoning would be similar to that applied for key executives (par. 84c). That is, conflict of interest and other ethics requirements (such as financial disclosures) address the significant influence concerns associated with related parties.

Mr. Dacey explained NSF's issue gets back to the definition of key executives of the federal government and would that encompass the people that are the Board members?

Ms. Payne explained that she was not sure we need the word because all employees are covered by conflict of interest, therefore we could change key executives to employees.

Mr. Dacey explained when he sees "key executives" of the federal government, he thinks of federal government employees and these Board members are not "traditional" federal government employees. Ms. Payne explained that she believed they are special government employees. Ms. Payne explained the Board members would be key executives of FASAB and are also special government employees. The reason it is structured that way is to subject members of boards to the conflict of interest laws.

Mr. Showalter noted he was a bit confused with the rewording and whether the key was "key executives" or "covered by conflict of interest regulations." He was not sure which the decision point was and it seemed broader now.

Mr. Dacey asked if it was true that all key executives are, as defined are covered by conflict of interest regulations, but there may be others that are covered by such regulations. Mr. Showalter suggested that he would assume any employee is covered by conflict of interest and he did not know if that was intentional or not. Ms. Payne explained that you are only considering it in isolation, in the related party piece the person has to rise to a pretty high level of influence to be considered for related party disclosure.

Ms. Payne explained that Ms. Loughan endorses the Basis for Conclusions and she did not object to that. However, considering the early discussions of related parties, the reasoning was conflict of interest laws meant that related party information about employees of the government would not be valuable in a financial statement. Therefore, it appeared a very simple fix would be to clarify the intent C served. That said, in reviewing the National Science Foundation disclosures about their board members, they were good disclosures and really either option provides a good alternative or perhaps there is something in the middle.

Mr. Showalter suggested that A is different than B, in that B turns on the conflict of interest. A is not dependent upon them having a conflict of interest and that is why he preferred A because it was broader.

Mr. Bell explained his first reaction were these two options are mutually exclusive? But A is preferable, and it seems -- it would seem to give NSF auditors -- there seems to be enough there to provide assurance parameters. While his initial reaction was is there room for both? They did not strike him as immediately mutually exclusive. But having thought about it some more, his preference wound up being for A, the basis for conclusion language.

Mr. Dacey stated he was a bit concerned, as he reads paragraph 84c as drafted, it states the following would generally not be considered related parties. Therefore, with the proposed changes, it appears it would include key executives in federal government, which we said would be the board members, and organizations owned or managed by them. Would that be their affiliated organizations, which could be in the case of NSF the grant recipient? Ms. Payne explained that 84(c) would not absolutely preclude it because it is preceded by generally but would imply that they are not. That would give leverage to not reporting them as affiliated organizations. And that is the difficulty, because right now the NSF disclosures seem helpful.

Mr. Dacey explained that he agrees that it may be helpful and there are other entities with similar situations that are disclosed. That practice has been driven by the auditing standards and not by the accounting standards. His concern is this could end valuable disclosure. So, he preferred Option A for that reason. However, after reading the basis he was expecting to see an indication that these entities may be related parties. If you read 84(c) ,it would seem to say they are not reported.

Mr. Dacey suggested that Option A could be expanded to acknowledge the decision should be based upon the facts and circumstances. Mr. Reger explained that it is a matter of fixing B or expanding A.

Mr. Dacey explained he was not sure because he prefers the general concept of A, but not the specific language. He does not think option A clarified the issue that maybe they will need to be reported. He thinks that would depend on how it is read in connection with 84(c).

Mr. Steinberg explained he did not believe 84(c) addressed this at all because it says key executives of the federal organization and organizations owned or managed by key executives. Mr. Steinberg explained that he would say all the people on the NSB Board are not owners or managers of those universities, but may be employees. He explained there should be disclosure regarding the relationship between the NSB members and the NSB because you can say they are not involved in decisions, but their presence on that Board gives them influence when NSF is making grants. He explained that the Board should not write anything that prevents the disclosures we have now because that would be doing a disservice to full disclosure. Mr. Steinberg explained he supported option A, the basis of conclusion language but questioned if that will be enough to ensure that they continue to do what they are doing now?

Mr. Dacey explained he may be in agreement but he is not passing judgment on whether or not they have influence. There is a relationship that readers should be aware of. Mr. Steinberg agreed and suggested that Ms. Loughan’s draft language for the basis to the point; laid it out very well in that paragraph. Mr. Steinberg only questioned if disclosures would continue.

Mr. Dacey agreed and stated that was his concern. He wondered whether or not a change to balance this was necessary in paragraph 84. Mr. Dacey explained that NSF has raised this issue and indicated that they would like to remove the disclosures. His understanding from the comments is that the Board needs to make it extremely clear, if that is the Board’s position, that the disclosures should continue. Mr. Steinberg noted agreement, along with other members.

Ms. Payne acknowledged that staff has direction from the Board that they have a preference that the current disclosures regarding related party (affiliated organizations) at NSF continue. Staff will consider wording within the body of the standard to make it clear. Staff will work with general counsel and Board members to determine appropriate language that would be clear that 84 is not inclusive of special government employees and would still include the affiliated organizations.

Chairman Allen suggested that it is really a mixture of option A and B and the change will ensure the current NSF disclosures continue. Ms. Payne agreed and that staff would seek input from certain members and that it would be included with the rest of the changes in the complete document at the next meeting.

Ms. Loughan explained the next related party area deals with the component reporting related party information. Staff explained that KPMG noted that paragraph A84 was confusing and they did not understand why this statement should defer to OMB for additional disclosure requirements for related parties. They believed this statement should be all inclusive of the required related party disclosures or the Board should consider a separate standard to address related parties.

Staff noted that at previous meetings the Board discussed in great detail how component reporting entities work together to accomplish goals but are not considered related parties. The Board also deliberated the issue of whether component reporting entities should disclose additional information to better recognize the relationship and contextual information that is conveyed about the component reporting entity of a sovereign government. FASAB has not established requirements for a description of the component reporting entity other than the discussion of the organization and mission required in the Management's Discussion and Analysis section (MD&A). Nonetheless, most key points are addressed individually in agency MD&A and notes either as a result of existing standards, OMB form and content requirements, or voluntarily. However, coverage and placement differs among agencies.

This was conveyed in paragraph 82 of the Related Parties language and paragraph A84 of the Basis for Conclusion. Staff recommended changes to clarify paragraph A84 regarding the fact that component reporting entities are not related parties under federal standards and that addressing additional disclosures is beyond the scope of this project. Staff believes these points would be clearer without the reference to further guidance from OMB and would address the point made.

Mr. Dacey asked if the draft was intending to refer to anything other than intra-governmental transactions, which are defined in our standards and for which there are disclosure requirements beyond those listed in the paragraph. He explained that this may be confusing to many people reading it. If we mean intra-governmental, it seems that we ought to refer to it in this discussion. Mr. Dacey noted the draft uses the word "component", which would imply that you have got a piece of the whole entity, and wanted to clarify if the Board intended to go beyond intra-governmental.

Ms. Payne acknowledged that we have not directly said "intra-governmental" entities are not related parties. She noted the text also meant disclosure entities are not related parties either. Mr. Dacey stated he understood that and that would not fit the common control issue here.

Chairman Allen noted the issue was the concern of us referencing OMB and we were just trying to get rid of that. He noted the length we are going to address each response. Chairman Allen explained that Ms. Loughan has gone way over to what is normally expected due to the nature of the project and that is why we are having these kinds of discussions. He did not think the Board should give too much weight unless there is a fatal flaw or something that we should be aware of, but this is a case where we were simply trying to omit the OMB reference and write that in a more generic way.

Ms. Payne suggested this paragraph was included in the Basis for Conclusions because we were proposing to depart from practices of other standard setters. The only comment was regarding the reference to OMB. Another option is that we just drop the whole paragraph since it really is not necessary as it was not controversial. Chairman Allen agreed and stated it would not offend the party that commented.

Mr. Dacey said he did not have a problem with the paragraph, he was just asking more for clarity. Mr. Showalter asked if it is needed for implementation. If it is not, then it can be dropped. Ms. Payne explained that she did not believe it is needed.

Chairman Allen explained the reason it was included was that there may be a common understanding, and we are departing from that. In our environment we are applying something a little bit different. He thought it a helpful explanation to have. Therefore, he would probably vote to keep the explanation of why we are not doing it the way other people are doing it but not making specific reference to OMB. However, if others prefer to drop it, that would be fine as there may be no harm.

Ms. Payne asked if Mr. Dacey believed it needed to be edited for clarity. Mr. Dacey explained he was generally happy with the paragraph but wanted to note that intra-governmental transactions are not related party transactions. Ms. Loughan suggested a footnote or other clarifying language could be added to the paragraph regarding intra-governmental transactions.

Chairman Allen asked if any members objected. All members agreed to the change along with the footnote to address intra-governmental transactions.

Ms. Loughan explained the remaining series of issues regarding related party raised by respondents are presented for the Board's consideration but based on staff's analysis of the issues; staff did not recommend any specific changes to the proposed standards.

Ms. Loughan explained the first issue noted concerns that led them to suggest a separate standard should be considered for related parties. The second issue noted concern with differences between a disclosure entity and a related party. The last area a respondent raised some concerns about the use of the term 'related parties.' Staff reiterated they did not recommend any changes for those areas. And most of those areas the Board had actually discussed before.

Chairman Allen asked if any members disagree with the staff recommendation not to make changes. No members objected.

Mr. Bell noted that he did not have anything specific in mind, but there is just still some residual uncertainty where we draw the line between disclosure and related party and even misleading to exclude. He wanted to go on record as saying that we still have some uncertainty. There could be some clearer distinction there among those categories and perhaps there could be something in the Basis for Conclusions.

Mr. Dacey explained that to some extent coordinated guidance by the sponsors could be helpful in bringing clarity. If there are implementation difficulties, they could always be brought back to the Board. Mr. Reger explained there may need to be a mechanism for addressing that issue as they come up.

Mr. Dacey explained that is why he is suggesting that if we do not have specific changes that need to be fixed; maybe any implementation issues can be raised to the Board later . Mr. Bell understood and explained he did not have something specific in mind at the moment.

Ms. Loughan explained the last general question in related parties was after seeing all of the changes to this section if any Board members wish to offer any other changes to the related party language.

Mr. McCall asked about page 25's use of the term "operating cost and decisions," and he understood that we have already made a decision on that. His question relates to paragraph 87 where it talks about percentages of ownership in A, and it talks about financially related exposures in B. He asked if staff was comfortable with that use of financial and if that is far enough away from the term financial that it is not so financial related. Mr. McCall explained he was okay with the first part of paragraph 87. His concern relates to using financial terms where we have already eliminated the term financial and operating decision and whether that is consistent.

Ms. Loughan explained that we are using the term in different contexts. One was to describe the relationship and this is in regards to the disclosures. And as it relates to the disclosures, B states other information that would provide an understanding, and includes the example financial-related exposures.

Mr. Dacey noted he had a different concern over that in terms of ownership interest and an entity that would be considered in the related parties' category where the federal government has an equity ownership. He believes large equity interests would be included based on inclusion principles, but he does not believe a change is necessary.

Chairman Allen confirmed there were no other suggested changes to the related party language.

Ms. Loughan explained the next related to the conforming changes to Statement of Federal Financial Accounting Concepts (SFFAC) 2, Entity and Display, to rescind or amend language to remove criteria for determining what organizations are required to be included in a federal reporting entity's GPFFR from the concepts statement because criteria will be in a statement of federal financial accounting standards. The Board asked respondents if they agreed or disagreed. 20 respondents agreed and one respondent disagreed. After staff's review of the specific comments, staff did not see a need to make any specific changes to our amendments to Concept 2 amendments.

Mr. Reger asked if we have removed the provision to say how organizations that used to go to OMB for resolutions should now do it in accordance with these standards. Mr. Reger asked if the standard provided for how disputes would be resolved, and if there needed to be some resolution to that process.

Mr. Bell asked if that would be something to address in the standard or is that more implementation? Mr. Reger explained that is why he thought we were taking it out because we agreed then it would come through this process, and it is going to be up to the preparer and the auditor to make that decision.

Ms. Payne explained she believed that it is part of the Concepts 2 amendments. However, she is not sure how explicit SFFAC 2 is.

Mr. Reger explained he wants to be sure what the resolution is and the removal of that condition.

Ms. Loughan explained there is nothing in the current proposal that would direct someone to OMB. Mr. Reger explained he understood that, but absent that, it would be the preparer and the auditor who would decide. And in this case, that is Treasury, OMB and GAO, right? Just want to make sure that that is the interpretation of that. Mr. Dacey asked which paragraph he was referring to. Mr. Reger explained he did not have the details with him from SFFAC 2.

Mr. Reger explained he was fine as long as that is the interpretation that everyone has and we did not want to see individual organizations try to come back through the Board. Ms. Payne explained she did not anticipate that individual organizations would come to the Board unless the standards themselves are unclear.

The Board agreed that no specific changes were necessary to address comments or concerns in the SFFAC 2 Amendments. The Board also requested staff to provide a marked up copy of SFFAC 2 Amendments.

Ms. Loughan explained the next issue for discussion was the effective date. The Board proposed the Statement be effective for periods beginning after September 30, 2016. 18 respondents agreed with the effective date and 4 respondents disagreed. Two respondents believed the date should be delayed. One citizen respondent that disagreed believed the date should be sooner because political campaign years should not be influential in these decisions.

One respondent did not agree because they believed early implementation should not be permitted because it would lead to inconsistent reporting across federal reporting entities.

Staff explained that the early implementation should not be encouraged considering the government-wide guidance will ensure consistency.

Staff believes the draft implementation timeline was an anchor in determining the appropriate effective date. It provided for approximately 18-24 months implementation period. Based on anticipated milestones and the fact there is anticipated to be a coordinated effort from the central agencies to ensure consistency, staff explained it may be advisable to delay the effective day by one year to ensure there is a 24 month implementation period afforded.

Chairman Allen explained the main point is the timetable and we have discussed this at a couple meetings. He thought there was some question initially about is it really too tight of a schedule. Therefore he does not think any of the sponsors would disagree with that, but somebody else may have some questions about that. Chairman Allen asked if any members objected to extending it a year.

Mr. Dacey explained it is particularly important if we are talking about coming out in the September to December timeframe to the principals because it is unlikely that guidance could be developed in that timeframe. It probably would not be until February or March that the central agencies start on this. Mr. Showalter noted the agencies will not get around to it either because they are too worried about the yearend close.

Mr. Granof explained he would just note that we are not going to see these new statements until 2018, right, which is four years from now. Mr. Dacey explained that implementation activities would not start until calendar year 2015. Mr. Granof suggested that folks could get started today planning for it. Mr. Reger explained that there have been meetings with the Fiscal Service and talking with others for over a year now. However, to roll it out to the agencies and have them look through all their relationships and identify things with implementation is going to take awhile.

Mr. Steinberg explained that he believed identifying the relationships is not going to be difficult, but assessing whether it will be a disclosure or consolidation entity may be more difficult.

Mr. Granof questioned how many agencies would this affect and how many agencies that were previously not consolidated that will now be consolidated? Mr. Bell explained that will come through the agencies. Mr. Reger explained we did do some outreach after the public hearing, but the response we got from those people was do you have a standard? And we did make a number of changes after that.

Mr. Showalter noted another option is to leave the original date but be open to delay it. He explained he is not necessarily proposing that, but noting it is an option. Chairman Allen explained he is normally one who argues for early implementation and a tightened date with an option that we can push it back if we need to, but through this conversation he was convinced that this maybe a complex enough issue that it is going to take some time. Mr. Showalter agreed too.

Mr. Granof questioned if in another couple of years, the Board may be seeing a request for delay.

Mr. Reger explained that he and Mr. Dacey sat down and thought about this and scripted out some things, and Treasury has done some very deliberate things and initiated discussions on this. The real question is that this is going to be a fundamental change for a very long time. He explained there are other implications to calling some of these entities part of the federal government.

Mr. Granof explained he would certainly defer to his judgment, but at the same time, philosophically he is in the camp where he believes in having as quick an implementation date as possible, and then, if necessary, extend it a year.

Mr. Reger explained he would be happy to keep the Board abreast of progress. If we find the opportunity to do it sooner, we will be glad to let you know.

Mr. Granof explained that this happens to be an excellent standard. It is a major improvement. If we wait another year, it is not going to be the worse occurrence in the world.

Mr. Smith confirmed that we are not going to allow early adoption. Ms. Loughan explained that is correct because the central agency guidance is needed to ensure consistency.

The Board agreed to delay the effective date to periods beginning after September 30, 2017 and to not permit early implementation of the standard.

Ms. Loughan explained the next issue is the two non-authoritative appendices to assist users in the application of the proposed standards. The Flowchart at Appendix B is a tool that can be used in applying the principles established. The Illustrations at Appendix C offer hypothetical examples that may be useful in understanding the application of the standards.

24 respondents agreed that the appendices were helpful and should remain after the Statement is issued. (14 respondents did not answer the question.) One respondent disagreed or noted concern with maintaining Appendix C Illustrations. Staff noted there were a few suggestions for additional illustrations as detailed in the memo but staff offered reasoning for why these may not be needed.

Therefore, staff just needs the Board's confirmation that it would like to keep the appendices and whether or not the Board would like to add another illustration (such as for another intervention such as a conservatorship or receivership).

Chairman Allen explained he would argue strongly against having another intervention illustration as that key issue is going to be over this temporary, and we are not going to illustrate anything.

Chairman Allen asked the members if anyone believed there should be another example. He also requested agreement that all members agreed to maintain the appendices. The Board agreed both appendices should remain once the Statement is issued and no other illustrations need to be provided.

Ms. Loughan explained the last issue related to the comments received when we asked the respondents if there were any unique examples that they believed should be addressed in the statement or they believed that the standard did not address. Staff explained as detailed in the memo, there were several examples or specific situations that were provided.

Staff explained that the memo addressed each one of those individually and if the Board had any questions on those, we could discuss them. Staff also explained that after reviewing all the cases, no specific changes to the standards were recommended. However, staff recommended or provided the Board with an option of including a paragraph in the basis to say that we considered all of the examples or the Board could remain silent.

Mr. Bell explained that he liked the paragraph for the basis and that it at a minimum demonstrates that we are receptive and responsive to the agency.

Mr. Showalter agreed and thought it did especially since we addressed so many other comments.

