

Withdrawal/Redaction Sheet

Clinton Library

DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. outline	re: Japan, Asia, & the Yen (2 pages)	06/13/98	P5

COLLECTION:

Clinton Administration History Project

OA/Box Number: 24124

FOLDER TITLE:

[History of the Department of the Treasury - Supplementary Documents] [9]

jp38

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]

- P1 National Security Classified Information [(a)(1) of the PRA]
- P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
- P3 Release would violate a Federal statute [(a)(3) of the PRA]
- P4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA]
- P5 Release would disclose confidential advise between the President and his advisors, or between such advisors [(a)(5) of the PRA]
- P6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA]

C. Closed in accordance with restrictions contained in donor's deed of gift.

PRM. Personal record misfile defined in accordance with 44 U.S.C. 2201(3).

RR. Document will be reviewed upon request.

Freedom of Information Act - [5 U.S.C. 552(b)]

- b(1) National security classified information [(b)(1) of the FOIA]
- b(2) Release would disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA]
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- b(7) Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA]
- b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
- b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

ADMINISTRATION HISTORY APPENDIX
CHAPTER TWO: INTERNATIONAL ECONOMIC ENGAGEMENT

YEN

1998-SE-007142

File copy

TO WATCH OFFICE:

FROM: Timothy Geithner

Please forward to Secretary, Summers, Lipton ASAP. Fax to Truman at the FRB. And cc: to Gagnon and Dulaney.

Thanks.

*Loj
and
Peter*

June 11, 1998

MEMORANDUM FOR SECRETARY RUBIN
LAWRENCE SUMMERS
DAVID LIPTON

FROM: Timothy Geithner

SUBJECT: The Yen

The Deputy Secretary and I had a number of conversations on the subject of the yen during our meetings in Paris, and he suggested I put on paper some of the ideas we discussed.

My concerns are these:

- The markets perceive a serious risk that the yen could weaken significantly further. Sometimes the strength of a conviction implies the worst may be over, with everyone already positioned in anticipation of the expected, but there are very strong fundamental reasons to support this fear of a further decline.
- The general consensus is that a significant further decline in the yen would be very damaging to Japan's trading partners in Asia, with the direct effects most acute for Korea, Taiwan, and possibly Hong Kong, but with China and the rest of Asia ultimately vulnerable as well.
- It is possible that the fear of, the perceived risk of, the decline is more of a problem than an actual decline would be. If this is true, then getting the decline out of the way would be beneficial for the region. This is something that is impossible to know with confidence, and it's a proposition that is dangerous to test.
- As always, it is hard to know on the basis of fundamentals whether the yen should weaken significantly further, has already overshot, or is about right.
 - With Japan's current account surplus now on a path to approach four percent of GDP, the models that pay attention to external sustainability tend to view the yen as wildly undervalued at current levels. These models have not proven to be a particularly accurate measure of how exchange rates move, even over periods of time measured in years.
 - On the other side of the argument, the yen has not declined that much in real effective terms over the past year, despite a very dramatic deterioration in both reality and perceptions of the real economy and the financial system. In part because of intervention and noise from the Japanese officials, the market may not

have fully priced in the deterioration that has already occurred.

- We are unlikely to see any changes in policy or fundamentals in Japan over the next several weeks or even months that will be dramatic enough to improve confidence.
 - The economy is likely to continue to deteriorate in the short term.
 - Fiscal policy is now essentially set. Prospects of permanent tax cuts seem to have receded. They are likely to take a run at revenue neutral package personal and corporate tax reform, but this won't help the short-term problem. At some point during the next few months, the substantial money in the recent package will start to flow. This will help, but there's no talk now in Japan of a second fiscal package.
 - The Government's financial system strategy seems to be evolving toward an approach closer to the one we have suggested. But this won't be outlined in more concrete terms clear until mid-July, and even then there will be a lot of fog and uncertainty and skepticism until we start to see actions on the ground.
 - Monetary policy seems likely in the short term to continue to have the effect of putting downward pressure on the yen, as the BOJ continues to supply liquidity to the banking system.
- In this context, we face, under the best of circumstances, a period of limbo, with no help from policy, and no good hook to use as a device to try to change sentiment in exchange markets.
- I still think we can be reasonably confident that the dollar is doing us more good than harm.
 - The appreciation in real effective terms has been significant -- between 10 and 15 percent or so against the average of the past five to ten years. It has begun to affect earnings and expectations of earnings, and it is clearly one factor contributing to the expected deterioration in our current account deficit.
 - So far, however, these costs do not seem that significant. And the benefits of the appreciation in terms of lower inflation, lower interest rates, and some restraint on growth are much more compelling.
 - It is more appropriate for us to be worried about the consequences of a significant further rise in the dollar, than to be concerned about the present level.