Chairman Allen agreed and said it is not inconsistent with what we have already done.

Mr. Smith questioned if we would be setting a precedent that with future statements everything that comes before us now, we some kind of way need to address it? Or, if we do not address it, does it look bad?

Chairman Allen acknowledged that was a good point. He believes the process to make sure that does not happen is actually earlier than right now. The basis of conclusion normally explains what we have done -- we have done all of this.

Ms. Loughan noted that this issue may be important to include because it was a specific question we asked to respondents.

Mr. Smith agreed and said it is good that we consider them because it is a difficult standard and we want to make sure we get it right. He just questioned do we want to put in there that we considered it or do we just want to be quiet and not say anything?

Mr. Bell explained he believes Mr. Smith's point is valid. However, with the size and scope of this particular standard, it sets it apart somewhat from a number of the other issues we have dealt with and therefore it was an appropriate acknowledgement.

Chairman Allen asked if any other members feel strongly.

Mr. McCall noted he had a comment. He explained that it seems like we do really well in the first seven or eight sentences but then we come down to 'therefore the Board did not revise the proposed requirements in response to this input' seems to cut it too short.

Ms. Loughan acknowledged there have been some editorial suggestions from other members on that paragraph.

Mr. McCall suggested an edit to at least acknowledge that they are unique.

Mr. Dacey explained that he had some editorial suggestions to offer staff. His concern with the paragraph in Question seven was that it says we consider these unique issues but then says the Board does not intend to name or classify certain organizations. His concern is that we never set that up as one of the issues and it just seemed that we were replying to an issue we had not even raised. He questioned if it was necessary to put that part of the sentence in if we did not raise that as the issue we considered. Staff agreed to revisit the wording.

The Board agreed to include the paragraph in the Basis for Conclusion (subject to the changes discussed) regarding the consideration of examples provided by respondents during due process. It was agreed members should provide additional editorial comments to staff.

Chairman Allen asked if there were any other issues.

Mr. Steinberg noted that he did not know if it would be considered editorial or not, but it has to do with the conversion of FASB and FASAB entities at the component level and staff plans to present this in June. Ms. Loughan explained that it would be a small change and staff would present it at the next meeting.

Chairman Allen reiterated that staff is open to editorial comments. The formal vote on a pre-ballot draft will be after the June Board meeting discussion. Chairman Allen explained that at the next meeting the Board will see all changes in the document. At that time, everything discussed will be editorial changes.

CONCLUSION:

The Board agreed with the staff recommendations (subject to the modifications discussed) to the component reporting entity language to address the concerns with the misleading to include provision. [Changes included the Board agreed to drop the phrase “no shared strategic goals or objectives” from 63d. and to add discussion regarding the OIG should not be excluded from department financial statements to the Basis for Conclusions.]

The Board agreed with staff’s proposed language to the Basis for Conclusions to explain organizations partially in the budget. Staff will also add clarifying language to footnote 9 and 35 to explain the organization in its entirety is included.

The Board generally agreed with staff’s recommendations to resolve issues in the related party issue area. Specifically the Board agreed to:

- the revision to par. 83b. to clarify that not all multi-lateral development banks are related parties.
- the conforming changes to par. 79 (to drop the adjectives “financial and operating”) regarding policy decisions from the related parties language
- Staff will work with general counsel and Board members develop language to

be clear that 84 excludes people serving as special government employees but would still include the affiliated organizations. [a mixture of options A and B presented at the meeting]

- the changes to the Basis for Conclusions to address component reporting related party information, along with an additional footnote to address intra-governmental transactions.

The Board agreed that no specific changes were necessary to address comments or concerns in the SFFAC 2 Amendments. The Board also requested staff to provide a marked up copy of SFFAC 2 Amendments.

The Board agreed to delay the effective date to periods beginning after September 30, 2017 and to not permit early implementation of the standard.

The Board agreed both appendices should remain once the Statement is issued and no other illustrations need to be provided.

The Board agreed to include the paragraph in the Basis for Conclusion regarding the consideration of examples provided by respondents during due process. It was agreed any other members should provide additional editorial comments to staff.

The Board agreed to include the paragraph in the Basis for Conclusion (subject to the changes discussed in the meeting) regarding the consideration of examples provided by respondents during due process.

Board members should forward any editorial comments to staff. The formal vote on a pre-ballot draft will be after the June Board meeting discussion.

- **Leases**

Ms. Valentine opened the lease discussion by reminding the Board that most of the prior Board discussions have centered around the proposed FASB/IASB lease accounting standards and the GASB tentative discussions on revising their lease accounting standards. Since the Board has decided to defer any decisions on a federal lease accounting approach until the other standard-setting bodies are further along on their proposals, the current project focus is on intra-governmental leases and other federal-specific lease issues. Staff asked the General Services Administration (GSA) to brief the Board on its intra-governmental leasing activities. Staff also provided to GSA in advance several questions that could be addressed during their Board briefing.

Ms. Valentine thanked Mr. Gramp for coordinating the GSA side of the presentation. The GSA representatives introduced themselves.

- **Christi Dewhirst** - Financial Management Analyst, OCFO
- **Edward Gramp** - Director, Financial Reporting Division, OCFO
- **Sheldon Kravitz** - Financial Management Analyst, Office of Portfolio Mgmt.

- **Jane Pritchett** - Accountant, Financial Reporting Division, OCFO *(via telephone)*
- **Mark Sachse** - Supervisory Financial Management Analyst, FAS, OCFO
- **J. Kenneth Schelbert** - Director, Policy, Strategy & Delegations Div., Office of Leasing

Mr. Sachse began the GSA presentation by discussing the Federal Acquisition Service's (FAS) full-service fleet vehicles and total workplace leasing program. Mr. Sachse made the following points about the Fleet Vehicle Program.

- GSA operates a full service leasing program comprised of 200,000 vehicles.
- About one billion dollars in revenue
- All vehicle leases are treated as operating leases for budget scoring, and there are not specific MOU's or termination clauses for the majority of the services, also scored as operating leases for financial reporting.
- Termination clauses are drafted for most large vehicle consolidations and special circumstances.
- All services provided to customer agencies are fully reimbursable and a Replacement Cost Pricing component is factored into leasing rates.

Chairman Allen asked if the leases were intentionally structured to avoid capital lease scoring.

Mr. Gramp noted that in most cases it is a long-term arrangement, but there is usually no long-term commitment from the entity. The arrangements are very flexible. Also, in most every instance the vehicles are owned by the government.

Mr. Sachse continued his discussion with the Total Workplace Program.

- Total Workplace offers operating or capital leases to customer agencies for IT equipment and furniture.
- There are supplemental agreements to an Occupancy Agreement.

Mr. Gramp added that from a budget scoring perspective, A-11 has an exemption on intergovernmental transactions that as long as the lessor, in this case GSA, had fully acquired the asset, then the lessee or customer agency does not go through and have to apply the budget scoring rules it normally applied to capital lease and installment acquisitions.

Mr. Gramp gave an overview of the GSA Portfolio.

- 8,638 Active Leases – GSA is the lessee to a private sector lessor.
  - 8,632 Operating Leases
    - $5.61B Annual Rent
    - 194.8M Rentable Square Feet (RSF)
  - 6 Capital Leases
    - $0.04B Annual Rent
    - 2.7M RSF
- GSA Leasing Obligations – GSA has authority to enter into long -term Operating Leases without obligating for the full term upfront.

    - 40 USC § 585 …*the lease agreement may not bind the Government for more than 20 years and the obligation of amounts for a lease under this subsection is limited to the current fiscal year for which payments are due without regard to section 1341(a)(1)(B) of title 31*
- 21,107 Active Occupancy Agreements (OAs)
    - 10,141 Federally Owned
        - $3.90B Annual Revenue
        - 183.0M RSF
    - 10,966 Leased
        - $5.87B Annual Revenue
        - 194.9M RSF
- The majority of GSA's Occupancy Agreements (OAs) are Cancelable by the tenant agency at any time after the first year with 120 days notice.
    - 89% of all OAs are Cancelable
- A small number of GSA's OAs are Non-Cancelable by the tenant agency, meaning the agency has committed to paying for the space throughout the OA term.
    - 11% of all OAs are Non-Cancelable

Mr. Gramp clarified that all of the leases where GSA is the lessee is acquired space from non-federal entities and then assigned to federal entities. He added that GSA's agreements with other federal entities would not be viewed as arms length transactions.

Mr. Schelbert added that the leasehold interest in the property can range from a single point interest to a full 100 percent. Mr. Kravitz noted that GSA can have multiple leases in the same private sector building. Mr. Gramp stated that GSA has explicit authority to enter into long-term contracts up to 20 years without having to obligate the full up-front funding and includes an Anti-Deficiency Act waiver. GSA only obligates the annual amounts under the lease agreement. Mr. Schelbert added that GSA rarely enters into a 20-year firm term lease, but more often we enter into a 10-year firm term with two five-year options that allows for more flexibility. Ms. Valentine asked if GSA's explicit authority can be delegated to other federal entities. Mr. Kravitz replied, yes.

Mr. Steinberg asked if that explicit authority allows GSA to get a good price on the lease. Mr. Kravitz noted that the leases GSA enters into with private sector are legally binding contractual obligations backed by the full faith and credit of the United States government; this is not the same agreement that GSA has with its tenant agencies.

Mr. Gramp discussed some of the related GSA terminology.

- GSA's Occupancy Agreements (OAs) are technically referred to as Assignments of Space, not Leases. In general, GSA does not grant the broader enforceable rights as with a lease. There is also no standing to bring legal action against another federal entity.

- However, we recognize that from an accounting perspective these OAs can be viewed as Leases based on the FASAB definition of the term " Operating Lease".

- *An agreement conveying the right to use property for a limited time in exchange for periodic rental payments.*

Mr. Gramp added that 98 percent of all of the occupancy agreements are cancellable and almost always with 120-day notice. There is no fixed long-term, although they are intended to be multi-year, usually nothing less than 2 years. The small number of non-cancellable agreements are normally for a unique space assignment for an entity and it is almost always a whole building space assignment. Mr. Kravitz noted that the unique space would typically be a lease construction asset.

- *GSA's Financing*

  - *Please explain how GSA finances its operations (that is, appropriations, borrowing, third-party financing, agency reimbursements).*

    - The Federal Buildings Fund (FBF) is a quasi revolving fund that uses income derived from rent to finance activities.

    - Funds are appropriated annually and allocations place limits on FBF activities, including Rental of Space, which is used to acquire and administer leasehold interests in privately owned buildings.

    - In the past, GSA has had borrowing authority and has utilized the Federal Financing Bank (FFB) to refinance agency indebtedness; however, under the current scoring requirements borrowing would require upfront budget authority comparable to that required for using appropriated funds.

- *GSA's Role*

  - *What is GSA's role as landlord for Federal civilian agencies?*

    - GSA has jurisdiction, custody, and control of public buildings and the authority to acquire leasehold interests.

    - Our portfolio is mostly composed of office buildings, courthouses, land ports of entry, and warehouses.

    - GSA has authority to construct, renovate, operate and maintain public buildings as well as assign space to executive agencies.

Mr. Kravitz added that for property that GSA leases from private sector entities, the OMB scoring guidance precludes GSA from assuming ownership responsibilities.

  - *What types of real property needs at civilian agencies do not fall to GSA?*

    - Most post-office buildings, department of defense buildings (e.g., military installations), buildings located in a foreign country, and buildings constructed for a special purpose that are not generally suitable for use by another agency such as hospitals, prisons, schools and family housing.

Mr. Steinberg asked how involved GSA was with postal facilities. Mr. Kravitz replied that GSA's involvement is minimal with postal facilities – occasional interagency agreements.

- *Does GSA provide a full suite of landlord services such as maintenance and improvements?*
    - Yes, GSA provides a level of service comparable to that of a "gross lease" in the private sector in the GSA-owned buildings. In the leased buildings the private sector lessor provides those same services not GSA.

Mr. Kravitz led the discussion on GSA as a lessee.

- *GSA as a Lessee*
    - *What is the mix of Government-Owned versus Leased properties in your portfolio?*
        - GSA has a portfolio of approximately 378 million rentable square feet of which 48% is Federally Owned and 52% is Leased.
    - *When you lease facilities, is the lease classification for budget scoring generally capital or operating?*
        - The vast majority of GSA lease agreements are classified as Operating Leases for purposes of budget scoring. Capital Leases require congressional approval and upfront budget authority.
    - *Does the financial accounting classification usually match the budget scoring now?*
        - Yes
    - *How do termination clauses (e.g., termination for cause clause, fiscal funding clause, etc.) affect the classification of a lease?*
        - OMB Circular A-11, Appendix B, recognizes GSA's unique budgetary circumstance. "For Operating Leases funded by the General Services Administration's Federal Buildings Fund (which is self-insuring under existing authority), only the amount of budget authority needed to cover the annual lease payment is required to be obligated."
        - Consequently, GSA does not include termination clauses or availability of funds restrictions in longer term lease agreements

due to GSA's legal authority in 40 USC § 585(a)(2). Termination clauses are still used to minimize vacancy risk for planned relocations to alternative space.

- Note: For agencies other than GSA, lease agreements must contain termination clauses for Operating Lease treatment. In addition such agencies must budget up front for the costs of termination in addition to the annual rent.

- *What factors influence your decision to lease versus buy to meet a particular need?*
  - The lease versus buy decision in most circumstances is based on the following:
    - Agency needs
    - The availability of funds in the context of competing budgetary priorities
    - What the market offers in purchase opportunities
  - Purchase options - Can be included in the leasehold interest. This is primarily used for office space.
  - Federal construction - Better suited to more specialized Federal requirements, such as land ports of entry, courthouses, and installations for high security agencies.
  - Economic analysis typically shows ownership to be more cost effective than leasing, but GSA recognizes that leasing enables us to more quickly respond to changing market conditions and tenant requirements.
  - GSA considers not only our rate of return, but also our portfolio mix and tenant mission when making lease versus buy decisions.

Mr. Shelbert led the last topic of GSA as a lessor and then GSA as an assignor (not as lessor).

- *Do you enter into lease agreements that bundle other services such as maintenance or parking? Does this pose any special accounting challenges now? Are you able to obtain a breakdown of the various costs inherent in the lease payment?*
  - GSA typically enters into fully serviced leases that include maintenance and may include parking based upon client agency requirements.

- Due to the fact that 73% of GSA's leases are for fractional space in a building, the majority of GSA's leases (94%) are fully serviced.
- GSA does not consider maintenance and parking as separate, additional services, rather they are part of the leasehold interest. GSA does receive a cost breakdown comprising utilities, janitorial, and maintenance as part of the lease and this is considered as part of the cost and price negotiations during lease procurement.

Ms. Payne asked if GSA would be able to determine the interest rate implicit in a new capital lease. Mr. Gramp replied that generally, having the additional cost breakdowns provided one can distinguish between the capital and the operating component of the lease payment stream and determine the implicit rate calculation. Mr. Schelbert added that of the overall land and real property holdings of the government, the Department of Defense holds 80 percent, the Postal Service holds 8.5 percent, GSA holds about 9 percent, and the rest is spread over agencies such as NASA and others that have the statutory authority. Of those holdings, about 10 percent of the 3.35 billion square feet that the government controls is leased. GSA and the Postal Service are the two major lessees of privately-owned leased space. Also, 96 percent of GSA's leased space is leased on the behalf of other federal entities that do not have the authority to acquire leased space.

- GSA is an Assignor, not Lessor, when dealing with other Federal agencies. This authority is found in 40 USC § 584 "the Administrator of General Services may assign or reassign space for an executive agency in any Federal Government-Owned or Leased building." GSA has the contractual leasehold interest in the leased space.

▪ *GSA as an Assignor*

- *Are occupancy agreements with other Federal entities considered legally binding documents?*
  - OAs are interagency agreements that are administratively binding; however, they do not rise to the level of being legally binding. The OA memorializes the rent so that entities can budget for it in the out years.

Mr. Steinberg noted that for purposes of the lease accounting standard, the Board will have to remove the distinction between administratively binding and legally binding – meaning substance over form.

- *What terms are usual in intra-governmental leases?*
  - There are no intra-governmental leases. GSA is the lessee and assignor; the tenant agency is the assignee.

Mr. Granof asked if the lease terms between GSA and a federal tenant entity are similar to those between GSA and private lessor. Mr. Schelbert stated that it is a direct pass-through with the exception of GSA's 7 percent fee (for a cancellable 120-day give-back clause) or 5 percent if it is non-cancellable. Mr. Gramp added that financially it is a pass-through, but the commitment of the length of the lease is very different. The lease agreements are generally 10 years between GSA and the private lessor while the occupancy agreement with the tenant entity is cancellable after the first year with a 120-day notice.

Mr. Schelbert continued the discussion of GSA as an assignor.

- *Pricing (how are prices established)*

    - Leases are generally awarded after conducting a competitive lease procurement for leased space based upon the lowest priced technically acceptable offer. GSA seeks to award leases at or below prevailing market rates.

    - In rare cases, due to client agency requirements or scarcity of offerings in the market, GSA may conduct a sole source procurement - although price reasonableness must be established in those cases.

    - In either case, the negotiated lease rent plus a GSA fee are charged to the tenant agency. Occupancy Agreements between GSA and tenant agencies memorialize the rent rates and monthly rent bill for tenant agencies.

Mr. Showalter noted that the GSA financials show that it cost GSA more for the leased building than what is received. Mr. Gramp stated that the difference is primarily due to imputed costs, rent abatements and free-rent periods.

- *Leasehold improvements (advance funded or spread over the lease term)*

    - Tenant improvement allowances are negotiated in the lease contract to make the space ready for occupancy based upon client agency requirements.

    - Tenant improvements above the allowance are reimbursed to GSA through a Reimbursable Work Authorization.

- *Cancellation or termination clauses (with or without penalty)*

    - In the vast majority of leases, GSA awards a lease that contains a firm term with no termination rights.

    - The base firm term of the lease (typically five to 10 years) may be supplemented by an option period that GSA - based upon tenant agency requirements - may choose to exercise. Often termination rights, with a period of notice to the lessor, may be exercised during the option period.

Mr. Showalter asked if in the instances when a tenant entity vacates a space and it is difficult to lease out the space to another federal entity, can GSA sublease the space to a non-federal entity? Mr. Gramp noted that GSA does not normally sublease to non-federal entities but does have the authority to out-lease.

- *The option to avoid termination penalties if another Federal agency assumes the lease*
  - GSA, as the lessee, maintains assignment rights in the leases it acquires. If a tenant agency (assignee) vacates a lease, GSA may backfill that space with another Federal tenant.
  - Termination penalties would only apply if the lease was terminated, requiring a buy-out of the lease.
- *Other services included with the lease (maintenance, annual improvement allowances)*
  - Most of GSA's leases are fully-serviced.

Mr. Gramp continued the discussion on GSA as an assignor.

- *How do these terms affect classification by the lessee agency?*
  - GSA interprets the lessee agency as itself and a tenant agency who pays GSA to occupy space leased from a private sector lessor as the assignee.
  - The charge is a pass -through to enable GSA, as lessee, to pay for the space provided by the private lessor.
  - Occupancy Agreements define the terms of this relationship between GSA and the tenant agency. However, in the event of a dispute, there is no standing to sue, since both GSA and its tenant agencies are United States Government entities.

Mr. Gramp stated that OA's normally display a five-year term although there is still only an annual agreement for binding purposes. The purpose of the five-year display is to show the out-year information for budgeting.

- *Are intra-governmental agreements usually classified as Operating Leases?*

    - All GSA leases are entered into with non-federal entities. Agreements between GSA and tenant agencies are not leases, and therefore, are not subject to classification for budgetary purposes.

    - OMB scoring criteria, as defined in Circular A-11, Appendix B, are predicated on the allocation of risk between the Government and the private sector.

    - Operating Leases maintain the appropriate level of private risk consistent with the private owner's continuing performance of the ownership responsibilities of the asset leased to the government.

    - Therefore, intra-governmental transactions, such as GSA's Occupancy Agreements with customer agencies, are structurally incompatible with the concept of an operating lease classification.

Mr. Granof asked what is meant by, "intra-governmental transactions, such as GSA's Occupancy Agreements with customer agencies, are structurally incompatible with the concept of an operating lease classification." Mr. Kravitz explained that from a legal perspective the allocation of responsibilities and corresponding levels of risk is not comparable between two federal entities as it would be between a private entity and a federal entity. Mr. Gramp added that from an accounting perspective they would be viewed as operating leases and very rarely as capital leases.

  - *Are lessees able to obtain a breakdown of the various charges (bundled services, improvements, profit) in their lease payments?*

    - GSA is the lessee in all its leases. Cost breakdowns are part of the Request for Lease Proposals (and subsequent offers) and the awarded lease contract.

    - The Occupancy Agreement between GSA (the lessee) and the tenant agency (the assignee) breaks out the charges that comprise the rent payments made by the tenant agencies.

- *Intra-governmental*

  - *What is the approximate value of real property lease commitments as opposed to the value of personal property lease commitments?*

    - GSA has real property Operating Lease commitments of $23.626B for 10/1/2013 and beyond

      - *Data from FY13 Agency Financial Report (AFR), Footnote 9*

    - GSA has real property Capital Lease commitments of $208M for 10/1/2013 and beyond

      - *Data from FY13 AFR, Footnote 9*

        - GSA has no personal property lease commitments for 10/1/2013 and beyond
            - *Data from FY13 AFR, Footnote 9*

Mr. Gramp added that GSA's personal property leases are immaterial and vehicle leases are all operating leases.

    - *What are your thoughts on lessee/lessor symmetry if a single model approach is implemented?*
        - *Some have noted that maintaining symmetry if right-of-use assets are recognized would require more communication between GSA and agencies.*
        - *Others have noted the need to coordinate intra-governmental balances now (that is, payables and receivables and treatment of improvements) means a process should already be in place.*

Mr. Gramp noted that because of the need to identify intra-governmental transactions, symmetry is very important.

    - GSA defines the single model approach for the purpose of responding to this question as the following:
        - Accounting treatment for all leases includes right of use asset and liability on the Balance Sheet.
    - If the single model approach is incorporated into FASAB guidance, then GSA as the lessee will be required to establish a right of use asset for both funded and unfunded leases and report these assets on the Balance Sheet along with a right of use liability.
    - Both the asset and liability will be amortized/drawn down over the lease term.

Mr. Steinberg asked if consistency between the budget scoring for leases and the accounting for leases would be important. Mr. Gramp noted that the consistency would be preferable.

- *Intra-governmental*
    - GSA is the Assignor of space when dealing with other Federal agencies.
    - If the tenant agencies were to be required to establish a right of use asset and liability based on their Occupancy Agreement, the tenant agency right of use liability would need to "match" a GSA right of use receivable for this assigned space.

        - This would require regular communication between GSA and the tenant agency to ensure no intra-governmental variances are created.

- *Current Accounting*

    - *What matters require attention under the current accounting standards for leases?*

        - SFFAS 5 and 6 do not provide sufficient guidance for all leasing activities.

        - If FASB moves forward with proposed Leasing Topic 842, this will be a significant divergence from the current leasing accounting guidance GSA has relied upon.

        - Once Leasing Topic 842 becomes effective, will the SFFAS 34 Hierarchy of Generally Accepted Accounting Principles be amended?

        - These topics require attention under the current accounting standards for applying accounting treatment, presentation and disclosures:

            - Rent abatements
            - Free rent periods and credits toward space alterations
            - Broker commission credits
            - Straight-lining of expenses and revenues
            - Leasehold improvements
            - Sales-type leases
            - Leveraged leases
            - Direct financing leases
            - Sale-leasebacks
            - Public, Private Partnerships
            - Build to suit leases
            - Leases related to portions of assets
            - Sub-leasing arrangements when GSA is the lessee and assignor of space.

Mr. Gramp discussed several questions/issues for FASAB to address in its revised lease standards.

- If right of use assets and liabilities will be unfunded, will the current year amounts for both GSA and tenant agencies be moved from unfunded to funded at the beginning of the year or on a monthly basis?

- What should be included in the calculation of right of use asset and liability amounts?

    - All options?
    - Tenant improvements?
    - Rent abatements?

- Note: Today, the Intra-Governmental Transactions (IGT) Team does not include Other Assets (SGL 1990) in the intra-gov matching of Other Liabilities w/o Related Budgetary Obligations (2990) and Capital Lease Liabilities (2940). GSA has an on-going quarterly intra-gov variance with a tenant agency because of this.

- Is FASAB considering only a single model approach and not the dual model approach?

- Will Federal agencies and their stakeholders receive value added from the proposed single model approach?

- GSA's mission is to promote economy and efficiency by leveraging our economies of scale. Will this new accounting treatment create efficiencies?

Chairman Allen thanked all of the GSA representatives for their very insightful presentation and that the Board and staff look forward to continuing to work with GSA.

- **Steering Committee Meeting**

The Steering Committee discussed the staffing plans presented in the briefing memo and agreed to the plans contingent on developments between now and the next fiscal year.

The draft statements of work were discussed. A decision was deferred until following the next day's discussion of the three-year plan. The committee reconvened Thursday at 4 PM and discussed options for contract support of two highly rated projects – responding to the Department of Defense request and reviewing requirements for reconciling budget to accrual information.

Adjournment

The Board meeting adjourned for the day at 5:30 PM.

Thursday, April 24, 2014

Agenda Topics

- **Reporting Model**

The Board continued its April 23, 2014 discussion of an ideal reporting model and the remaining Board members, Messrs. Granof, Bell, Dacey, and Reger presented their individual views regarding an ideal reporting model.

<u>Mr. Granof</u>

Mr. Granof noted that the existing model addresses many of the unique aspects of the federal government, except the money supply. He also noted that the existing model is rooted in the 20th Century – it does not acknowledge the use and benefits of computers and the internet. The model that the Board establishes today is likely to be in effect for the next 40 or 50 years and paper-based statements, including Portable Document Formats (PDF), will be well behind the times. Consequently, the Board should think strategically.

Mr. Granof's presentation included the following points:

- The Board should move in the direction of linking cost and performance information.

- The Statement of Budgetary Resources provides information only on budgetary resources in a very legalistic sense and those who are not intimately involved with the federal government do not understand it. Accordingly, it should not be a main financial statement.

- Budgetary integrity requires information to determine whether the budget provides a reasonable estimate of what the costs will be – a budget-to-actual comparison.

- Retain the government-wide Statement of Net Cost, but link it to the financial statements of the individual departments and agencies. The department and agency reports could provide drill-down capability and link to the cost of specific programs.

- Specific program costs could link to major goals and major goals could link to performance measures. The idea would be to link to some statement that indicates as specifically as feasible the performance measures and costs – a Statement of Performance Measures and Costs. Links could also be used for the government-wide Balance Sheet and link line items, such as Property, Plant, and Equipment to department and agency statements.

- Agency reports need to be easier to understand and Mr. Granof presented a simplified Statement of Changes in Net Position, using language that people can understand, and indicating what were the budgetary resources and revenues (where did they get their resources); what were their cost of operations; the excess revenues over expenditures; unexpended appropriations; beginning position; and the position at the end of the year.

- The existing financial statements do not inform users about a critical aspect of federal financial management - managing the money supply, what were the changes in the securities that it bought and sold during the year. A statement (Federal Reserve Statement of Changes in Key Assets and Liabilities) could indicate the assets and liabilities of the Federal Reserve; the increases during the year; the decreases during the year; and the ending balance. Items could be linked to the narrative in the annual report of the Federal Reserve.

Details of Mr. Granof's presentation are attached.

Comments/Questions

Mr. Showalter noted that the model appeared to focus on the money supply while the federal government performs many other functions. Mr. Granof noted that the government influences the economy through fiscal policy and through monetary policy. Although information on the money supply is already available, monetary policy has definite economic and financial implications and deserves special treatment. If one looks at the financial statements of the federal government, one should be able to readily get the information they need.

Mr. Steinberg noted that Mr. Granof's model is based upon linkages and drill downs in order to be able to provide a much richer, more robust panoply of information to the users. It indicates that we should develop a model for using electronic reporting to report financial position or results. Mr. Allen agreed that the Board needs to consider the forward-looking, drilldown aspect; however, he noted that he would consider starting with functions which could involve various departments and agencies. Mr. Steinberg added that an electronic model should allow one to enter the model as they see necessary, e.,g., those interested in Childhood Education could see Childhood Education costs from the Department of Education, Health and Human Services, Labor, etc.

Mr. Dacey noted that the model discusses the impact of the government on the economy and the stewardship objective of reporting requires such information. However, he expressed concern about where the Board should establish boundaries for the model.

<u>Mr. Bell</u>

Mr. Bell noted that as a reporting model task force member, he could recall discussions talking about things like presentation and ideal content but, later, the group would find itself talking about electronic reporting. Consequently, the real challenge for the Board is determining a general strategy for approaching this project.

Mr. Bell noted that he begins his presentations with the quote from President Thomas Jefferson to his Treasury Secretary, Albert Gallatin, "We might hope to see the finances of the Union as clear and intelligible as a merchant's books so that every member of Congress and every man of any mind in the Union should be able to comprehend them to investigate abuses and to consequently control them". This is the mantra that we should keep in our minds as we consider where we want to go with this project.

Mr. Bell discussed two themes: 1) The What versus The How; and 2) achieving and maintaining balance within the reporting model, regardless of the direction the Board decides to take.

The What Versus the How

The Board should manage the scope of its expectations and focus on the “what” - what is being reported, the content of what is being reported, such as the previous presentations. This would include identifying critical gaps in our current reporting model. Linking cost and performance may have a place in the model, but going too far into performance information can be a “slippery slope.”

Also, the Board should consider opportunities to streamline the current reporting model. Rather than adding information, the Board could refocus the message or better communicate information.

The “how,” such as electronic reporting, should be secondary or a separate project. Trying to do both could divert attention and focus from the model itself. Also, the Department of the Treasury (Treasury) has ongoing projects and there are efforts with respect to data transparency. In addition, Treasury recently released its traditional html version of the financial report.

Achieving and Maintaining Balance

The cost and value added should be considered when deciding whether to add information or fill a void. Users want the information appropriate for answering their questions and there are opportunities to improve the information being presented. For instance, risk-based reporting is becoming more of a prominent topic as agencies are considering risks and Treasury has started a Risk Management office.

Also, there is significant opportunity with improving the reporting of budget and accrual information. It could facilitate efforts to resolve some of the audit weaknesses at the government-wide level, particularly with respect to reconciling the accrual and budgetary information.

In addition, cost reporting especially in the government-wide report is at a very high level and this makes preparing the Management's Discussion and Analysis challenging. Accordingly, there are opportunities for enhanced cost reporting.

Moreover, the Board should consider opportunities to streamline or to refocus. The Chartered Institute of Public Finance, a UK group, is looking at streamlining the reporting for the UK.

The Board should also seek to achieve and maintain balance in the area of "traditional" versus "non-traditional" reporting. Traditional refers to statements such as the balance sheet, operating statements and the like, while non-traditional would involve things like social insurance and fiscal sustainability. Both play valuable roles and important roles in the reporting structure that we have but we should maintain a balance to ensure that one does not become so prevalent that it overshadows the other.

Comments/Questions

Members noted that while costs are relatively easy to measure, measuring the benefits of additional information can be challenging. The issue is who will use the information and whether it is being provided by other sources. Ms. Kearney noted that the Analytical Perspectives has budget-to-actual information. Mr. Allen explained that while at the GASB, it was important for bond raters to know how well an entity can project rather than reconcile budget to actual. Mr. Showalter noted that the Board could consider discussing this topic with the PCAOB. They have to show cost versus benefit information and they created a function to try to do that. Mr. Steinberg noted that preparing financial reports forces agencies to learn about themselves.

Ms. Kearney noted that the Chief Financial Officer's Council wanted to focus on streamlining the financial reporting and one of their concerns is that they prepare their statements and subject them to an audit, then they prepare a closing package that provides information for preparing the government- wide report.

Mr. Allen noted that members should consider what they would like to know as a citizen and how the information could be more understandable as discussed in FASAB's conceptual guidance.

<u>Mr. Dacey</u>

Mr. Dacey noted that he was expressing his views and not the position of the GAO.

One concern is how much information is included in the financial statements versus what is provided elsewhere. Mr. Dacey discussed that other information is already available to users and the Board should consider how that information might fit into this process. He noted that most government standard setters recognize that there are other items of information available to users that are not part of their direct purview.

Mr. Dacey provided examples of the information that is available to help achieve the reporting objectives:

- The Combined Statement of Receipts, Outlays, and Balances which is by agency and by appropriation year. The document provides extensive detail. Financial statements that link to detailed budgetary information include the Statement of Budgetary Resources (SBR) and a footnote that states whether this information in the SBR tracks back to the President's Budget and shows the reader if there are any reconciling items between what is in the financial statements and what is in the detailed budget report. In addition, the disclosures include a reconciliation of net operating costs to obligations incurred.

- At the consolidated level, a financial statement tracks to the actual budget deficit and explains how the number that users generally see regularly, the deficit, and relates to the accrual basis financial statements. In addition, the trustees' reports provide a wealth of information supporting our Statement of Social Insurance (SOSI).

- Annual Performance Reports and the strategic planning process provide a whole series of documents. Also, some agencies prepare Performance and Accountability Reports which include financial statements and performance information.

- Unlike some state and local governments, and other sovereign governments, the federal government has a legal framework and a process for reporting performance information.

- USAspending.com provides detailed information.

- The statement of spending would be a linkage which would track to the detail included in spending information and will be an important area for the Board to explore going forward.

- Agencies are required to file at the end of the year a Summary of Performance and Financial Information sometimes referred to as SPFIs, the acronym. The reports are akin to the Citizen's Guide for the consolidated level. There is a whole set of data elements required to be included in these reports which the Office of Management and Budget publishes as part of their financial reporting requirements.

- Monthly and daily Treasury statements, statements of public debt, and monthly budget reviews by the Congressional Budget Office (CBO.)

- Information that helps to meet the systems and control objective and in addition to financial statements, the Management's Discussion and Analysis include reporting on controls and compliance.

- The agency reports include reporting in improper payments, serious management performance challenges (those are identified by the IG and include the progress in fixing those). The agency reports also include a host of other information as well like tax revenue and analysis tax revenue and foregone revenues and so forth.

There are a number of benefits in preparing financial statements. For instance, the CFO anniversary report cited the evolution of reliable, timely, and useful information and increasing levels of credibility and confidence in government information.

The consolidated financial report (CFR) provides summary level information and should continue to be linked back to the agency statements. However, it may not be reasonable to expect the citizenry to read and analyze an entire agency report or CFR. Accordingly, the Citizen's Guide is a primary tool to communicate to the citizens the overall financial results, and it may be necessary to provide summary performance information. The federal government is considering government-wide performance measures.

The Board might consider how the information is communicated to users. For example, there are opportunities regarding how to array the information in the Statement of Net Cost. The standards were not focused on reporting on the entity’s programs; rather, they were focused on how the entity was managed and what are the strategic goals. While it might be important to tie cost to management's strategies and performance plans, some agencies do not use their strategic goals as the basis for associating costs to particular items. Accordingly, current reporting on responsibility segments may not provide the level of detail being sought.

Also, there is a desire to have information and accountability continue at the component level. Starting in 1996 with the agency statements, Congress was very concerned about the accountability at the agency level. They were concerned about whether agencies were reporting all the assets and liabilities and whether there are adequate controls, because they were managing at the agency level. So in 2002, Congress passed the Accountability for Tax Dollars Act which, for entities with over $25M in appropriations, required a full set of financial statements showing information on all assets, liabilities, and operations and other information. Component level areas that the Board should consider include:

- Statement of spending
- Responsibility segment reporting
- Statement of Net Cost
- The linkage between the reconciliation statements in the consolidated report to the information in the agency statements.

- SBR – Is it reporting the right information on receipts and outlays, which are the components of the budget deficit? Also, disclosures reconciling accrual to obligations need revision because the budget deficit is on an outlay basis not on an obligation basis.

In addition, the Board has been talking in terms of an electronic reporting model. Drill-down capability can be built under our current structure and have information that would link the CFR back to the agencies. Also, there are adjustments that are made for inter-governmental transactions and for certain cost allocations. This information could serve as an intermediate level between the CFR and agency statements. The current array in the CFR statements work well because users can then drill down to lower level detail in the agencies. However, it may be helpful to provide users information on what could be considered "identifiable" programs, such as where one could locate the National Weather Service.

At least in the near term horizon, we should expect to have a static set of financial statements with opinions on them. The audit model is based on the opinion on a static set of information. However, that does not mean that information cannot be linked to richer detail.