- A final point on the present context. The market now perceives us to be resigned to the yen's fall, cheerleading the dollar's rise, flirting with the possibility of the monetary expansion/yen depreciation strategy for Japanese recovery, and unwilling to cooperate with the Japanese in trying to put a floor under the yen without more fundamental change in policy. The market also perceives the threat of intervention by Japan to have receded and is impressed by the apparent support in the official community in Japan for letting the yen fall.

- In general, I think one should view skeptically the effect of these perceptions of official policy on market behavior. But they may be contributing to the negative sentiment about the yen, and correcting them could make some difference.

In the context of all this, my inclinations are to recommend the following steps:

- On the policy front, we should maintain our present emphasis on a macroeconomic policy stance (substantial fiscal stimulus with monetary policy about where it is now) that would help produce domestic demand led growth and reduce the risks of a damaging further weakening of the yen, and not embrace at this stage the alternative strategy of radical monetary expansion.

- In this context, we should explore the possibility of a new set of fiscal measures that could be put in place later this year if necessary and continue to look for ways to reinforce the apparent shift in Japan to a more aggressive strategy to strengthen the financial system.

- We should shift our public formulation on exchange rates to emphasize more explicitly our concern about the weakening of the yen, and the risks this presents to Japan, to Asia, to Japan's external surplus, and to the system as a whole.

- In this context, I would suggest we give less prominence to emphasizing continuity in our policy, and less emphasis on the strong dollar mantra. And I think it would be helpful if we could reduce the market's current conviction that we have foreclosed completely the possibility of intervention, which could be done simply by stating that we are watching developments in the markets closely and that we are in close contact with the G-7 and Asian authorities.

- The challenge here is to frame a clear message about the yen that does not imply that we think the dollar has necessarily become too strong.

- And in talking about the yen, I think we want to preserve

ambiguity about what we think about the current level. We should not state with conviction it has gone too far, because we can't know that with confidence. And we should not consent that our objective is necessarily to strengthen it, though that might be the natural consequence of a successful macroeconomic and financial system strategy to restore confidence.

- We should consider the merits of exchange market intervention to send a more forceful signal of concern about the yen, to help provide a bridge to the policy measures now coming on stream in Japan, and to help reduce the risk of a damaging further decline.

- On option would be to conduct a concerted operation with the United State, China, Hong Kong, Singapore, and Germany. By including the countries in Asia who have the capacity to use their reserves in this way and who are most vulnerable to the yen's fall, by making the operation global, and by making it obviously focussed on the problem of the yen, rather than the dollar, we could reduce some of the risks involved in intervention.

- We may be approaching conditions which would make intervention effective. The market seems to be very short yen, though it's never really clear what that means. Expectations of intervention have receded. And there are policy measures coming on stream in Japan that are likely to help strengthen the fundamentals over time, although at this point these look unlikely to be sufficient.

- On the other hand, there are lots of reasons to think a concerted operation would fail, and could be damaging. The market's perception of the fundamentals in the U.S. and Japan suggest the yen should weaken further. Action by the United States to sell dollars would be a consequential act, and could be particularly dangerous given the fragility of sentiment around U.S. equity prices. We might not be able to convince the markets that we are interested in stabilizing the yen, not in weakening the dollar. And failure could precipitate a sharper decline in the yen than might otherwise have occurred, by dramatizing the force of the fundamental pressures against the yen.

- Finally, I think it would make sense to call a special meeting of the Manilla Framework Group of finance and central bank deputies, perhaps as early as next week.

- This would provide a chance not just to review where we are in the

Asian crisis and explore whether there are new initiatives we could be considering to help, but also to dramatize the problem of the yen and mobilize broader pressure on Japan to act.

- Of course, meetings like this can be damaging without a clear sense in advance of what could be achieved in practical terms. But we could probably come up with a common statement that would help our objectives.

URGENT

June 14, 1998

MEMORANDUM FOR SECRETARY RUBIN
DEPUTY SECRETARY SUMMERS

FROM: Timothy Geithner *TG*
SUBJECT: Japan, Asia and the Yen

Attached is an outline of the scenario we discussed earlier today, with the following sequence of steps.