Ideally the federal government would get to a point where there is a common body of data that everyone can use. It is not necessarily this Board's task, but it could be a goal to have one data source that can provide the kind of reports to the public, management, and whomever. Accordingly, it will be critical to identify what are the attributes to assign to those transactions and balances; what do we want to sort on; what do we want to pull from; and what are those key elements, realizing that we cannot identify every element that we may later want to sort on.

The other challenge is the level of aggregation. At the transaction level, direct costs can be coded, but the ones that go to overhead or are allocated require some judgment and a process to assign to a particular responsibility segment. At some point, we would need to say here is what we want this cost to be associated with, one of them being the agency's performance goals.

Comments/Questions

Regarding whether there is sufficient information within the budget process to identify what has been budgeted by a program, Mr. Dacey noted that he was not sure that it is feasible to track the funds authorized back to that level because it is not decided in that manner, it is decided by appropriation. However, budget execution information, such as receipts and outlays, could be linked. Also, much of the spending involves mandatory programs rather than discretionary. Budget authority is not the driver for mandatory programs; instead, recipients need to meet certain criteria to receive the funds.

Mr. Steinberg noted that the summary reports Mr. Dacey mentioned are getting smaller – presenting less information.

Mr. Showalter noted that the Board should be aware of what other information is being made available to users as we develop a model. Mr. Dacey noted that he was not proposing major changes to the structural relationship between the consolidated report and agencies. To know how well the government is doing as a whole, one could start at the Citizen's Guide or go directly to the CFR. However, other people may want to go directly to programs. Different users will enter at different levels depending on their interests, but the CFR could have links.

Mr. Dacey also noted that required supplementary information in the U.S. has no equivalent internationally. Mr. Bell noted that there are some countries that are moving toward accrual budgeting; such as Switzerland and some Central American countries have started getting into sustainability reporting.

<u>Mr. Reger</u>

Mr. Reger provided the following remarks:

Since the implementation of CFO Act in 1990, federal agencies devoted significant time and resources to the process of producing reliable comprehensive financial statements for the use of the taxpayers, legislatures and the financial community. Much progress has been made and in fact for 2013, the most recent year, 23 of the 24 CFO agencies have achieved opinions.

However, concerns have been raised over the relevancy and usefulness of the financial statements in their current forms. That said, we do realize the value provided in the discipline of producing the statements. So, as we look at what an ideal reporting model might be, we thought about would we really want to abandon those robust efforts of the past 20 years, and are we close enough that we just need to address the concerns that are being expressed. As if that statement itself was not evidence enough given today's budget realities, we thought the latter opinion would be the best.

We think we should develop real changes to solve traditional problems when taking new approaches. For example, we know there is a disconnect between some of the statements required government -wide and the statements required by the agencies in their agency-based comments. This we need a solution to.

Instead of the traditional approach to develop new reconciliation statements, what if we rethink what should be reported and match the information at various levels.

The previous remarks are an indication of the commitment towards the process that we have all developed jointly which is the construction of a fundamental framework for accounting which is now regarded not only in the United States but worldwide as the model of monitoring government performance, financial performance at the least.

I have been lucky enough in the couple of years that I worked at Treasury to go to OECD and to present the financial report of the U.S. Government and the report on financial condition. And it is always an awe inspiring experience to sit in that room of maybe 60 individuals at a time; and most people speak in English or French, the two languages of OECD. But when you are there representing the United States, it is the only country when they go to present that the room goes quiet and people really want to hear what we say. They want to hear not only what our financial data says, but what are we doing, where are we headed. So, the discussion today about how to improve the financial reporting model is not only fundamental to everything going on in this country and for us, but I have to tell you it is incredibly fundamental to all the other countries of the world because while many of them tweak our model to aid their own circumstance, all of them want to follow us.

For example, the South Koreans come to see us repeatedly and, in the last visit, they said yes, we have done all that, what should we do next. It is refreshing and encouraging that we are sitting around thinking about what do we do next.

Now that we have this incredibly robust set of data and information, let's hope that the only thing we do with them is print them. Also, with the robustness of the data that we compile to get to these numbers, what are we doing with that and what do we do to help people understand that there is incredible value in this. It is a little weird when you do sit in OECD and 60 something countries of the world are asking us that question, and we are not hearing it more in the United States.

Observations

The United States is moving towards a mass consolidation of accounting systems and processes around a standardized accounting structure largely similar to Treasury's CGAC. Now, we have 153 entities that combine into the consolidated report every year and a huge number of accounting systems, many of which run on four basic platforms but are different. Their structures are different, their flags for controls are different, and it is insane because we cannot then easily garnish data from all those systems and processes. Also, the most recent cost data available was from 2008 and it was $8.1B. That was for federal financial operations not additional things, just for federal financial operations it was costing, on agency estimates, about $8.1B a year and roughly 53,000 full-time equivalent employees.

We know that it costs about $100M to start the replacement process for a system, and we all are burdened because roughly 50 percent of the time, those things do not occur within budget or on time. Also, industry success standards for commercial applications and upgrades are actually lower. So, while we may complain about how long it takes us and how much it costs to replace those systems, if you looked at industry data, they advise people going through the same process that it is an even lower rate of success within budget.

It takes years to implement new systems and when we do implement those systems, unfortunately they tend to be near the end of their already supported life cycle. So we do not get the very robustness to the systems that we are putting in.

Technology is improving more rapidly than we can take advantage of in our accounting work. How many of you are dealing with a bank where you can now do a deposit by taking a picture of it with your phone, check your balance on your phone, do all kinds of transactions with new technology. And, yet, financial accounting systems are just getting to where we are generating information to a broader group, and we have not even talked and figured out how to get that information into the hands of maybe the project or program manager who needs it the most.

To identify the attributes of these systems, it is incredibly difficult, almost impossible, to identify attributes among these systems. Here are two examples:

- The only way to figure out how much the federal government contributed towards the City of Detroit was to do a data call amongst all the federal accounting systems.

- More recently we have been asked what money we have available to Puerto Rico; what grants are outstanding to Puerto Rico; what the funding level of those grants are; and what problems we are having with disbursing money. The only way we found to do that is to identify through books the actual grants that are out there and start to pick up the phone. I think this is just unacceptable in today's world.

Canada, Great Britain, Australia, New Zealand and Sweden have adopted more consolidated approaches to financial operations that far surpass the United States in information available at significantly lower costs. Most major international corporations including Walmart, Marriott and IBM have been the focus of studies for us to try to figure out how they collect information and how they share it back.

The United States is moving towards mass consolidation of accounting systems. OMB Bulletin 13-08 in 2013 mandated that Treasury foster the creation of a robust shared services marketplace in the federal space and charges OMB and Treasury to review all agency plans for financial systems' modernization, working towards the consolidation of those systems.

There are three major case studies involving large federal agencies combining their core operation to existing service centers and the lessons already coming out of those cases have been fabulous in terms of what do we have to do to actually consolidate accounting activity and have it be more consistent.

This could result in the consolidation of core accounting operations into a limited number of accounting processing operations in the next ten years with all operations on a limited number of systems using the same or virtually the same processes and data requirements. This would allow us to upgrade all financial systems at once for a fraction of the cost incurred today. Also, this would foster the consolidation of functions such as electronic invoicing, collecting of administrating receivables, generation of standardizing reports and allow for faster searches and information gathering. In addition, uses of that information would be easier; application of new processes and technology; creation of integration of centers of excellence around grants, loans and other related activities so those functions could be done uniformly throughout the government; and it would allow CFOs and accountants to analyze, not spend for, to collect.

So the accounting staff of the agencies could play that role of CFO and of advisor that most of the CFOs joined the federal government to provide to help their agencies know what information they had and how that financial information could aid in their decision making, not spend huge amounts of time making sure that a file is posted when the data was collected.

There are wonderful electronic systems, as an example, for invoice collection where you can actually outsource your invoicing to the vendor. The vendor caring more than anybody else that you have received his invoice and if it accepted it.

What Should FASAB Do?

FASAB should continue efforts to ensure that the agency and the CFR include all the major risks faced by the United States. Also, we should work with DoD to encourage and aid their efforts to gain an opinion over DOD's financial management, and support DoD and the financial community combining resources wherever possible. The staff of DoD would benefit from the interaction with staff of the agencies, and the auditors auditing the agencies would benefit from the interaction with the auditors working with DoD.

Also, work with Treasury to resolve the inter-governmental and the consolidated disclaimers. In addition, FASAB should encourage education of all the users of the statements regarding the value of generating this information and the cost and uses of the information generated; and find ways to expand access to the information and all the associated background data that is generated to compile these reports.

Additionally, FASAB should review our rules and determine as the systems and consolidations begin to move along what opportunities are created for consistency and growth, and consolidation of the activities we manage and rule.

Moreover, we all need to figure out how to define program. There are, in most of the accounting systems that I could research quickly, six or more administrative levels of activity that just in our presentations we talked about program as 23 things that represent the most cost of the United States.

If you talk to program mangers, they talk about a program as that little tiny program that they are running and wanting to know what the costs of that program are. If you talk to a CFO, he will talk to you about being able to look across programs under his or her purview to know how they relate to each other and be able to grow, to get comparisons going. So we need to find a way of defining this term that Congress and we use as "program" and then allow for accounting above and below it.

We need to find a way of tracking long-term views of needs and commitments, and I think we need to talk about how to look longer term at revenues and costs.

Also, the robustness of the data and the years' worth of efforts that go into the reports every single year is not being used to its potential at all. If we could do things regularly and consistently to show people the use of that data, in a way that state and local governments found ways to use their financial data, then we would accomplish a large important mission that we have not even tackled.

Addressing views on the ideal model is our one opportunity to be passionate about what we feel. I feel incredibly passionate about consolidating accounting activities so that it is cheaper to do it; the information's more consistent; and we can actually use the data better because we could get it uniform enough that people could use it, see it and make decisions with real financial data.

Comments/Questions

Regarding transparency, Mr. Reger noted that the information in the reports has adequately demonstrated to people all over the world that we have the ability to cross political lines to come to representations of financial position and, for that, the printing of this report and the generation of this data is invaluable. The question is can we be more effective with the information we are collecting; can we find a way to make it more effective in what it represents; and with the wealth of information behind these reports, can we make them more transparent, more available so that they can be used more robustly I guess.

Mr. Granof noted that the cost of upgrading systems is trivial given the size of the budget and if the system can enhance efficiency by a fraction of a percent, the government would be more than paying off its investment. Mr. Reger noted that there is a pressure to look at total administrative costs inside the federal government and there is room to invest in the consolidation activities so that we improve the data and improve the transparency of the data and we lessen administrative costs in many, many associated entities. Mr. Dacey noted that the spending on systems is intended to reduce overall costs.

Regarding the Board's role with respect to forward-looking information, Mr. Reger noted that he has advocated for people to stop looking just backwards. It is great to know what your performance was, but the only reason I can think to know what your performance was that it should influence your performance in the future. What we do in the financial data and in the information on sustainability is incredibly valuable and FASAB has played a very positive role in dealing with the Social Security issue and the associated liability. Also, FASAB will continue to play a valuable role as we identify and consider other risks and their longer-term impact because there is difficult political pressure of what to do with those things.

> **Conclusion:** Staff will summarize the presentations, indicating common themes, to facilitate discussion in June 2014.

- **Risk Assumed: Insurance and Non-loan Guarantees**

Ms. Gilliam opened the risk assumed session. She stated that she received comments from most members and some had concerns about the definition. She also explained that some members were interested in seeing how the definition would look written up in a Standard format. Therefore, staff provided an additional hand out which included the draft Standard format and track changes to the definition. She asked for comments about the updated version of the definition.

Mr. Granof referenced the updated definition and #2 of the handout, asking how that would be different from the loan guarantees programs.

Ms. Gilliam said that some of the criteria would be similar such as the first bullet, “They are administered by an agency established to do so or within a larger agency with many programs.”

Mr. Granof wanted to know how/what criteria distinguish insurance/non-loan guarantees (I/G) from loan guarantees.

Ms. Gilliam said that the difference comes when we start to exclude the programs in #3, the last bullet above #3 does say that “They assume risk for the uncertainty of an adverse event occurring, other than a defaulted debt obligation covered under the Federal Credit Reform Act.”

After some discussion, Mr. Granof and Ms. Gilliam agreed that default of a debt obligation is also an adverse event. The only distinction between loan and non-loan guarantees is that the adverse event for I/G is not a default of a debt obligation.

Mr. Granof said that is not much of a distinction in the definition and then asked why cannot the I/G and loan guarantee programs be treated together?

Ms. Gilliam said that through the research with the task force there were some very distinct differences that were included in TAB F and in particular, the uncertainty that I/G programs face and how they measure their loan guarantees. Loan guarantees can measure their potential loss from the loan amount and duration. However, in working with the insurance programs, staff has learned that they cannot provide those types of projections.

Mr. Granof asked if staff can then bring that distinction right up front to the definition or the subsequent paragraph.

Ms. Gilliam said that staff can do that.

Mr. Bell inquired as to whether we should consider including in the definition an SBA direct loan type program in response to a natural disaster that is a non-loan guarantee program?

Ms. Gilliam said that we have excluded loan guarantees which are covered under SFFAS 2 and we have excluded programs providing relief under the Stafford Act which probably includes SBA disaster relief loans.

Mr. Bell agreed.

Ms. Gilliam said that she did find an SBA non-loan guarantee program for surety bonds that would probably fit into this definition. For clarity, she asked if members want more clarity as far as the distinction and to clarify what the next step is to take with the definition.

Mr. Granof wants to see right up front the rational for excluding loan guarantees.

Ms. Payne said that the federal government is the world's largest insurance company and loan guarantees are insurance. In fact, some of the program titles are even named insurance.

She noted we have standards for direct loans and loan guarantees. As we evolve into standards about insurance other than loan guarantees, we will have to rationalize the two, and we have always recognized that. But the phased approach recognizes we cannot boil the ocean so we are going to divide it up. We have got something that is reasonable for loan guarantees and it aligns with the budget. There are debatable points about fair value versus expected cost. So, at the moment, we are focusing on insurance as a meaningful piece.

The next piece of this phase will be looking at the measurement options that we have. When does a liability exist; what are the measurement options? We may find that the best measurement option is just like loan guarantees.

If we find the best measurement is fair value, staff will ask if the Board thinks it is also the best measurement for loan guarantees. So, as we progress through this, I think we will have to rationalize the types of insurance-like activities that we have and any differences in the standards.

Ms. Payne acknowledged that this is a rules-based definition because we have lists of exclusions. For this phase we are trying to focus on the discrete piece.

Mr. Granof said that he would hold his reservations until staff presents findings on the next steps. .

Mr. Granof asked what, "they follow this hierarchy… or are otherwise enforceable by law" under the second bullet point means."

Staff could not remember and agreed to remove it.

Ms. Gilliam stated that the task force explained how the program gets administered, beginning with the law and moving toward the specifics in the arrangements or agreements.

Mr. Granof asked what the difference is between an arrangement and an agreement.

Ms. Gilliam referred to the last Board memorandum which explained that the agreement is a contract while some programs have arrangements versus a legal contract where they have arranged something. For example, there is an arrangement between FAA and DoD where DoD will indemnify FAA for any wartime damage to their aircraft after FAA pays the claim.

Mr. Granof asked if an arrangement was a document where they agreed on something.

Ms. Gilliam said yes according to the law and regulations.

Mr. Marchand (general counsel) explained that if you think of it as a continuum you have a contract on one side which is a legally binding contract. An agreement may be legally binding in the form of another type of agreement, such as grants, or cooperative agreement, etc. An arrangement is less formal and not necessarily legally binding.

Mr. Granof asked if a contract is an agreement.

Mr. Marchand said that yes, an agreement can be a contract. But an agreement is a broader category of legally binding documents.

Mr. Steinberg said that if an agreement was stronger than an arrangement, perhaps we should switch those words in the document.

Ms. Gilliam agreed to review that.

Mr. Dacey said it still was not clear as to whose losses the program assumed risk for, (losses incurred by a designated population?) and wanted this addressed in the definition.

Ms. Gilliam agreed and Ms. Payne made the changes to the definition to move "by the designated population" after "for losses incurred."

Mr. Dacey continued with a discussion on whether "adverse event" was clear in the definition or from the criteria below.

Ms. Gilliam referred members to the third bullet down which states that the arrangement or agreement will state the specific adverse event.

Mr. Dacey agreed with leaving the definition as is since that bullet clarifies where to find the definition of "adverse event" and whether the federal government is compensating people for their losses, all or partial. He was also concerned with the nuance of the definition stating "authorized by law" as compared to bullet #2 that stated "they follow this hierarchy of authority." The prior definition "as defined by law" was fine. But this is not as clear.

Ms. Gilliam speaks to a previous conversation with Mr. Bell, that when the hierarchy was part of the specific definition that the hierarchy defines all of the pieces that the program is supposed to follow: the adverse event, the losses, and the designated population. She recommends merging bullets #2 and #3 together to help clarify.

Mr. Dacey said that “following this hierarchy of authority” may not provide additional clarity.

Mr. Bell suggested that we merge bullets #1 and #2 instead.

Ms. Gilliam agreed.

Ms. Payne and Ms. Gilliam agreed that staff will update the definition with the suggestions collected so far and send it out for email comments.

Mr. Steinberg asked about financially compensated. Are there insurance programs where the compensation is other than financial? One example, I can think of is crop insurance, where the farmer cannot sell his crop, so he is given other crop.

Ms. Gilliam stated that from their research with the task force, the compensation for insurance companies is always financial.

Mr. Steinberg asked if FAA would replace the aircraft instead of financially compensating for the loss.

Ms. Payne clarified that from the task force discussions concerning programs that can exercise discretion for what goods or a services to provide when someone is harmed, staff determined that those disaster relief programs should be in another phase because it is very difficult to define what type of compensation will be provided until the event occurs.

Mr. Steinberg asked if the word “financial” limits the definition. Ms. Payne explained that use of the word “financial” was intentionally limiting the scope.

Ms. Gilliam referred the members to the exclusion of compensation by programs for natural disasters where the compensation is non- financial and discretionary, versus insurance programs that, per their arrangements or agreements must pay a certain amount and there is no discretion. For example, when there is a disaster, FEMA has the discretion as to what they are going to provide, i.e., how many trailers for homes.