- POTUS call to PM Hashimoto
- U.S. exchange market intervention, with Japan, in yen early in the week, possibly Tuesday.
- Followed closely by PM's statement.
- Calls to Chinese and other Asians.
- Possible G-7 Statement.
- LHS trip to Japan and China.
- Manilla Group meeting.

cc: Lipton, Froman
Greenspan, Truman, Fisher

URGENT

Withdrawal/Redaction Marker

Clinton Library

DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. outline	re: Japan, Asia, & the Yen (2 pages)	06/13/98	P5

**This marker identifies the original location of the withdrawn item listed above.
For a complete list of items withdrawn from this folder, see the
Withdrawal/Redaction Sheet at the front of the folder.**

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Possible Statement by Secretary Rubin following intervention operation

The U.S. monetary authorities operated in the exchange markets this morning to support the yen, in cooperation with the monetary authorities of Japan. We believe a strong and stable yen is critically important for Japan, for the nations of Asia, and for the world economy as a whole. The Japanese Government is committed to taking actions to strengthen domestic demand and restore the health of the financial system, which will help create the conditions that are essential for exchange rate stability. We look forward to implementation of an effective program over the next few months. Japan has the financial resources and the capacity to deal with the challenges it faces, and the international community has a large stake in seeing it succeed. We are prepared to continue to cooperate in exchange markets, as appropriate, as these new policies are put in place.

*US DRAFT
6/12
WJ 20175*

Elements of a Statement by the Prime Minister

A strong and stable yen is of vital importance to Japan, to the recovery of Asian countries affected by financial market turbulence, and to the entire world economy.

Toward this end, the Government of Japan is committed to taking all necessary steps to achieve domestic demand-led growth, to restore its banking system to health, and to open and deregulate its markets.

We are committed to accelerate the implementation of the recently enacted substantial fiscal stimulus package. Indeed, we project that over 80% of all budgeted public works projects will be contracted by September 1998. *with Act Told*

*amounting to ¥ 20 trillion
corresponding to 8% of GDP*

In addition, we are committed to expedite the implementation of public works contained in the economic measures just approved amounting to ¥ 7.7 trillion, corresponding to 1.5% of GDP, starting from July, 1998.

We are prepared to ~~take~~ ^{take} additional future fiscal actions, including tax reductions, as needed to ensure that recovery is established and sustained.

we also intend to reform tax structure, including corporate tax and individual income tax, which will contribute to revitalizing Japanese economy.

The Government of Japan is committed to an expeditious reform of the financial system based on the following four action proposals:

1. *Dispose of bad assets more aggressively*

The overhang of bad assets needs to be liquidated to restore confidence and lending activity. The Japanese Government will actively encourage Japanese banks to sell off bad assets and will put in place the legal and institutional measures necessary to sell the collateral underlying bad loans.

2. *Rapidly resolve insolvent institutions and restructure weak ones*

The "convoy" system will be abandoned, ~~weak and~~ insolvent institutions will be closed or merged. The use of public funds to assist viable institutions to remain open will be conditioned so as to improve management and corporate governance.

3. *Improve transparency and disclosure*

Recognizing the importance of transparency and disclosure in improving capital market efficiency and reducing uncertainty, Japanese banks will be required to disclose the full extent of nonperforming loans based on world-class accounting and disclosure standards by ~~September 30, 1998.~~

4. *Strengthen banking supervision and prudential standards*

Government oversight and supervision of the financial sector will be improved to ensure that prudential standards are being met and to thereby promote confidence in the system. The new Financial Supervisory Agency will receive stronger enforcement powers and more examiners.

Finally, the Government of Japan is committed to take further actions to open and deregulate the economy to improve real incomes of the Japanese people.

ADMINISTRATION HISTORY APPENDIX

CHAPTER THREE: IMPROVING FINANCIAL SERVICES, AND MARKETS AND THE
FEDERAL GOVERNMENT'S FINANCIAL MANAGEMENT

ACCOUNTING

FINANCIAL

ACCOUNTING

STANDARDS

BOARD



DEPARTMENT OF THE TREASURY
WASHINGTON

Action Deadline: March 23
March 16, 1993

ASSISTANT SECRETARY

MEMORANDUM FOR SECRETARY BENTSEN

FROM: *fr* Gerald Murphy
Fiscal Assistant Secretary

SUBJECT: Request to Approve Federal Accounting Standards
Advisory Board (FASAB) Interim Accounting Standards
Guidance

ACTION FORCING EVENT:

Elmer Staats, Chairman FASAB has transmitted the Board's completed action on revised interim accounting standards guidance. The existing interim accounting standards need to be revised as a result of recommendations from FASAB along with other guidance such as financial statement form and content requirements issued by the Office of Management and Budget. Mr. Staats requests your approval of the interim accounting standards guidance as one of the three principals for FASAB. Requests for similar approval have been transmitted separately to the Director, Office of Management and Budget and the Comptroller General of the United States.

RECOMMENDATION:

That you sign the attached FASAB RECOMMENDATION FOR REVISED INTERIM ACCOUNTING STANDARDS GUIDANCE approval sheet.

Approved _____

Let's Discuss

BACKGROUND/ANALYSIS

This recommendation is necessary to provide the audit community with timely guidance in selecting appropriate guidelines/standards in performing their audit of federal government agency financial statements. Current interim accounting standards no longer provide appropriate guidance. As Treasury's Board representative, I believe approval of this recommendation is essential to allow effective and efficient audit efforts to continue.

ATTACHMENT: FASAB Recommendation for Revised Interim Accounting Standards Guidance for Signature

cc: Frank Newman

g-k

Edward S. Knight

RECOMMENDATION FOR REVISED
INTERIM ACCOUNTING STANDARDS GUIDANCE

The Federal Accounting Standards Advisory Board (FASAB) recommends that the Interim Accounting Standards Guidance issued as a result of the Board's recommendation of March 29, 1991 be revised as follows:

Until a sufficiently comprehensive set of accounting standards are agreed to and published by the Joint Financial Management Improvement Program (JFMIP) principals, which will constitute "generally accepted accounting principles for the federal government", the following hierarchy shall constitute an "other comprehensive basis of accounting" and shall be used for preparing federal agency financial statements:

1. Individual standards agreed to and published by the JFMIP Principals.
2. Form and content requirements included in OMB Bulletin 93-02, dated October 22, 1992.
3. Accounting standards contained in agency accounting policy, procedures manuals, and/or related guidance as of March 29, 1991, so long as they are prevalent practices.
4. Accounting principles published by authoritative standard setting bodies and other authoritative sources (1) in the absence of other guidance in the first three parts of this hierarchy, and (2) if the use of such accounting standards improve the meaningfulness of the financial statements.

Disclosing differences between the accounting standards being followed and Title 2 of GAO's Policy and Procedures Manual for the Guidance of Federal Agencies is no longer required. Federal agencies will instead fully describe in the footnotes to their financial statements the accounting standards in the above hierarchy followed in preparing the statements.

Approved



Lloyd E. Bentsen
Secretary of the Treasury

3/24/93
Date

Approval requests of Leon E. Panetta, Director, Office of Management and Budget; and Charles A. Bowsher, Comptroller General of the United States; forwarded under separate cover.

Federal Accounting Standards Advisory Board

750 First Street, NE, Room 1001
Washington, D.C. 20002
(202) 512-7350
FAX: 512-7366

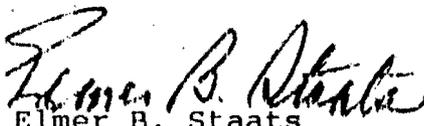
March 10, 1993

To: Secretary of the Treasury
Director, Office of Management and Budget
Comptroller General of the United States

In one of its first actions the Federal Accounting Standards Advisory Board recommended guidance for interim standards to apply until standards were recommended by the Board and adopted by the Board's principals - the Secretary of the Treasury, Director of the Office of Management and Budget and the Comptroller General.

The interim guidance provided that agencies were to continue the use of accounting standards that were formally adopted within their policy directives. Agencies were to indicate in notes to their financial statements where the standards used departed from standards issued by the Comptroller General in Title 2 of GAO's Policy and Procedures Manual for the Guidance of Federal Agencies. The guidance now needs revision to take into account standards to be issued as a result of recommendations of this Board along with other guidance such as financial statement form and content requirements issued by the Office of Management and Budget.

A recommendation for revised guidance is attached for your approval. This guidance has been developed in consultation with the American Institute of Certified Public Accountants. It establishes an order of precedence for applying accounting standards issued within the federal government and by other authoritative standard setting bodies.


Elmer B. Staats
Chairman

TREASURY CLEARANCE SHEET

NO. 93-118986
Date 3/16/93

- MEMORANDUM FOR: SECRETARY DEPUTY SECRETARY EXECUTIVE SECRETARY
 ACTION BRIEFING INFORMATION LEGISLATION
 PRESS RELEASE PUBLICATION REGULATION SPEECH
 TESTIMONY OTHER _____

FROM: Gerald Murphy
 THROUGH: _____
 SUBJECT: Request to Approve Fed. Accounting Standards Advisory Board

REVIEW OFFICES (Check when office clears) (FASAD) Interim Accounting Standards Guidance

- | | | |
|--|--|---|
| <input type="checkbox"/> Under Secretary for Finance | <input type="checkbox"/> Enforcement | <input type="checkbox"/> Policy Management |
| <input type="checkbox"/> Domestic Finance | <input type="checkbox"/> ATF | <input type="checkbox"/> Scheduling |
| <input type="checkbox"/> Economic Policy | <input type="checkbox"/> Customs | <input type="checkbox"/> Public Affairs/Liaison |
| <input checked="" type="checkbox"/> Fiscal | <input type="checkbox"/> FLETC | <input type="checkbox"/> Tax Policy |
| <input type="checkbox"/> FMS | <input type="checkbox"/> Secret Service | <input type="checkbox"/> Treasurer |
| <input type="checkbox"/> Public Debt | <input type="checkbox"/> General Counsel | <input type="checkbox"/> E & P |
| <input type="checkbox"/> Under Secretary for International Affairs | <input type="checkbox"/> Inspector General | <input type="checkbox"/> Mint |
| <input type="checkbox"/> International Affairs | <input type="checkbox"/> IRS | <input type="checkbox"/> Savings Bonds |
| | <input type="checkbox"/> Legislative Affairs | <input type="checkbox"/> Other _____ |
| | <input type="checkbox"/> Management | |
| | <input type="checkbox"/> OCC | |

NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
INITIATORS				
G. Murphy	<i>Gm</i>	3/15	OFAS	2-0550
REVIEWERS				
John Bowman	<i>JB</i>	3/16	Asst. Gen. Counsel (Banking & Finance)	2-1964
Dennis Foreman	<i>DF</i>	3/16	Acting Gen. Counsel	2-0283
Frank Newman Exec. Sec.	<i>FM</i>	3-22	Under Secretary for Finance	2-2800

SPECIAL INSTRUCTIONS

Review Officer _____ Date 3/23/93 Executive Secretary _____ Date _____
Rom
 DO F 80-02.1 (04/89) **Roger D. Martin** **Edward S. Knight**



DEPARTMENT OF THE TREASURY
WASHINGTON

ASSISTANT SECRETARY

MEMORANDUM FOR SECRETARY RUBIN

THROUGH: Frank N. Newman *FNA*
Deputy Secretary

FROM: Gerald Murphy *GM*
Fiscal Assistant Secretary

SUBJECT: Request to Approve Federal Accounting Standards Advisory Board (FASAB) Statement of Recommended Managerial Cost Accounting Concepts and Standards

regular basis
budgets should
full costs
Inter entity
cost of inputs from other entities must be accounted for. Res. for production
ACTION

ACTION FORCING EVENT:

Elmer B. Staats, Chairman, FASAB has transmitted the Board's completed action on its recommended "Statement of Recommended Managerial Cost Accounting Concepts and Standards" and requests your approval as one of the three principals for FASAB. Requests for similar approval have been transmitted separately to the Director, Office of Management and Budget and the Comptroller General of the United States.

RECOMMENDATION:

That you sign the attached FASAB approval sheet for the "Statement of Recommended Managerial Cost Accounting Concepts and Standards."

Agree Disagree Let's Discuss

BACKGROUND/ANALYSIS:

This recommendation represents a significant effort in reaching FASAB consensus on providing reliable and timely information on the full cost of federal programs, their activities and outputs. Managerial cost accounting is especially important for fulfilling the objective of assessing operating performance. Based on sound cost accounting concepts, these standards are broad enough to allow maximum flexibility for managers to develop costing methods to improve operating economy and efficiency. This cost information can also be used by federal executives and the Congress in making decisions about authorizing, evaluating, and modifying programs and allocating resources. The CFO Act of 1990, the Government Performance and Results Act passed by Congress in July 1993, and the National Performance Review all emphasize the need for and use of a set of cost accounting standards for all federal activities.

ATTACHMENTS: FASAB Recommendation Approval Sheet for Signature and Accompanying Transmittal Sheet from Elmer B. Staats, Chairman

Tab A: Statement of Recommended Managerial Cost Accounting Concepts and Standards

The Deputy Secretary of the Treasury

Dow -

~~John Poller~~
~~James Barr~~
~~Spitzer~~

this looks
improper - I initialed.

Ane Bowler +
Kivlin staffs request
to recommend signatures,
also? ? Yes 7/12/95
Pharis.

Room 3326

F -

622-2800

**STATEMENT OF RECOMMENDED ACCOUNTING CONCEPTS AND STANDARDS
MANAGERIAL COST ACCOUNTING CONCEPTS AND STANDARDS
FOR THE FEDERAL GOVERNMENT**

APPROVED:

Robert E. Rubin

Robert E. Rubin
Secretary of the Treasury

Date

Signature pages for approval by Charles A. Bowsher, The Comptroller of the United States, and Alice M. Rivlin, Director, Office of Management and Budget, are forwarded under separate covers.

Federal Accounting Standards Advisory Board

750 First Street, NE, Room 1001
Washington, D.C. 20002
(202) 512-7350
FAX: 512-7366

May 31, 1995

To: Secretary of the Treasury
Director, Office of Management and Budget
Comptroller General of the United States

Enclosed is the Statement of Recommended Managerial Cost Accounting Concepts and Standards for the Federal Government, prepared and submitted for your approval by the Federal Accounting Standards Advisory Board.

In developing the recommended concepts and standards, the Board convened an advisory group with members from federal agencies, consulting firms, and the academe. After considering their proposals, the Board issued an Exposure Draft for public comment. We conducted public hearings on this subject. Comments from all respondents were carefully reviewed and considered by the Board. The Board recommends that you adopt the concepts and standards contained in the enclosed statement.