Whereas insurance programs are bound by their agreements as to how much compensation they can cover. For example, FDIC can cover up to $250,000 for deposits

Mr. Allen referred to Mr. Steinberg's point in reference to bullet #3 stating that due to the explicit statement to exclude non-financial programs under the Stafford Act, that he read that as limiting the exclusion to that one program. He asked if we should we expand that to all non-financial in our exemptions?

Ms. Gilliam asked Mr. Allen to clarify whether he meant one act or one program because she referenced the Stafford Act, and not just one program.

Mr. Allen said that Mr. Steinberg was using some examples that probably would not have fit under the referenced Act. Should we just say that we are exempting all non-financial in case there are other non-financial transactions not referenced here?

Ms. Gilliam agreed.

Mr. Steinberg asked why we are excluding non-financial compensation.

Ms. Payne explained that there is a tremendous amount of discretion with non-financial compensation in determining, for example, the number of trailers to house people after a hurricane, or how much National Guard Service to secure property.

It is just a decision based on what happens, and some of it's discretionary because it does not come into play until, for example, a national disaster is declared. So it is simply the degree of uncertainty. And it is not that we will not get to them. Just that we will address them in the next phase; I think they fall in Phase 2.

Mr. Showalter asked if staff was just trying to carve this out so it could be more measurable.

Ms. Payne said yes.

Ms. Gilliam directed members to the research and analysis in relation to the credit reform act. She continued stating that there were quite a few similarities stated under "A" on page seven. But then for each one of those similarities, we found quite a few differences that we discuss under "B," and the biggest ones being the uncertainty having to do with the limitation of data, timing of data and just the uncertainty of the event.

She asked if there are any concerns or any other research the Board wanted staff to do in relation to the Credit Reform Act and, specifically, the loan guarantee programs?
Mr. Dacey said that due to the difference between the lengths of contracts for loan guarantees and insurance, in particular short- term casualty insurance (life is a little different), that we may have a different measurement. But in a credit reform program, a guarantee on a loan is not just for a year at a time, it lasts for the life of the loan.

Ms. Gilliam agreed that the guarantee lasts for the life of the loan.

Mr. Dacey explained that with an insurance policy there are concepts related to the period of coverage of that policy that can be used in measuring the policy. Therefore, that is a difference from credit reform, because these insurance policies have got a different measurement potential than what you're going to measure with loan guarantees. Which he is not sure that was drawn out in the analysis.

Ms. Gilliam agreed that this was a good point. Most insurance programs have short term, one year contracts (for example, flood insurance) and will adjust premiums in relation to losses from prior years and do rely on renewal for this funding. The only long-term contracts we found were at OPIC, for political risk insurance.

But most of them had short-term one year contracts and they can adjust premiums to fix funding from previous years. And some programs also relied on renewals to keep the funding available for prior or potential future losses. So that is a big difference as to how long insurance contracts are in relation to loan guarantees.

Mr. Dacey asked what our measurement criteria are. What is the horizon, the policy or future losses? Is staff only focusing on the exposure to all things during that policy period opposed to credit reform where it is a many years' horizon in terms of our estimated cash flow?

Ms. Gilliam directed the members to the credit reform analysis where there are a number of similarities, but within those similarities are differences. The staff can see two possible camps: the high impact/low probability and the short term contracts, both being hard to model. And, when we look at how to measure, staff wants to look at how these programs project their expected losses. And, even though they do not do project for the financial statements, they are doing it for the budget and projecting out 10 years, so staff wants to look at how we can use that on the financial side.

Mr. Showalter said it was a pretty good list. Ms. Gilliam thanked Mr. Showalter and also thanked the task force, stating that they worked hard on it. She explained that the task force met for two meetings to go through, and with special thanks to Sarah Lyberg who is our credit reform expert from OMB. She was very helpful in providing information and educating the task force.

Ms. Payne directed the Board to the next steps on page five of the memo stating that this is a check to see if members are comfortable with how staff should proceed and if they agreed with the next steps.

Mr. Bell asked if we are taking it as a foregone conclusion that there are no agencies that are making any kind of recognition of this information, or should one of our questions be to what extent are any agencies already recognizing or disclosing this information and include this as one of the questions for next steps.

Ms Payne apologized stating that it appears that the questions in next steps do imply that no one's recognizing this information. But through a general survey, programs are recognizing consistent with Standard 5, Probable Losses, usually based on events that have occurred before the statement date. So, for example, at PBGC, a plan is in failure or there are signs that it is in failure.

Mr. Bell then suggested that a gap analysis be part of our analysis to provide a baseline and a reference back to what is currently being recognized.

Ms. Payne, Ms. Gilliam and Mr. Dacey agreed that a gap analysis would be beneficial.

Mr. Dacey said that one of the issues for the risk assumed project is that some of the measures for the exposures are not consistently prepared today between the different programs.

Therefore, the first part is the recognition and disclosure part which is to figure out what do we want to disclose besides the liability recognition, what disclosures in terms of magnitude potentially or exposure do we want to disclose because there are variants and variances in the way the numbers are coming out today. However, he did recognize that there is a lot there to digest.

The other part is that there is inherently a liability where we collect premiums to the extent there is another expected premium. And that is considered typical in the FASB short- term insurance contract world which it appears they are not changing their path at this point, based on current articles.

Ms. Payne asked if there was any other information the Board would like to discuss before we move to P3.

Mr. Allen referenced an article that identified agencies providing financial help to victims of the landslide in Washington State. He was concerned that out of the $56M provided to date that some of the agencies were providing financial support in the form of cash grants instead of discretionary goods or services. He would like to know if they are excluded under 3.C since it is a financial benefit rather than a non-financial benefit.

There was another exclusion concern in relation to the word “guarantee” in that these programs do not collect a fee against which they are guaranteeing any benefit. Yet, they are “authorized by law to accept part of the risk” as the definition states. He asked if these federal agencies would be paying money outright if they do not have authorization to accept risk and if that really is not a guarantee.

Ms. Payne said that staff’s intent was for bullet 3.C to exclude the discretionary activities. And our understanding was that they were goods and services. So, we will research to get a better understanding about financial benefits provided during a declared national disaster.

Mr. Dacey said that Mr. Allen raised a good point and maybe it is inherent in reading this that insurance deals with a structure that is in place pre-event that explicitly says these are the things the federal government will cover and here’s as identified in the third bullet; versus after an event occurs and the government decides they are going to provide some relief assistance.

Ms. Payne agreed with the word ‘explicit” for insurance set up prior to an event and Mr. Reger said that they are not an insured when the government steps in after an event to help.

Mr. Dacey said he does not believe that to be insurance, it is another area that determines what to provide at a point in time in reaction to a disaster and possibly to some extent beyond what they are legally required. But he did not know if it is exactly within the confines of our government acknowledged event structure. But that would be an interesting question.

Mr. Allen said that we should consider saying “financial or non-financial” under 3.C in relation to discretionary benefits.

Mr. Dacey clarified that the concept is around the timing of the event and when the program is authorized to provide benefits, before or after, that we need to address.

Ms. Gilliam said that staff will reach out specifically to our task force at FEMA. They can explain to us what happens when a national disaster is declared and what agencies are authorized to respond to and provide what types of benefits.

Mr. Allen also requested staff to research the word “guarantee” to determine if that is the right word to use for this standard and to determine if these agencies have some type of guarantee authority or if they had resources that they could voluntarily be called upon to provide assistance. And, if that is the case, then we would not want any kind of liability reorganization. He would argue there should not be a liability if it is discretionary to do that. But maybe we just go back to 3.C and clarify it there.

Ms. Payne said that would be possible and suggested staff continue to work with the task force to talk about whether we want to keep the long name insurance/non-loan guarantee, or just go to insurance.

Mr. Allen added to then exclude everything that is discretionary.

Ms. Gilliam added that one of the task force members requested that insurance and non-loan guarantees be defined separately.

Ms. Payne requested that if the Board had any additional thoughts after the meeting to please send them to Ms. Gilliam.

Mr. Allen and Ms. Payne thanked Ms. Gilliam.

Ms. Gilliam thanked the Board and the Risk Assumed topic was concluded.

- **Public-Private Partnerships**

Mr. Savini began this portion of the meeting by handing out a revised draft Exposure Draft document (ED) and noted that recent changes were made to the document contained in Tab G pursuant to member input subsequent to Tab G's mailing. Specifically, staff obtained suggestions from Messrs Allen, Steinberg, Showalter, and Granof which are reflected in the revised ED.

Staff began by welcoming Mr. Lauredt Rafidimahavonjy, an American University accounting student interested in federal accounting. The Chairman recognized Mr. Rafidimahavonjy and thanked him for attending the Board meeting.

Ms. Payne displayed the revised ED handout version on the screen and invited members to offer suggestions or, if they would prefer, work from the original Tab G material. Members agreed to work with the revised draft ED.

Staff noted that the revised handout version accepts all the changes shown in the original Tab G material. This is based on the assumption that members would accept all the changes because the edits primarily came from the March Board minutes and related Board discussions. Mr. Savini suggested that prior to moving to a pre-ballot draft, the Board should review concerns that some members had at the last meeting primarily in the following 3 areas:

1. <u>Proposed P3 Definition and Application of the Risk-based Characteristics</u>
    a. Operating with a broad definition, and
    b. Whether subjecting that definition to risk-based characteristics would identify those P3s possessing risk while excluding those arrangements the Board does not believe should be subject to the proposed disclosure requirements.
    c. Refer to paragraphs A10-A14. In staff's opinion, the risk-based characteristics adequately identify those risks that the Board seems most concerned with or said another way, the proposed process should filter-out arrangements the Board believes fall outside the scope of this proposed standard such as traditional-type contracting arrangements.
2. <u>Materiality and Probability</u>
    a. Whether materiality included probability and to what degree materiality (1) serves as an adequate backstop against disclosing immaterial amounts of risk and (2) helps ensure that we do not require disclosure of traditional-type contracting arrangements.
    b. Refer to paragraphs A17-A19. In staff's opinion, (1) materiality does include probability assessments and (2) because materiality includes qualitative assessments, its application should help ensure that traditional-type contracting arrangements are excluded from the disclosure requirements.

3. <u>Application of SFFAS 5, Accounting for Liabilities of the Federal Government</u>

   a. Whether SFFAS 5 can be relied on as a framework to specifically address the P3 risks (fiscal exposures) addressed by the proposed ED.

   b. Refer to paragraphs A20-A22. In staff's opinion, the Board should not limit this proposed standard to SFFAS 5 primarily because P3s can possess risks that do not necessarily arise from an existing condition, situation, or set of circumstances.

Mr. Steinberg inquired about a change made in the Executive Summary where we have noted that the P3 project is a two phased project; first we do disclosures and then we go to measurement and recognition. We are meeting this afternoon to talk about the agenda, and one can make the argument that some of the other agenda items may be more important than the measurement and recognition phase of this project. I'm wondering whether in the introduction we want to be that definitive; maybe putting in something about "subject to the acceptance of the technical agenda."

Mr. Allen replied by saying he thought the introduction was fine and that what he asked for was a sentence discussing that this disclosure piece was the first of a two-phased project. To the extent that we want to be careful and note that the second phase may not immediately follow is reasonable.

Ms. Payne noted that this is an easy fix that we could footnote.

Mr. Steinberg concurred with Ms. Payne's recommendation.

Mr. McCall then addressed the proposed definition noting that the second feature talks about financing arranged by the private sector. Specifically, because P3s may involve the use of a mix of appropriated funds and/or non-appropriated funds, should the Board suggest that the second feature be changed to reflect this fact? That is, should we instead say, "…financing arranged or shared by one or more of the parties", thus not just focusing solely on the private sector?

Mr. Allen then asked if the government actually provided the financing, the arrangement might not be considered a P3, albeit there are other features identified in the definition.

Mr. Savini agreed with Mr. Allen by noting that financing is but one of the features we have identified in the definition.

Mr. McCall responded by noting that he was emphasizing the government's sharing in the financing. For example, a governmental entity may actually provide part of the financing at say a one percent interest rate. There is quite a bit of risk in such cases.

Ms. Payne then provided military housing as an example of Mr. McCall's observation.

Mr. Dacey asked Mr. McCall if he was suggesting whether it would be more appropriate to say, "financing provided in whole or in part by the private sector".

In reply, Mr. McCall stated that Mr. Dacey's suggested language could probably work.

Messrs. Allen and Savini concurred.

Mr. Bell then said that he saw no specific mention of what role the suggestive characteristics have in the process.

Mr. Showalter noted that the language Mr. Bell was searching for was embedded just below the chart on page 15 and that he also had the same problem when he first read the draft ED.

Upon review, Mr. Bell acknowledged the language.

Mr. Savini stated that he would make a correction via insertion of a page break.

Mr. Bell concurred and then directed members to consider paragraph 8 where we mention the interplay with SFFAS 5 and if the Board was comfortable with the language.

Mr. Reger asked Mr. Bell if he was suggesting something specific.

Upon reconsideration of his observation with his assistant, Mr. Bell withdrew his query.

However, Mr. Granof stated that he found paragraph eight confusing. For example, what does reasonably high materiality threshold mean?

Mr. Savini replied that "reasonably high materiality thresholds" is in connection with remote risks. Specifically, as noted by a Board member at the March meeting, once an entity factors in likelihood or probability, management still might decide to have a higher dollar threshold to meet before disclosing the remote risk in question. That seems reasonable and plausible to staff so that is why we have included that language in paragraph eight.

Ms. Payne then asked if what we are saying is if there is a remote chance of losing $4B, you might waive the notion that remote risks do not get disclosed, you go ahead and disclose it. Is that what it means in application? She noted difficulty reconciling the reasonably high materiality threshold. It just was not intuitive.

Mr. Granof then asked what constitutes a materiality threshold being "unreasonably high."

In reply to both Ms. Payne and Mr. Granof, Mr. Dacey stated that he was fine conceptually with the proposed language and that it is consistent with the Board's March discussion. For example, when the federal government first became conservator for Fannie Mae and Freddie Mac, the government said that it would support up to $200B, and some people did not think that number was actually likely and felt that it was remote. However, even in light of the final agreement and revised projections which indicated that the federal government was not expected to make any further payments to Fannie or Freddie, the limit to which the federal government might make payments under the agreement is still in the hundreds of billions of dollars. Therefore, even though it is expected that it is not likely that the federal government is going to make more payments, the financial statements disclose that limit even though it is remote by all accords. However, if that limit were $20B and not $200B, I'm not sure we would think that would be significant enough or not reasonably high enough to disclose for remote risk. This is what we are talking about when paragraph eight says "…that certain remote risks may have a reasonably high materiality threshold". I think I'd like to figure out a better way to describe this concept, but in practice this is what is used as a thought process.

In reply, Mr. Granof addressed the next sentence which says, “As such, remote risks that are not contingent should not be dismissed from disclosure without further consideration of user needs, qualitative and quantitative assessment, and materiality.” This is the definition of materiality.

Mr. Dacey clarified that when addressing remote risks it is not quite the same materiality as you would use for measuring misstatements. In his opinion, remote risks have a higher disclosure threshold level. Simply put, it is a bigger number than you're probably looking at from a qualitative standpoint and saying the risk is remote but if it happened, it is going to be so significant to this entity that you need to disclose it so you're not misleading the users.

Mr. Showalter suggested that we say, regardless of the amounts involved, that preparers should not dismiss disclosing these risks just because they are remote.

Mr. Granof indicated that what we are basically trying to say is that even though you may have a remote risk, it should not be dismissed. This is especially true because it may involve significant amounts of money. Therefore, we are saying that if it is a material risk that is deemed to be remote it should be disclosed.

Messrs Dacey and Showalter concurred.

Mr. Allen proposed that we could say the remote risks could be evaluated on a cash flow basis in order to ascertain their significance.

Mr. Reger then noted that “significance” is in the eyes of the beholder.

Mr. Dacey agree with Mr. Reger’s observation and said that despite not having the words to propose, he believed a more clear statement in paragraph eight would be helpful.

Turning to staff, Mr. Dacey asked if we were trying to distinguish beyond this idea of remote which SFFAS 5 is unclear about. That is, SFFAS 5 almost suggests that you would not disclose remote risks. It does not say that, but it leads you in that direction. So, the question is, is this the main issue we are trying to bring out or does staff believe there are other differences between SFFAS 5 and where we are now in this draft ED? In looking at paragraph eight , it may be confusing.

Mr. Bell noted that he had the same question and further noted that half way through paragraph eight , even though it is uncertain that a past event indicates the loss may have been incurred, is not part of SFFAS 5 a requirement that an event has in fact occurred?

Mr. Dacey agreed with Mr. Bell’s observation that SFFAS 5 requires that an event has to occur. Mr Dacey said that an event could be non-performance by the other party or a risk of non-performance by another party. As such, because we have entered into a contract where we are bound or locked-in, when such conditions arise, SFFAS 5 addresses “probably” and “reasonably possible” which then drive you to deal with the appropriate disclosures.

At this point Mr. Allen identified a key point. That is, we normally drive to events and that such (1) events may have happened but we are not aware of them happening or (2) events may have happened, but we do not have our hands around the event. Therefore, Mr. Dacey raises a good point; the event is not the loss. The event is that we signed the contract and that is the event that leads to a possible loss. It does not have to be in default but just the fact that we signed the contract alone is the event. That is a different way than we normally look at these events using SFFAS 5.

Mr. Dacey agreed with Mr. Allen, further noting that if we say, for example, that the risk of loss is probable that the private partner is going to default, we are locked-into recognizing the loss. Similarly, if the risk of loss is reasonably possible, we also have SFFAS 5 to guide us.

Mr. Showalter concurred.

Mr. Allen then returned to his earlier point concerning expected cash flows. Simply put, expected cash flows could care less about whether something is remote or probable. It basically just says if you have something that is remote but it has a high potential, then you assign for example, a five percent probability to the $200B Mr. Dacey was talking about earlier. This is what we are saying ought to be disclosed. Staff is thinking along the lines of expected cash flows as opposed to the way we usually think of in terms of SFFAS 5. So, is it possible for us to say that here?

Mr. Dacey replied in the affirmative but noted that disclosures criteria can be different than recognition criteria.

Mr. Granof noted that such a concept is a rather radical departure. Do we really want to go there?

In response, Mr. Dacey noted that we are disclosing to the reader that there is a risk that could materialize into an expected cash out-flow, that is, we are not using this as a basis for recognition. This is a disclosure requirement.

Mr. Allen echoed Mr. Dacey's remarks by stating that this is a disclosure requirement versus a recognition requirement and that if we are comfortable with this notion, maybe the right finesse is saying that we should think beyond SFFAS 5 and here are some considerations.