The second page of the transmittal letter provides a signature block for you to indicate your approval of the statement.


Elmer B. Staats
Chairman

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TREASURY CLEARANCE SHEET

NO. 95-147381
Date 6/23/95

MEMORANDUM FOR: SECRETARY DEPUTY SECRETARY EXECUTIVE SECRETARY
 ACTION BRIEFING INFORMATION LEGISLATION
 PRESS RELEASE PUBLICATION REGULATION SPEECH
 TESTIMONY OTHER _____

FROM: Gerald Murphy, FAS

THROUGH: Deputy Secretary Newman

SUBJECT: Request to Approve FASAB Statement of Recommended

REVIEW OFFICES (Check when office ^{Managerial Cost Accounting Concepts and Standards} clears)

- | | | |
|---|--|--|
| <input type="checkbox"/> Under Secretary for Finance
<input type="checkbox"/> Domestic Finance
<input type="checkbox"/> Economic Policy
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<input type="checkbox"/> Public Debt

<input type="checkbox"/> Under Secretary for International Affairs
<input type="checkbox"/> International Affairs | <input type="checkbox"/> Enforcement
<input type="checkbox"/> ATF
<input type="checkbox"/> Customs
<input type="checkbox"/> FLETC
<input type="checkbox"/> Secret Service
<input type="checkbox"/> General Counsel
<input type="checkbox"/> Inspector General
<input type="checkbox"/> IRS
<input type="checkbox"/> Legislative Affairs
<input type="checkbox"/> Management
<input type="checkbox"/> OCC | <input type="checkbox"/> Policy Management
<input type="checkbox"/> Scheduling
<input type="checkbox"/> Public Affairs/Liaison
<input type="checkbox"/> Tax Policy
<input type="checkbox"/> Treasurer
<input type="checkbox"/> E & P
<input type="checkbox"/> Mint
<input type="checkbox"/> Savings Bonds

<input type="checkbox"/> Other _____ |
|---|--|--|

NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
INITIATOR(S)				
Gary Spittle		6/15	OFAS	622-0570 - 1808
REVIEWERS				
Gerald Murphy	Gm	6/16	Fiscal Asst. Secretary	622-0550
John Bowman	JB	6/20	Asst. General Counsel	" -1964
Edward Knight	EN	6/21	General Counsel	" -0287
John Hawke	JH	6/21	Under Secretary for Domestic Finance	" -0386
Exec. Sec.				

SPECIAL INSTRUCTIONS

Please return to Rm. 2112 for mailing to FASAB.

Review Officer _____ Date _____ Executive Secretary _____ Date _____



DEPARTMENT OF THE TREASURY
WASHINGTON

95-146366

ASSISTANT SECRETARY

*Defines reporting entities
sets out criteria to include
as part of an entity
determines what should be in
an entity's financial statement*

ACTION

MEMORANDUM FOR SECRETARY RUBIN

THROUGH: Frank N. Newman
Deputy Secretary

FROM: Gerald Murphy *Gm*
Fiscal Assistant Secretary

SUBJECT: Request to Approve Federal Accounting Standards
Advisory Board (FASAB) Statement of Recommended
Accounting Concepts, Entity and Display

ACTION FORCING EVENT:

Elmer B. Staats, Chairman, FASAB has transmitted the Board's completed action on its recommended accounting concepts for "Entity and Display" and requests your approval as one of the three principals for FASAB. Requests for similar approval have been transmitted separately to the Director, Office of Management and Budget and the Comptroller General of the United States.

RECOMMENDATION:

That you sign the attached FASAB approval sheet for the Statement of Recommended Accounting Concepts, "Entity and Display."

Agree Disagree Let's Discuss

BACKGROUND/ANALYSIS:

This recommendation represents a significant effort in reaching FASAB consensus on definitions of reporting entities and the types of financial statements which meet the four objectives of Federal financial reporting. An explicit understanding of what a reporting entity entails will ensure that the users of the entity's financial reports are provided with all the information that is relevant to the reporting entity, subject to cost and time restraints. Also the uniqueness of the display of Federal financial information may include information from other than accounting records. It is for these reasons that the Board felt compelled to prepare this set of concepts.

ATTACHMENTS: FASAB Recommendation Approval Sheet for Signature and Accompanying Transmittal Sheet from Elmer B. Staats, Chairman
Tab A: Statement of Recommended Accounting Concepts, Entity and Display

EXECUTIVE SECRETARIAT

Federal Accounting Standards Advisory Board

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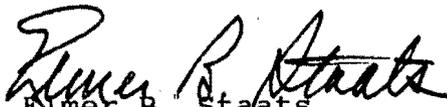
April 20, 1995

To: Secretary of the Treasury
Director, Office of Management and Budget
Comptroller General of the United States

Here for your approval is the Federal Accounting Standards
Advisory Board's Statement of Recommended Accounting Concepts,
Entity and Display.