Mr. Dacey summarized that he agreed with what we are currently saying in paragraph eight and that the other nuance is conceivably at two levels as well. In other words, we may decide that certain risks related to this P3 are significant enough to disclose despite being remote because the risks are large. But even within that contract, we would not necessarily disclose every single risk with that P3 contract. . I think there are two levels that you would apply conceptually, that is, whether you disclose the risk at all and then what parts of that risk do you disclose.

Mr. Bell asked if the Board wanted to focus this language to reflect that there may be other interpretations or other key elements of these transactions rather than saying on its surface that we are pushing the boundaries of SFFAS 5.

Mr. Dacey replied only if we really need to. For example, if you go to some of our insurance arrangements, the federal government has contracts under SFFAS 5 where a liability is booked because there is a probable loss even if it is not manifested itself.

In reply, Mr. Bell said that Mr. Dacey's point sounds a little different than saying something about uncertainty of a loss because we have just interpreted the event in a certain way that this now becomes the new marker for loss versus the other "event".

Mr. Dacey replied that we could try to describe this more but wondered if we needed to get into that level of detail.

Mr. Showalter asked, are we discussing "loss" or is it "risk-of-loss"?

Mr. Reger shared in this query by asking whether we are discussing an actual loss or is it just the risk of a loss.

Mr. Bell thought that we are dealing with the risk-of-loss.

Ms. Payne concurred with Mr. Bell further noting that if it were an actual loss, it would be recognized. As such, we are focusing on the risk of loss.

In clarifying Ms. Payne's response, Mr. Reger said that if so, we are discussing the recognition of a risk as opposed to an actual loss.

Joining with Ms. Payne, Mr. Dacey then replied that if a risk of loss is probable it is going to be recognized.

Mr. Showalter concurred with Mr. Dacey's comment further noting that Mr. Reger may have been thinking about a loss being realized, and what we are talking about today is the risk of the loss. That is, the loss is the outcome of the risk.

Mr. Reger acknowledged that we are discussing the recognition of a risk-of-loss.

Summarizing this discussion, Mr. Dacey said that if one thinks that the risk-of-loss is going to be probable and result in a loss, then you recognize the loss. However, if you think risk-of-loss is reasonably possible, then you would disclose and not recognize. Moreover, we are saying that nuances exist around risks-of-loss deemed to be remote under SFFAS 5. That is, we are saying if such remote risks are substantial per se or could have a significant effect, they should be disclosed.

Mr. Allen asked whether in the last sentence where we mention "…not contingent in nature…", why couldn't we just say remote risks should not be dismissed from disclosure.

Ms. Payne and Mr. Granof agreed with Mr. Allen's change.

However, Mr. Dacey said that he would prefer a more positive statement concerning what we think about disclosing remote risks. For example, we are saying that although we have SFFAS 5, we think that in these P3 arrangements we really want to focus on certain remote risks. He wanted to make sure that is the point, he thought we can get there much more quickly with such a positive statement.

Mr. Granof agreed saying that we should say in a more positive way that you do not dismiss remote risks from disclosure.

Showing agreement, Mr. Showalter stated that basically remote risk should be considered for disclosure.

Mr. Allen concurred.

Mr. Savini referred members to paragraphs A20 through A22 that discuss remote risks. We should go through some of the logic here because this is where staff tried to tease out and draw distinctions from SFFAS 5.

Mr. Allen concurred but noted that as long as the Board agreed on a concept, staff could go ahead and begin making the appropriate revisions.

Although Ms. Payne concurred with Mr. Allen, she noted that his approach is fine as long as staff can get feedback on the entire document in the next cycle.

[LUNCH BREAK]

Mr. Savini asked members to look at the Risks that are Deemed Remote section of the Basis for Conclusions at paragraphs A20, A21 and A22 beginning on page 30. What staff attempted to do here was take a Board members' recommendation to better align the draft ED with SFFAS 5. In so doing, staff teased out SFFAS 5's relationship to past events and tried to figure out how that fits into P3 arrangements that have such a long life and variability of activities and events that could occur over that long life. Staff concluded at A22, in the first sentence, that due to their very nature P3s can also possess risks that do not necessarily arise because of an existing condition, situation or set of circumstances; this was staff's way of divorcing us from SFFAS 5 because in staff's opinion, SFFAS 5 never really foresaw such risks. Furthermore, as we have already heard earlier today, this issue of remote risks is somewhat undefined in SFFAS 5. Therefore, the way staff decided to detach from SFFAS 5 was to say that not all conditions or activities in the P3 necessarily need to exist in order to recognize that a risk also exists. Now, you might disagree with that if you say the signing of the contract as we mentioned earlier might be deemed the event. However, staff thinks the major point here is we have to stretch further than SFFAS 5 because it is insufficient in dealing with these types of remote risks.

Mr. Dacey stated that some of this language would have to be made consistent with our discussion before lunch.

Mr. Bell asked if we should couch or articulate more along the lines of something like, "….these P3 issues lend themselves to broader interpretations of SFFAS 5…." or are we pushing the boundaries too far saying that?

In reply to Mr. Bell's latter question, Mr. Savini stated that SFFAS 5 was written back in the mid- '90s and risk management techniques along with risk governance practices have greatly changed since that time. We are now in the era of enterprise risk management (ERM) solutions and different types of governance structures. In addition to that, COSO has not only changed the current Internal Framework Cube, they've even introduced the new cube, the ERM cube. Therefore, I think we might want to go back to SFFAS 5 and take another look at it because I do not think we foresaw (1) the kinds of risks we now see in P3s and (2) how these existing risks are being addressed by these different risk frameworks. This is part of the problem - P3s and their risk identification come from different frameworks, and I think that is part of the disconnect we have with SFFAS 5. So, however you want to word it is fine with me. I just make the point we should not be anchored by or to SFFAS 5.

Mr. Allen asked if we could say that positively. In other words, why do we have to start with SFFAS 5? Another approach could be that we just say these are the disclosures we want without having to defend ourselves in light of SFFAS 5.

Mr. Savini noted that he was specifically asked to address SFFAS 5 in the draft ED.

Mr. Dacey suggested that staff condense some of this to the essence of the point that (1) we are going to deal with remote risk which SFFAS 5 does not deal with, (2) we are going to require specific disclosures which are beyond the scope of SFFAS 5, and (3) we believe we are consistent with SFFAS 5; that is, we may disclose more but we are not inconsistent with SFFAS 5. Technically, it is hard to project forward, but some of these P3 risks may in fact have liabilities actually recognized under SFFAS 5 and not fall directly under this P3 standard. So, that is why I'm saying I think some summary of how this relates to SFFAS 5 may be the better point here; that is, we are not totally separate or pursuing a whole different idea than SFFAS 5 - that is the challenge.

Mr. Bell concurred.

Mr. Reger then asked if this P3 standard is really a revisit of SFFAS 5 or an amendment. The response was no, it was not.

Mr. Allen stated that he liked the way Mr. Dacey outlined the summary and kept it positive.

Mr. Dacey stated that the disclosure requirements in SFFAS 5 are generic but they are specific disclosures.

Mr. Bell noted that as the draft ED gets exposure we will get these questions and accordingly, we should try to mitigate some of the issues up front.

Mr. Dacey agreed but thought that the draft ED already contains questions to help address these matters.

Mr. Allen stated that as long as we are not changing the intent of what we are communicating, staff should work on the language and then just share it with us. I do not think we have to consider that in a meeting. I'm trying to avoid having to come back and debate or vote on the language again.

Ms. Payne thought that what we would do is work on individual pieces that we spent time editing and then send those discreet pieces to members to look at prior to sending the pre-ballot draft.

As an example, Mr. Reger suggested paragraph eight .

Ms. Payne agreed and added the series beginning at paragraph A20 as well.

Mr. Reger confirmed that staff agreed that he can make paragraph eight more positive and less negative; not its intent as much as its application.

Mr. Savini asked members to address some member concerns over scope and applicability which prompted staff to add a new paragraph 17 on page 12. There was some discussion at the last Board meeting regarding scope. As such, staff has presumptively chosen two conditions that should preexist before we consider a P3 eligible for application of the standard. That is, what we are basically saying at paragraph 17 is that one of the following two conditions should exist: (1) you have an arrangement or transaction that involves a long-lived asset or long-term financing liability; or (2) there is fiscal exposure that could ultimately lead to a liability.

Again, one of those two conditions should preexist but note that this is staff's attempt to best address some members' concern that we were going too broad with the definition and as a result, capturing too many arrangements.

Mr. Granof said that he did not like the wording. First, it says this statement applies only to P3s that possess a condition. I do not think you possess a condition; you meet a condition, satisfy a condition. Now, with that out of the way, the long-lived asset or long-term financing liability both apply as conditions and then you mention recognition concerns including reclassifications. I do not think I know what that means. Also, I do not know what a liability recognition concern is. Let's work on wording.

Mr. Savini concurred.

Mr. Bell asked if there is a general understanding or unwritten understanding of what constitutes a long-lived asset. Is there a threshold, did we define that somewhere?

Mr. Savini stated that he thought the definition could be in the FASAB glossary.

Mr. Allen asked if we meant more than five years.

Mr. Savini replied in the negative noting that this is specific to assets and not to the arrangement.

Ms. Payne asked staff if this really applies to PP&E, when we say long-lived asset.

Mr. Savini replied in the affirmative.

Ms. Pane asked if it would be too limiting if we replaced long-lived asset with Property, Plant & Equipment.

Mr. Savini replied in the affirmative citing as an example an intangible asset such as a patent that is created in a research lab.

Ms. Payne then suggested what if we said such as Property, Plant & Equipment (PP&E).

Mr. Savini replied in the affirmative.

Ms. Payne then asked if that helped clarify what is meant by long-lived assets or if it was still too vague.

Mr. Dacey noted that when one refers to PP&E it includes assets that are not long-lived such as personal property; autos. Mr. Dacey went on to ask if we should use five years that we have included in the draft ED as one of our criteria.

Mr. Savini replied that we could but noted that the five -year term is for the arrangement itself and not necessarily the asset.

Mr. Bell asked if we are applying the same threshold to these assets.

Mr. Savini replied that we’d have to go back to the FASAB glossary and see how we define long-lived assets before answering that question.

Mr. Smith noted that the statement referring to Property, Plant & Equipment or intangibles, infers one or the other.

Ms. Payne and Mr Savini agreed and Ms. Payne asked if members preferred an explicit number of years; staff could make those two adjustments.

Mr. Smith noted that before selecting a number we need to specify what we are talking about; the life of the asset or the life related to the contract.

Ms. Payne said she was thinking in this context the life of the asset.

Mr. Savini concurred.

Mr. Smith stated that would be fine as long as we in fact stay tied to the asset, otherwise we could create an incentive for someone to terminate the arrangement just to get around our disclosures.

Mr. Allen stated that he would prefer not getting to that level of detail. That is, we already had the discussion and understand why five years is appropriate in regards to the arrangement as a conclusive characteristic. However, since we allow entities total flexibility in selecting asset useful life amounts, it would seem counter-productive to get involved in saying any specific point in time because management already has that latitude.

Mr. Dacey then said that he appreciated the thoughts on whether or not to have a discreet number which may be problematic, but do we provide any context around the long- lived asset issue from a conceptual viewpoint?

Mr. Smith asked what members would think preparers would interpret if all we said was long-lived assets?

Mr. Showalter said that because he did not understand the concept, he did not know.

Mr. Savini noted that when you look at agency capitalization criteria and useful life information you will see a very wide range of useful life estimates for similar classes of assets.

In reply to Mr. Savini’s observation, Mr. Allen said that was his concern. However, we can say assets lasting at least as long as the arrangement so that would automatically push them out to at least five years.

Referring to SSFAS 6 capitalization criteria, Mr. Smith stated that if we were going to put a number, we should use two years to be consistent with SFFAS 6.

Mr. Dacey said that he was not sure that he agrees with Mr. Smith’s approach because it could sweep in short-term assets that are probably not part of P3s like cars and IT equipment, desks, etc. That is m concern with using PP&E as the criteria.

Ms. Payne then asked if we could you say something like buildings to be more specific.

At this point Mr. Dacey searched the glossary and noted that we refer to “long-lived ”.

Also researching, Ms. Payne looking through the handbook and noted that in dealing with long-term assumptions the Board picked five years and in other places we use it without defining what we mean. Long-term projections, obviously, that is 75 years. Long-term benefit of the expenses, we do not define it there. In condition reporting, in the deferred maintenance and the condition, we did use the phrase long-term asset, but we did not define it there either.

We do not define long- term anywhere.

Mr. Steinberg indicated that SFFAS 6 says two years.

Ms. Payne acknowledged the two year figure and noted that it is used to qualify a PP&E asset, and that she thought from Mr. Dacey's prior discussion with Mr. Smith, that he wanted to raise it a bit above two years.

Mr. Smith noted that if we go through the term of the contract as the Chairman has proposed, we'd go out at least five years.

Mr. Savini then asked, does that mean if you have a long-term P3 arrangement but its principal asset is under a five year useful life, it would be excluded from disclosure?

Mr. Smith then asked why would an entity enter into a P3 arrangement for say a seven-year period but the assets are going to be gone in two years or three years.

Mr. Savini said that such a scenario would be hard to envision. If we want to stay principles based, we can just avoid the argument and just move on.

Mr. Allen said that would actually be his choice; just leave it as-is; long-lived assets. However, the sentence does need to be clarified because it is awkward.

Mr. Dacey wondered if the Board could come up with any kind of conceptual term for long- life without a number. Moreover, there are other terms that Mr. Granof pointed to such as: recognition, de-recognition, long-term financing, etc., that we need to address.

Mr. Savini clarified what is meant by recognition noting that if you have got an asset that is long-lived, and the question comes up of who should be recognizing the asset; do we, the government, recognize it on our books or does the private partner reflect this on its books, that is an issue, that is a condition. That would be an example of a recognition concern. Conversely, if you have an asset that is excess to your governmental needs and you decide to enter into a P3 with a lease back provision, that might be considered a de-recognition concern. Lastly, a reclassification concern can be a typical lease where I've got an asset such as a building that I do not need but I still have some residual value so it is sitting on the balance sheet. So, by leasing it I convert it to a receivable; specifically a leases receivable, and that would be an example of a reclassification. Please note that I was trying to envision what conditions would help eliminate and address the issue of sweeping in so many P3s, and these are the two that I came up with.

Mr. Dacey stated that he did not think that the casual reader would pick up on these matters and that we would need to describe them in more detail to make it clear what we are talking about. The average reader might miss the context of our discussion.

Mr. Allen then moved to the second condition; fiscal exposure and noted that this is pretty obvious and self- evident.

Mr. Dacey stated the he also was not sure what that condition means. In essence, it could mean virtually anything but that is too low a threshold. He thought we were intending to exclude things where there is almost no possibility of a liability arising and I does not know how practical that is.

Mr. Savini noted that GAO has not defined fiscal exposure and this is why in parenthesis we have included risk. That is, we are looking at excluding any arrangement that basically has no risk that management feels would not result in a liability of some sort. Again, it is giving management that bite at the apple to exclude P3 arrangements from this portfolio that it really does not think have significant risk. Again, by establishing these two conditions staff was trying to help Mr. Dacey deal with the concern that we would be sweeping in too many arrangements.

Mr. Dacey then stated that the terms do not inherently have a clear meaning.

Mr. Allen asked if we should have a generic description rather than two specific conditions. In other words, could we discuss why this standard applies to these kinds of arrangements; that is, because there is the lingering responsibility with the government who signed the agreement may need to provide financial resources in the future. I'm not saying that is the right word but some generic explanation might help and people would look to the generic explanation rather than just to the specific examples. If you could write it that way, I wonder if that might be helpful and then that puts less burden on making sure we get the exact wording for those examples because we have given them the why. As it is now written it is not very principles-based when we just say the standard openly applies to these types of arrangements and we then give two specific examples without an explanation of what the criteria is.

In reply, Mr. Savini asked that the Board first acknowledge if they even agree with the two conditions before staff spends any additional time working on the issues in this paragraph.

Mr. Allen wondered why does a long-lived asset or long- term financing liability really matter. In other words, what is inherent in a long-term asset that tells me that I want to make these disclosures applicable? Does not it come down to risk either way? Said another way, it is the future risk to the government that seems to be the driver. One way we may manifest the future risk is that we have an asset that has a long- life if the government has some continued obligation to maintain or will receive the asset back in the future and so we care about the condition. What is the principle behind those two things, and if we could state that principle maybe we can proceed.

Ms. Payne noted that we only added this scope language to alleviate the concern that a lot of things would be swept in. One of the challenges in distinguishing the scope for me from the conclusive criteria was if it meets the conclusive characteristics, it also meets what is in paragraph 17. She noted that she had a very hard time deciding that paragraph 17 would do anything in a way that was different than what the conclusive criteria or characteristics did. So, it only narrowed down what could be considered for meeting the suggestive characteristics. In that sense it is kind of a pre-screen for conclusive characteristics and that means suggestive characteristics are probably not going to catch anything. She wondered whether we even needed this scope provision and whether the suggestive characteristics are useful.

Looking at the two conditions a little differently, Mr. Smith then asked if we are not looking for risk and off balance sheet items, and if so, that is why those two conditions almost kind of get to the heart of the type of P3 transactions we are looking for.

Mr. Allen asked when you say an off balance sheet item are you saying this is something possessing an on-going risk. What I mean is if it is not recorded why do I care? Presumably if it is not recorded and you're saying it is supposed to come back to me in good condition in 20 years, then I do have some of that risk. I think risk is what we are centrally concerned with.

Mr. Smith then proposed if in such a case did we actually pay for an asset and assume all the risk associated with that asset but because we entered this P3 it stays off my books. So, I get to a ten-year arrangement where I really purchased this building or developed this building but I got some third- party that is going to keep it off the books so now the liability and the asset are not on the books. I thought that is what we were trying to address and disclose so that you'd really understand that you do not have this asset and liability on the books.

Mr. Allen replied that could be true. He only looked at it from a risk exposure standpoint. So, as Mr. Smith explains, this is more than an exposure issue, it is also deals with potential assets.

Mr. Savini replied that the answer to that question depends on how you define risk. I mean, what I'm taking away from this discussion is that the first condition, does in fact conflict the conclusive characteristics and that Ms. Payne is making a very good point. I also think Mr. Smith is making another valid point about the risk being tied to assets. Now, if we were to eliminate the first condition, what would be the harm in saying the statement only applies to those P3s that basically have fiscal exposure associated with them?