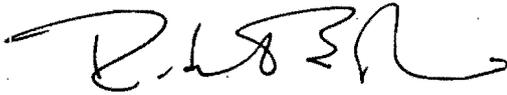
In developing the recommended concepts, the Board issued an
Exposure Draft to all federal agencies and to representatives of
the private sector and the academic community. We also conducted
a public hearing on this topic. Comments from all respondents were
carefully reviewed and considered by the Board. The Board
recommends that you adopt the concepts contained in the enclosed
statement.

The second page of the transmittal letter provides a signature
block for you to indicate your approval of the concepts statement.


Elmer B. Staats
Chairman

STATEMENT OF RECOMMENDED ACCOUNTING CONCEPTS
ENTITY AND DISPLAY

APPROVED:



Robert E. Rubin
Secretary of the Treasury

5/23/95

Date

Signature pages for approval by Charles Bowsher, The
Comptroller of the United States, and Alice M. Rivlin,
Director, Office of Management and Budget, are
forwarded under separate covers.

TAB A

Entity and Display

Statement of Recommended Accounting Concepts

Number 2

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INTRODUCTION

- 1 A basic postulate of accounting is that accounting information pertains to entities, i.e., circumscribed legal, administrative, fiduciary, or other organizational structures. Another basic postulate is that entities use financial reports to communicate financial and related information about the entity to persons concerned with the entity.
- 2 The purpose of this statement of accounting concepts is to provide guidance as to what would be encompassed by a Federal Government entity's financial report. The statement specifies the types of entities for which there ought to be financial reports (hereinafter called reporting entities), establishes guidelines for defining the makeup of each type of reporting entity, identifies types of financial reports for communicating the information for each type of reporting entity, and suggests the types of information each type of report would convey.
- 3 A statement of financial accounting concepts is intended to guide the members of the Federal Accounting Standards Advisory Board (FASAB) as they deliberate and recommend accounting standards for the Federal Government. It also would be useful to the Office of Management and Budget (OMB), when it carries out its statutory responsibilities for specifying who should prepare financial statements and the form and content of those statements;¹ and as broad guidance for preparers, auditors, and users of financial statements of Federal agencies. A statement of financial accounting concepts does not, in and of itself, represent standards that would be considered generally accepted accounting principles for Federal agencies to be followed for the preparation of financial statements.
- 4 This statement does not try to define which reporting entities must prepare and issue financial statements. That authority and responsibility resides with the Congress, OMB, and other oversight organizations and resource providers.
- 5 The specification of reporting entities intends to be suitable for all organizations within the Executive branch of the Federal Government,

¹OMB specifies the form and content of agency and governmentwide financial statements, pursuant to authority assigned in the Chief Financial Officers Act of 1990, as amended (title 31, U. S. Code, section 3515(d) and section 331(e)(1)) through periodic issuance of OMB Bulletins. OMB intends to base the form and content on the concepts contained in this statement.

adequate to ensure proper execution of transactions, safeguard assets, and support performance measurement.

- 7 The concepts are also intended, as FASAB's mission statement requires, to help in meeting the financial and budgetary information needs of executive agencies and Congressional oversight groups, and to strengthen the conceptual basis and consistency of Federal accounting data.
- 8 The entity and display concepts presented in this statement do not preclude the specification of ad hoc or temporary reporting entities to meet special reporting needs of users of Federal agencies' financial information. Nor do they preclude a reporting entity from preparing special purpose financial reports to meet the specific needs of persons in the reporting entity or in response to requests from persons outside the entity for certain financial information; or from preparing a so-called "popular report," which provides a simplified, highly readable, easily understandable description of a reporting entity's finances. These statements would not necessarily purport to be presented in accordance with generally accepted accounting principles.

REASONS FOR DEFINING REPORTING ENTITIES

- 9 The most basic reason for having an explicit understanding of what the reporting entity entails is to ensure that the users of the entity's financial reports are provided with all the information that is relevant to the reporting entity, subject to cost and time constraints. Clearly defining the boundaries of the reporting entity provides the users with a clear understanding of what the reporting entity encompasses. It helps to establish what information is relevant to the financial statements and what information is not.

hand, there are small agencies for which division into smaller units is generally not considered appropriate.