Ms. Payne replied that she thought that was a low threshold and was uncomfortable adopting it.

Mr. Dacey also wondered if that would be a meaningful filter except for that small group of P3s for which there is no exposure.

Mr. Savini then noted that we cannot unilaterally carve out asset types nor can we carve out types of arrangements like leases, sales or transfers. So, staff is not sure how to best address the concern of trying to narrow the population once it is been identified by our definition.

Mr. Showalter proposed deleting paragraph 17 and asking the question when we expose the draft ED to see whether people think the two conditions would be an effective filter. I would take it out and then ask the question do you think they would bring in more than what it was intended or something like that, that our intent is not to do that; do you think this would have you look at more than is intended. In addition, I think it does conflict your characteristics.

However, Mr. Allen prudently noted that we cannot add anything more than we would expose but we can certainly take away. So, with that in mind we could expose the two conditions and then ask the question.

Mr. Showalter concurred.

Mr. Dacey stated that the other issue when we get down to the end is that we have too many things coming in the beginning of this filter. However, if we apply materiality and probability correctly at the end of the filter, you may get to the right answers. In fact, if he were looking at these things, he might consider materiality and probability first because it may screen out things most quickly. That is really the question he sees here is how much do you want to take out in the front-end versus what I think we have as a back- end filter. He was not 100 percent happy with it but a bit happier than we were about the filter on the materiality and probability at the back-end, but the challenge remains that this resides in the non-authoritative Basis for Conclusions. The challenge of the filter is just trying to put enough in the standard itself to be effective. That is really the question, how much do you initially screen up-front. I'm not sure that these conditions screen out a whole lot. The long- live asset filters some away but that is also one of your conclusive characteristics.

Mr. Savini noted that we could leave it in as a filter and drop it out of the conclusive characteristics.

Mr. Allen objected noting that the characteristics are well structured and that the conclusive criteria are pretty clear and sharp.

Ms. Payne reiterated her earlier observation that if we leave the long-lived asset in as a condition then people would interpret that to mean the same thing as the conclusive characteristics. Therefore, you will not have anything come through that filter that does not meet the conclusive characteristics. Therefore, you have nothing to apply the suggestive characteristics to. Then if we expose it and then take it out, we expand the universe, and we do not usually expand the universe without re-exposing. Is that clear?

Mr. Showalter stated that is why we should just take it out.

Ms. Payne agreed and noted that if we could take it out and maybe ask a question about the need for another filter and suggest some other filters.

Mr. Allen agreed and stated that this is probably the best way forward. I think it is fine; the conclusive and the suggestive criteria stand on their own and I like the way they are structured.

Staff noted the decision to delete paragraph 17 and reminded members that in question two we are asking the community specifically about the definition. It will be interesting to see what the community-at-large might advise us concerning changes to the definition.

Mr. Allen the inquired about the genesis of paragraph 17 and if it pertained to task force discussions; that is, what were the concerns raised - that it would be bringing in too much? He also asked if we exposed paragraph 17 to the task force.

Mr. Reger recalled that this matter came up at the March meeting.

Mr. Savini then stated paragraph 17 did not come from task force discussions and we did not share this with them. The task force did have conversations about the definition and that it would capture many arrangements, but the task force did not specifically seem to be concerned with us capturing too many things because I think they felt that the characteristics would filter many arrangements away. One of the risks is that there are some P3s that are in essence not being reported.

Mr. Allen then said that he views this slightly differently than Mr. Dacey but agrees with his notion of materiality. In other words, I might go through the conclusive criteria and not meet any one of them, but you can be assured that when I get to the suggestive criteria, that materiality is going to be a big factor that is probably going to eliminate all of those arrangements that we are not concerned with. As such, you'll meet the criteria better by taking out paragraph 17. Therefore, if no one objects, why do not we take it out and make sure it is clear under question two.

Turning to Mr. Dacey, Mr. Allen asked him if he wanted to talk about materiality now or later. Mr. Dacey agreed to discuss materiality at this point if it would please the Chairman.

Mr. Dacey began by noting that there are two issues. First, we talked about a piece of that already in terms of dealing with risks that are remote and I do not want to reopen that issue as it is more context when looking at paragraph 19. That is, staff has written in BFC paragraphs A18 and A19 that probability is a subset of materiality but I think they are separate concepts. However, we do say that arrangements that are identified for disclosure should be further evaluated in light of materiality. He wondered if we can make a more definitive statement of what our target is. This gets back to the Chairman's discussions.

If we are looking for potential risks - he would not want to use the word exposure but will use it for the moment - or exposures that after considering probability and materiality should be disclosed, can we define that a little bit more getting into our remote discussion? He does not know if that is a better way to make it clearer that this is the filter we are using here. He is concerned in the body of the standard itself that this is the only language we have which is not capturing the thresholds for disclosure very well. Those are the two points, probability and materiality, that he would like considered and then described sufficiently in the authoritative part of the standards.

Mr. Savini first noted that he did describe in the Basis for Conclusions that probability is in essence a part of materiality consideration especially when we think about cash flows and expected cash flows. As such, I do think that probability works hand and glove with materiality.

Mr. Dacey replied that he agreed with that, but did not know if one's a subset of the other. It is the combination of the two terms that he was not suggesting we use. The question is do we want to state that as part of our standard here and defining those terms as necessary in the Basis for Conclusions. He is not sure the discussion on the evaluation of materiality is operational.

Mr. Savini then asked if Mr. Dacey disagreed with the language in paragraph 19.

Mr. Dacey replied in the affirmative stating that he is not sure it adequately describes the threshold.

Mr. Savini noted that this was because we really did not talk about the threshold at the last meeting.

Mr. Dacey concurred and went on to suggest that it would be better if we had some clearer criteria if this is effectively our filter.

Mr. Savini asked members to go to paragraph A10 and noted that one of the things staff learned in going back through prior FASAB deliberations is that the Board has tended to historically shy away from discussions of materiality because such discussions are best dealt between management and the auditor. There is at least one location where staff found where the Board basically came out and said we are not going to get into that discussion. It is up to the preparer and auditor. Apart from not discussing this at the last meeting, this is another reason why I did not elaborate more than trying to say that materiality should have qualitative as well as quantitative considerations. Please refer to A10, paragraph D, that is the language that I have here for materiality. Simply put, the Board has been vague about it and did not purposely want to wade in those waters.

Mr. Dacey stated that he appreciated that but what he does not see what the Chairman was saying is our target; that is, to identify the possible future risk of loss associated with these contracts and the subsequent application of probability and materiality factors. However, he does not know what that right threshold is. In other words, we are basically saying that if it meets the suggestive criteria, you move forward, you think about materiality and that is it. We do not say what that materiality relates to. If it is a firm number that is generally recognized as something easier to judge, for example, a number you're going to have in your books; determining if it is material or not is fairly clear. However, when we are talking about the potential risk, it may not be as clear. He is not sure SFFAS 5 has anything clear to offer in this regard either.

Mr. Savini replied that where staff has tried to make it clear is by introducing the notion that you have got to also include qualitative considerations in materiality and not just look at the quantum. That was my attempt to say you have got to take a harder and broader look at this as opposed to just looking at the dollars. However, when I went back and I saw that the Board did not want to give proscriptive guidance regarding materiality assessments, I felt that we couldn't go that way because we have already set a precedent.

Mr. Dacey agreed that prior Board positions did make this a little more difficult. However, he noted the distinction between materiality over disclosures versus materiality over recognition matters. We may be setting up a slightly different situation here.

Mr. Showalter asked Mr. Dacey if we could we take out the word “materiality” because that is in everybody's mind as a pretext. Could we just say that in reaching the ultimate decision, you need to consider the qualitative and quantitative aspects of the disclosure to identify the risk which should be disclosed?

Mr. Dacey replied that he did not know what the right words are to describe this notion.

Mr. Granof asked Mr. Showalter if he was talking about adopting that language in the standard or the Basis for Conclusions.

Mr. Showalter replied in the standard; specifically, paragraphs 19 and 20 and then asked Mr. Granof if the word “materiality” was creating some angst or concern for him to which Mr. Granof reserved comment.

Mr. Dacey noted that it is not creating angst or concern for him. What he has some angst about is whether we are clear enough about what should and should not be disclosed. For example, a copier lease should be filtered-out and not disclosed. However, if after going through the conclusive and suggestive characteristics, we are still sitting here having to make a decision about the copier lease; he has a concern. Now, others on the Board may think differently and he appreciates that.

Mr. Savini asked Mr. Dacey if his concern is mitigated by the fact that in applying the qualitative factor of materiality, which gives management significant leeway, management can come up with a good reason not to disclose something like a copier lease. In fairness, the auditor might look at something in the quantum sense, but then management can also look at it qualitatively noting that it might be something that should not be disclosed.

Mr. Allen responded by saying that I've always looked at that just in the opposite way. That is, that the only protection for management and their auditors and from their arguing with their auditors about materiality is the quantitative. It is the argument that the auditor would use about why they should do it. It has very little to do with the qualitative so I do not think management can get out of that.

Ms. Payne noted that one of the reasons staff did not find the word “material” in the body of the other standards is that we usually put that word in our usual text-box. Also, we consciously do not put “material” in our standard but instead we say “significant” and then we talk about factors that you can use to identify the significant things that you want to make disclosures for. Would you like us to consider going down that path?

Mr. Dacey stated that Ms. Payne’s suggestion would be a possibility.

Mr. Showalter noted that Ms. Payne’s suggestion is consistent with trying to define quantitative policy.

Mr. Allen then asked about using “significance of future risk or exposure” or something similar.

Mr. Dacey agreed suggesting “significance of the future risk”, or its magnitude. The risk and the magnitude of the risk may be a way to go.

Ms. Payne added that we could say a bit more by providing details of what we mean; i.e., the concept of materiality. However, there are reservations about doing that because like I say, when you get to a pure disclosure standard, this is not something we normally do.

Mr. Dacey agreed but noted that we have done that in other places so it is not a bad idea.

Mr. Showalter stated that we need to make sure it works both ways. We are concerned about having to look at too much, but there may be a situation where the preparer does not disclose something that the auditor thinks is appropriate to disclose. We want to make sure we do not leave the auditor hanging out totally on the back-end as well. You just need enough guidance here so that that both the preparer and auditor can generally get to the same place.

Mr. Dacey agreed noting that the real issue is avoiding a standard where the preparer and the auditor cannot agree on what it means, in whatever direction.

Mr. Showalter agreed noting that you do not want the issuer saying, “Well, the standard says I can do whatever I want.”

Mr. Dacey agreed and said that he hopes we do not convey that.

Mr. Savini then addressed the issue of the disclosures at paragraph 24 on page 19 and asked for comments or questions noting that members have gone through them and the only addition was the one dealing with contractual provisions for termination or default payments and related exit amounts.

Mr. Bell inquired about 24G; “applicable violations of legal and contractual provisions”. Are we literally talking about violations or can it be phrased to say something like arrangements that are made outside of or not pursuant to certain criteria? I'm not discounting their importance but it just seems like we would have a tough time compelling folks to report on something that was a "violation." I'm just literally talking about are we appropriately articulating the right tone with that particular requirement.

Mr. Savini noted that initially we had specified only “material violations” but a Board member objected to the use of “material”. Furthermore, staff stated that he could certainly address tone but noted that GASB requires such disclosures, so it is safe to say that “violations” are matters of fact and should be disclosed.

Mr. Dacey added maybe we can use “non-compliances” with certain criteria. This would be an instance of non-compliance that is known at the time these statements are issued.

Mr. Savini stated that he would like to seek counsel's advice in using “non-compliance” because if you open it to non-compliance, in my opinion, you can be in non-compliance with a whole lot of things. Please note that we are specifically looking for violations of legal and contractual provisions.

Mr. Granof asked what the difference is between that and using the term non-compliance.

Mr. Savini noted that non-compliance is a much lower bar and could sweep in such things as administrative non-compliances. For example, a private partner could be in an administrative non-compliance with a key provision of the agreement, but it might not rise to a legal violation or contractual violation. So, I do not know what we’d gain by using a term that staff believes is expansive. I do not want to wordsmith, but I do want to say I think you must be careful with the word non-compliance, but I'll defer to legal counsel and the Board.

Mr. Dacey stated that if we did use non-compliance, that could result in some exposure. He's struggling with the difference between non-compliance and violation but I think the issue is to focus on the ones that have a trigger like an immediate settlement of the financing or something that would be extreme.

Mr. Showalter said that the reason he would use non-compliance is because that is what the auditing literature refers to.

Mr. Dacey added that non-compliance is what is included in the internal control standard as well. We are talking about compliance with laws and regulations, and contracts and grant agreements.

Mr. Savini again noted that GASB standards also address material violations but that this matter is ultimately up to the Board to decide.

Mr. Allen asked if anyone would object to leaving it to staff and legal counsel to decide what is the most appropriate wording that we could have noting that members just suggested that we use "significant" rather than material. I think that "significant" is a good word choice because you always worry about something. For example, if you're one day late in filing some departmental report required in the Single Audit Act you have to decide what truly matters and what does not.

Mr. Dacey noted that it is really a measure of the impact and that is why he said if you do not like "significant" think about what significantly impacts the federal government's exposure. This would weed out the ones that have little to no consequence.

Mr. Allen agreed but noted that it would not have to ultimately result in an exposure. In any event, the Chairman directed staff to work on this and then circulate the wording to the members.

Ms. Payne agreed and noted that we'd send members separate parts to review.

Referring to paragraph 24e, Mr. Smith suggested a legal review of the word "default" in connection with the above discussion because that is what we are really trying to say; something where they would be in default of a term of the agreement. We can leave this with legal but that is probably another one that they should look at.

Mr. Dacey then addressed that the matter of commitments and contingencies at the tail-end of our conversation at the last meeting may have been left unresolved. He was not sure where we ended up other than some general discussions. Specifically, in 23d of the old version or 24 D of the revised version, we talked about disclosing the amounts that the government can be reasonably expected to incur or pay over the life of the P3 arrangement. It is a matter of clarity first of all and then a matter of policy whether we want to go there. In some respects, he could see if you have contractual commitments over an extended period of time which requires certain payments like our current lease reporting, that might be relevant. But when we say what can be "reasonably expected", that would seem to connote that we would consider any and all risks and the probability in coming up with an expected cash flow. Additionally, it seems to only deal with the outflow side so he's not sure what we are getting at and if we really mean what we say. I do not know if this was decided; I'm not sure it was.

Mr. Savini noted that it was discussed at the last meeting and decided. Specifically, one of your colleagues noted that he felt this was an extremely important piece of information that needed to be disclosed because of the long-term nature of the commitments that are involved. Granted, you have a point about the revenue side, but we can certainly add that requirement in if members would like.

Mr. Dacey then asked what if there are no fixed commitments of any payments, are you supposed to then calculate an expected value of what you might have to pay in the event of a non-performance?

Mr. Savini replied what we are trying to get at here is what can be reasonably expected to occur as a cash outflow.

Mr. Dacey stated that reasonably expected is not a defined term we use anywhere else.

Mr. Savini stated that his point here is that all we are looking for is what the government thinks under normal conditions over the life of the arrangement will be its cash outflow barring any unforeseen violations, default, etcetera.

Mr. Allen noted that “reasonably expected” is a good term and that we should use it.

Mr. Dacey said he thinks that “reasonably expected” may get confused with the concept of expected values.

Mr. Savini noted that the standard says nothing about present (expected) value.

Mr. Dacey’s concern remains that we are not defining this term.

Mr. Savini stated that we could add a footnote and say this does not include present value calculations.

Mr. Allen noted that we are also silent in the case of default. That is, we are not asking preparers to get into any of those projections.

Mr. Dacey said that we need clarity of what we want to have included in this disclosure.

Mr. Allen replied, just the normal expected flows.

In response, Mr. Dacey noted that then these would be payments or receipts under the terms of the contract.

Mr. Bell agreed that these would be payments or receipts under the terms of the contract, but noted that he thought clarifying whether we are dealing with present value or not is an important one.

Mr. Allen said he did not agree because the disclosure you're going to see is, for example, we expect to pay $5,000 a year over the next 20 years. Now one can discount that back if they would like, but I think that matters more for recognition than it does disclosure.

Mr. Bell asked about ensuring some level of comparability. If you have got one organization reporting it one way, another organization reporting it another way then you're going to be mixing current and future dollars.

Mr. Allen replied that staff has already told us there are not any two of these P3s that are identically alike so comparability is not as germane as one would like or think.

Mr. Savini stated that Mr. Bell does in fact make a very valid point and that because in many of these arrangements the internal rate of return is calculated, those discounting techniques, or more precisely, the present value figures are known because that is how they base their decision. However, in order to get to the present value, they have to begin with the un-discounted amount. I think it does pay for us to specify what we would like. Staff would advise using then-year or un-discounted dollars for simplicity's sake.

Ms. Payne noted that if we select then-year or un-discounted dollars, you would want it to show for all the years covered under the contract or arrangement.

Mr. Bell asked if this is something best left for implementation guidance to which Ms. Payne replied in the negative.

Mr. Allen then asked if staff meant over the life of the contract to which Mr. Savini replied in the affirmative.

Mr. Bell then asked if we wanted a total or year-by-year break-down or basis disclosed.

Mr. Showalter noted that we say consolidated so he'd assume it is one number.

Mr. Savini agreed with Mr. Showalter that the intent is just to have one number disclosed.

Ms. Payne asked if there was any indication of the time period over which you pay that total non-present value amount.

Mr. Showalter replied that since you can aggregate these disclosures, he was not sure how having a time-frame or period would work.

Mr. Dacey responded by saying that we do that for the non-cancelable leases and typically we have year-by-year and then beyond (future) the cumulative year.

Mr. Showalter noted that is not what we are asking for here. You could get a large number that says $20B, but what does that mean?

Mr. Smith then said when we are looking at this disclosure we should keep in mind that it is more of financing over the long-term and not really trying to get information akin to leases. The basic question is this, what is our annual commitment on these arrangements. Either way seems to be fine.

Mr. Allen then asked members to decide and then to allow staff to write it that way. Do you want to just see a lump sum number over the life or a year-by-year?

Mr. Showalter said because in essence, this is a type of financing, we just want to know how much of it is being signed off or assumed.

Mr. Dacey then added that there is a lot of context to this issue and that it is hard putting it into a standard. Obviously, if you say we have got payments of $1,000 a month for 40 years, that is easy to do. But variable payments, it is harder and is something that he does not mind but assumes would be accompanied with some narrative which explains the basis for the cash flows that we are estimating so that the reader is not just looking at a number, but understanding what that number represents.

Mr. Smith noted that the payments could be based on usage or something else that might be variable. However, it seems that the disclosure should be some amount that they are going to have to pay over the life of the P3. Therefore, this is the least amount of information that we should capture; that would be my minimum that I'd want disclosed.

Mr. Allen then asked if we just said a description of the amounts the government would be expected to pay and then guidance on telling preparers what to explain. For example, a preparer can say over the next 20 years it is $100,000; or I have to pay $1,000 a month for the next 20 years unless the occupancy drops below 50 percent and then I've got to pay the difference; or something like that. I think we care more about the description than the amount, do we not?

Mr. Showalter then asked Messrs. Reger and Bell a question: Who do you think will actually get and read this material? Do you think the paragraph 25 consolidated disclosures will apply? I know you do not know what you do not know, but what do you know?

Mr. Bell stated it is impossible to tell at the moment but the government-wide level disclosures are less likely from a materiality perspective.

Mr. Reger noted that they will not know that answer until the DoD reports.

Mr. Dacey noted that the DoD has a larger materiality threshold.

Mr. Showalter concluded that this is where he sees a conflict, meaning that agency reporting is probably going to be more in play with the government-wide reporting.

At this point, Mr. Dacey asked the Chairman for clarification. That is, are we limited to “expected” or “under the terms” -- I'm still struggling with “under the terms of the agreement”. Is this what we are aiming at?.

Mr. Allen asked if inserting the word “description” helps. For example, “description of the amounts” tells me something more than just giving me a dollar figure.

Mr. Dacey stated that he thought that would help, or you could make it an option as to what the best presentation is; additional payments.

However, Mr. Showalter cautioned against creating options as he envisioned FASB 13 in trying to come up with all the deviations on what payments are. He does not think we want to get into that detail dealing with payment rules. We have got to be careful we do not go down that route.

Mr. Dacey acknowledged that complication and stated that is why he thinks it is important to explain not only the number but a basis for what you're communicating to the user that the number it represents.

Mr. Showalter concurred.

Mr. Smith then said that it seems like a description would satisfy because then it would be up to the preparer to determine if that was going to be informative so now you'd have context concerning what you're paying for.

Mr. Allen responded by saying that he would say that is what you want and not these specific amounts each year.

Mr. Smith concurred.

Ms. Payne then asked if members wanted the single amount on a non-net present value basis.

In reply, Mr. Allen said he did not think the question is do you want the single amount on a non-discounted basis or number. My answer is that it does not matter; just describe what it is your disclosing.

Ms. Payne noted that was fine and asked a clarifying question concerning amounts to be paid by the government. She pointed to DoDs large program involving military housing where the government pays the service member, and the service member then pays the housing partner. Do members envision something like that being included as an amount paid by the government?

Mr. Smith answered by saying that if we require a description of how the P3 is paid, you would expect the preparer to describe how the government pays the private partner(s), that is, as an amount through the base housing allowance (paid to the individual service member) which is then paid to the P3 by the service member. Now, that may be a leap to say a preparer is going to actually go and describe that but if you really want readers to understand, you would think that you'd be trying to say how is the P3 or third-party being paid, and you would describe that transaction. I think that is all we would want to know.

Ms. Payne thanked Mr. Smith, finding his thoughts most helpful.

Changing the topic, Mr. Steinberg asked members to consider Appendix B and whether the illustrations add to the draft ED.

Messrs. Granof and Showalter questioned their usefulness and noted that they were not referenced to any of the provisions.

Mr. Savini noted that these are educational in nature showing respondents in the first illustration what some of our thinking is regarding why we are going with a more macro approach on P3s than what the IASB or GASB have done just focusing on service concession arrangements. That is why you see the hierarchy here. The second illustration is to make clear that we are concerned about P3s just not when they are external to the agency through let's say the formation of a special purpose vehicle, but can also include internal activities. Staff noted the members' concerns and agreed to delete Appendix B in its entirety.

Redirecting the discussion, Mr. Dacey noted to the Chairman that conceptually if you go down this process, he believes we will have disclosures related to contractual agreements that are not really P3s per se and this is because of our broad P3 definition. Mr. Dacey noted that he is not troubled by this because it is the nature of the risk that is driving this. However, do we need to say anything about whether it is a P3 or not if it meets these criteria?

Mr. Showalter noted that as long as the P3 is disclosed based on its risk attributes, why would the Board concern itself with something outside its scope.

Mr. Dacey noted that he was thinking out loud if the Board would need to put anything in here that clarifies that it was our intent that things that may not be traditionally thought of as P3s may be included.

Mr. Bell asked if that would that be something for a FASAB interpretation after-the-fact.

Mr. Dacey said that we could possibly ask a question if such guidance would be useful, however, he was troubled that potential arguments could ensue whether an arrangement meets this P3 definition or not.

Mr. Granof stated that we ought to be guarded and Mr. Showalter said that the only down-side is that we may get an extra disclosure.

Mr. Allen then asked Mr. Dacey do you want the disclosures even if there is a risk that what an entity describes is not a P3?

In reply, Mr. Dacey said that you do not need to go to that determination if it generally meets the P3 criteria in a very broad sense.

Mr. Allen clarified why he asked the above question noting that it was because he looked at the other side of this -- the question I would ask is do you believe this will sweep-in more organizations or more structural arrangements than the Board intended or something like that. After all, we discussed earlier in this session what is going to be included as a P3 and that we have to be careful not to sweep-in too much. This is why staff added paragraph 17 as a filter. So, I would not want to put anything in that says if you even think you're close to this, we want the disclosures.

Inquiring further, Ms. Payne asked if members would rather ask the question in the context of do you believe there are other arrangements besides P3s for which the risk characteristics are present and, therefore, disclosure should follow.

Mr. Dacey replied in the affirmative noting that there are two parts to that. If a preparer thinks there are, disclosure would be appropriate or do we need to somehow scope those out? That is the question. That would be a good way to do that.

Ms. Payne then stated that the Board should be careful not to say we should just not bother to define P3s at all.

Mr. Dacey agreed.

Mr. Allen noted that we could ask if preparers think or believe this will actually capture more organizations that do not have legitimate risk.

Ms. Payne said that would be fair to ask.

Mr. Dacey then added a subpart to that question. That is, if in fact we have something that already has disclosures, are these P3 disclosures on top of those disclosures? For example, we have SPVs at entities accounted for under credit reform so would we expect that these disclosures would be on top of the disclosures that are already present for them?

Mr. Savini said that his understanding about disclosures is that standard-setters usually do not set a structure for them like an order of precedence or do not ordinarily give that type of advice on writing footnotes. We might make suggestions that you start off with the Statement of Significant Accounting Policies and then you progress from there. As such, it would stand to reason that if there was disclosure overlap, and there will be in some cases specifically as you mentioned, you would think management could easily deal with overlap by either referencing or curtailing the subject notes.

Mr. Dacey emphasized clarity. Do we say that we want you to provide these disclosures even if you have other disclosures?

Mr. Showalter said yes, we want you to do these disclosures even if you have other disclosures.

Mr. Allen stated that in other words, what we are putting forth here is what disclosures are required but you have already got 80 percent of them elsewhere, we are only talking about the 20 percent here.

To which Mr. Dacey replied, that is fine, but it is a matter of clarity; do we need to clarify this to preparers?

At this point Mr. Reger asked members to pause for a moment noting that this creates an interesting question that he had not thought about. We are not necessarily talking about a P3 footnote rather we are talking about disclosing this information in the place where it is most appropriate. Now, if we had a place where there was something that we were going to disclose anyway but, incidentally it is also a P3 arrangement, we would just ensure that in that other disclosure we include the required disclosures we are establishing here; is this what we are saying?

Mr. Dacey replied in the affirmative noting that we need to clarify that this is in addition to, rather than instead of, these other disclosures that are required under other standards.

Mr. Reger again asked, do we do that in general?

In reply, Mr. Dacey said we do not have too many places where we have conflicting disclosures like this that come up.

Mr. Savini reminded members that Mr. Reger made a recommendation at the last meeting that staff incorporated in paragraph six on page nine, we added that “such disclosures should generally accompany the related asset and/or liability display contained within the financial statements”.

Mr. Dacey said that he understood location and that is where the disclosure can reside but all I'm saying is we are going to have some disclosures required by credit reform, related to SPVs and he would not want anybody to read this and say well, these are the disclosures for SPVs and I do not need to do these other P3 disclosures related to SPVs.

Mr. Showalter suggested that we can fix that by going into paragraph 24 and just saying if these disclosures are not disclosed elsewhere make sure to include them or something like that if you have a concern.

Noting the agenda and remaining time, Mr. Allen and Ms. Payne concluded the P3 session by asking members to contact staff if they had any additional editorial or technical matters to discuss.

Conclusion: Mr. Savini will revise the draft and circulate it, or specific portions, for review before the June meeting.

- **Fiscal Sustainability – Deferral of Transition**

Ms. Payne introduced the request for deferral by noting two reasons for the request -- the audit guidance that the American Institute of CPAs (AICPA) is developing has not been completed and the unprecedented staff shortages at the Office of Management and Budget (OMB). The draft provided to members is largely an update of a similar proposal issued previously.

Members approved two changes to the draft – the deletion from the Executive Summary of a paragraph explaining the difference between basic information and required supplemental information (RSI) and the omission of the reference to staff shortages at OMB. Members noted concern that reliance on the staffing issues to justify a deferral could set a precedent.

In response to a member's question, Mr. Dacey provided an update on the AICPA's progress. He explained that a proposal was made to the Audit Issues Task Force several weeks ago and an alternative is being prepared based on feedback from the AITF. He understands that the alternative may need to be reviewed again by the AITF and the Audit Standards Board (ASB). The guidance will not be in new standard. Instead it will be an interpretation in question and answer format.

Members asked about the content of the guidance. Mr. Dacey responded that it would clarify the wording of the audit report consistent with the clarified audit standards. Some had proposed to eliminate the word "fairly" from the phrase "fairly presents" but that proposal was not adopted. Also, the guidance will clarify that the opinion is provided under the audit standards and not under other standards.

Mr. Steinberg asked why someone would remove the word "fairly"?

Mr. Dacey noted that at least one firm was concerned that referring to a projection as "fairly presents" might lead to misinterpretations. There are two views of the meaning of "fairly presents." He ascribes to the view that "fairly presents in accordance with GAAP" means that the auditor assesses GAAP compliance and overall fair presentation. That is, that there is nothing misleading in the information and it is not omitting anything that would be necessary to understand the situation. Others ascribe to the view that "fairly presents" is a much broader stand back view of the statements being a "fair presentation of the status of the entity."

Mr. Bell noted that Treasury is certainly in support of the year of deferral. He referred to a memo provided last year expressing Treasury's support for the prior deferral. He added that with this year's deferral, Treasury would like to discuss the auditability of this information in general. There are some concerns, some significant concerns at Treasury, as to the auditability of this information conceptually. He noted that the discussion should begin soon so that we do not face this issue at the same time next year.

Ms. Payne suggested that the discussion begin at the next meeting (June). She would like to invite the experts who prepare this information and the experts who audit this information to identify the issues that would make it less auditable than desirable.

Conclusions: Staff will provide a ballot draft incorporating the agreed changes following the meeting. Treasury will coordinate with staff to present information regarding auditability concerns for the coming meeting.

- **Three-Year Plan**

Ms. Payne introduced the three-year plan discussion. She noted that she had listed any projects that were either on the research agenda from the prior year or mentioned by respondents to the three-year plan. She also included the Department of Defense request.

Members asked for an update regarding Congressional outreach efforts. Ms. Payne noted that she met with two staff directors for members of the CPA Caucus and hoped to follow up with a briefing to the Caucus as well as outreach to individual Caucus members. She indicated that staff met with staff from seven committees regarding the lease standards. All but one meeting showed staff were excited about the idea of seeing comparable information across the government regarding leases. Information they were interested in included a full inventory with an associated present value and the interest expense component in the leasing activities.

Ms. Payne also reported that she contacted Department of Defense (DoD) staff regarding the current state of inventory accounting. She found that they do not yet have a consistent approach across all the services. The services changed systems, inventory systems, beginning in 2002 and some changed as late as 2008. So it is possible that there are some items in the moving average cost that were entered at the latest acquisition cost rather than a true historical cost average.

Ms. Payne also noted that for reparable items, the challenge is greater because they are older and cycle in and out of inventory. She noted that one may believe estimating the historical cost of inventory would not be as challenging as for property, plant and equipment. However, she was not persuaded this is true since inventory may not turn over quickly.

Ms. Payne also noted that doing the same thing that we gave them permission to do in SFFAS 35 would probably not be as effective at reducing the cost of implementation. She wondered if they would have budget documents for small components of an overall aircraft or inventory purchases. She thought the number of items and the age will be quite variable. She expressed the view that there is little value in precise estimates in this area. She hoped that guidance could be developed that would reduce the cost of implementing the 15-plus year old accounting standard.

Mr. Allen asked if a very significant increase in the materiality level – that is, the capitalization threshold - would be helpful.

Ms. Payne said she did not think they would be using the same approach with their inventory because it is an aggregation and it is very much a management system.

That said, she would consider how materiality might aid in reducing the cost.

Mr. Allen agreed that DoD should not waste a lot of time coming up with things that they do not have. He did note that inventory has more direct meaning because it is the cost of goods.

Ms. Payne noted she also discussed with DoD staff the revolving fund item. This topic really came down to the statement of budgetary resources. She suggested the revolving fund item come off the FASAB list and OMB assistance be solicited.

Mr. Allen asked if there were questions about the projects. Regarding currently active projects, he noted that members could remove these if they wished to prioritize one lower.

Mr. Showalter asked about the budget reconciliation project and if it was a budget-to-actual.

Ms. Payne noted that it was the budget-to-accrual reconciliation but would not be a budget-to-actual in the traditional sense. It would follow up on the AGA study that suggested better alignment between the government-wide and the agency reconciliations. It would include the auditor comments that note reconciliation is more variable than it used to be when it was the statement of financing. They indicated the not lacked understandability and better labeling of the items would help.

Mr. Reger asked about the DoD request on accounting for internal-use software.

Ms. Payne explained that this was actually about research and development leading up to a new weapons system – which DoD likened to internal-use software. They asked for help to determine the proper timing of capitalization in a changing R&D world similar to IUS issues as methods moved from linear to spiral development.

Members asked about the break out of the DoD's six items. Ms. Payne responded that the AAPC will be addressing the contract financing payments question. Of the remaining three (inventory, deployed assets and R&D) she recommended that if members want to take on all three, we put one staff person on and form a task force with subgroups. The larger team would then address this with one staff person as support. In voting for priorities, members should alert her that they do not support addressing one of the individual pieces of the DoD request.

Members noted that some of the DoD requests could become major projects. Also, in the end, success relies on DoD's willingness and ability to do the work it takes to implement.

A member asked if these were critical issues and if DoD was likely to follow through.

Ms. Payne said she would assume they are critical issues and noted they have been around for a long time. The fact DoD was willing to make a request suggest there is readiness to address solutions. In the past, FASAB was aware guidance would be needed but left it to DoD to identify the point in time when the guidance could be most helpful.

Mr. Steinberg noted that he likes a lot of the projects, but DoD is still not auditable. It may be partially because their stuff is so complex, so unique, so different. It may be partially because they do not have the right attitude. It may be partially because over the years, DoD just never paid attention to it. But if we're going to hit the point where the federal government can get a clean opinion, DoD is going to need a clean opinion. If we could help them simplify the requirements for some of the things that they do that are different and difficult then it is worth giving up one of the projects wanted.

Having said that, he added that we have to approach it the right way. We have to make sure that they are committed to doing this.

Members briefly discussed options for additional staff support for the project.

Mr. Smith asked about the existing research projects and why they were priorities.

Ms. Payne noted that the research projects were identified the prior year. The only update relates to the oil and gas project. She had a briefing from the Interior staff who developed the estimates for natural resources. They estimate the cost at the RSI level of developing estimates to be $170,000. They find the information useful at that level. They believe the cost would be extraordinary to transition to basic and, therefore, they advised not to transition to basic.

Some of the challenges they identified were that reserves are underground and estimates are provided by the Energy Information Agency on a nationwide basis. Estimates of proved reserves are not stratified by federal and non-federal. So you get a state amount proved reserves and then, of course, you get the off-shore proved reserves.

Interior determines the federal part is to look at the current year's production at a particular state, and they are able to say what the federal piece is because they got the royalties. Based on that annual split, they then figure out the what is in the ground that is federal. That's very imprecise. Production may bear no relationship to the quantity in the ground.

Then they have to estimate the timing of it coming out of the ground and that is influenced by price and by technology. The timing can change dramatically.

So they project the price forward and then bring it back to a present value. They described it as an “estimate of estimates of estimates.”

Ms. Payne noted the first and most critical step of an oil and gas project would be outreach to stakeholders to see if they find the information useful and do they need to have it in a note or recognized in a basic financial statement.

Mr. Allen asked members to name their highest priorities from among the potential projects. The following table shows the members’ rankings.

	PROJECT	Tom Allen	Scott Bell	Hal Steinberg	Sam McCall	Michael Granof	Scott Showalter	Gray Smith	Bob Dacey	Mark Reger
1	Department of Defense Request	1	2	1	1	Funded	1	1	1	1
2	Managerial Cost/Linking Cost to Performance		3		2	2	3	3		
3	Tax Expenditures	3		4						
4	Budget to Accrual Reconciliation	4	1		3	3	2	2	2	3
5	Evaluation Existing Standards									2
6	Inter-gov Financial Dependency									
7	Electronic Reporting	2		2		1				
8	Intangibles									
9	Derivatives									
10	Internal Use Software			3					3	
11	Asset Retirement Obligations									
12	Natural Resources									

Ms. Payne noted that means the DoD request is the first; reconciling budget to accrual is second; and managerial costing cost to performance is third; and then electronic reporting and internal-use software.

Some members expressed regret that tax expenditures could not be addressed as well.

Ms. Payne noted staff would begin by requesting a meeting with the DoD staff but that we will not fully staff this until we complete the reporting entity project.

Adjournment

The meeting adjourned at 4:00 PM.