Budget Perspective

13. From another perspective, the government is composed of accounts presented in the budget, hereinafter referred to as **budget accounts**. Budget accounts are composed of expenditure (appropriations or fund) accounts and receipt (including offsetting receipt) accounts. The size and scope of these accounts varies according to Congressional preference. They can vary from very small accounts, which are useful for constraining management, to very large accounts, which can be used to finance many activities.
14. Budget accounts are not the same as Treasury accounts. The latter are accounts established in the Treasury to, among other purposes, record the appropriations and other budgetary resources provided by statutes and the transactions affecting those accounts. For the most part, budget accounts are aggregations of Treasury accounts. Also, Treasury accounts include deposit accounts as well as budget accounts.
15. Nor are budget accounts the same as the uniform ledger accounts established by the U. S. Government Standard General Ledger (SGL). SGL accounts record specific homogeneous types of transactions and balances that aggregate to specific classifications on the financial statements. They have been established so that agencies can establish control over their financial transactions and balances, meet the basic financial reporting requirements, and integrate budgetary and financial accounting in the same general ledger.
16. A budget account may coincide with an organization or one or more of its suborganizations. Other times, several budget accounts need to be aggregated to constitute an organization or sub-organization.
17. Budget accounts are classified as federal funds or trust funds. Any account that is designated by the laws governing the federal budget as being a trust fund is so classified. Federal funds comprise the larger group and include all transactions not classified by law as trust funds. Three components make up federal funds: the general fund, special funds, and revolving funds. The definition of each of these

Program Perspective

- 22 From a third perspective, the government is composed of **programs and activities**, i.e., the services the organizations provide and the specific lines of work they perform. Each program and activity is responsible for producing certain outputs in order to achieve desired outcomes.
- 23 There is no firm definition for the term "program;" it varies in the eye of the beholder. For example, the Highway program could relate to the entire Federal highway program, the program to build interstate highways (in contrast to city streets, secondary roads, etc.), or a program to build a highway between two specific points. Moreover, in accordance with the sequester provisions of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, the House and Senate Appropriations Subcommittees annually define, in the Committee Reports, the meaning of "Programs, Projects, and Activities" as they relate to each of the Appropriations Acts.
- 24 The term "program" is also often used interchangeably with the terms "function" and "sub-function" (see paragraph 21). Generally, however, the term "function" would be used only for the functions defined in the budget. Otherwise, the term "program" would be used.

Intertwining of the Perspectives

- 25 The programs are administered by the organizations and financed by the budget accounts. In a few instances, there is a one-to-one relationship among the three perspectives. A single budget account finances a single program and organization. Thus, the program is carried out only by the single organization and the organization performs only one program.
- 26 However, most programs are financed by more than one budget account, some of which might not be under the control of the organizational unit administering the program. Some programs are even administered by more than one organization. Likewise, a single organization or budget account could be responsible for several programs. In some instances, a program could also be considered an organizational unit, e.g., the Center for Disease Control and Prevention.

- 30 Budget accounts, in and of themselves, do not meet the criteria in the preceding paragraph and, therefore, would not be considered a reporting entity for the purposes of issuing general purpose financial statements. Also, the size and scope of the budget accounts across all government agencies lack sufficient consistency for them to be universally considered as the reporting entity. Similarly, programs generally do not meet the criteria in paragraph 29 and, therefore, would not be a considered a reporting entity that prepares general purpose financial statements.
- 31 On the other hand, organizations, and particularly larger organizations, meet the criteria in paragraph 29. While the occasional overlap of programs and budget accounts among more than one organizational unit could complicate financial reporting, the association of data with the responsibility centers, revenue centers, profit centers, cost centers, etc. which managers typically use for organizing and operating permit the following:
- aggregating information for not only the organization (and suborganizations), but also for one or more of the programs performed by the organization, and one or more of the budget accounts for which the organization is responsible, and
 - the subsequent arraying of the information not only by organization, but also by sub-organization, program, and/or budget accounts.
- 32 This approach to defining the appropriate reporting entities in the Federal Government supports establishment of accountability in the organizations (and suborganizations) while still enabling them to provide information pertaining to their programs.
- 33 Although a reporting entity might not control all the budget accounts used to finance one or more of the programs it administers, any revenues attributable to or costs incurred on behalf of the programs it administers should be associated with that reporting entity. This notion holds true regardless of whether the reporting entity maintains personnel on a payroll.
- 34 ~~The departments and major independent agencies are organizational units and therefore would be the primary reporting entities. However, in many instances, financial statements that present aggregations of~~

internal management purposes, or, perhaps to be more relevant and meaningful, combined with financial statements from other organizationally-based reporting entities.

- 38 The ultimate aggregation of entities is into the entire Federal Government which, in reality, is the only independent economic entity--although some would say the entire country is the ultimate economic entity. The Federal Government entity would encompass all of the resources and responsibilities existing within the component entities, whether they are part of the Executive, Legislative, or Judicial branches (although, as noted in paragraph 5, FASAB's recommendations pertain only to the Executive Branch). The aggregation would include organizations for which the Federal Government is financially accountable as well as other organizations for which the nature and significance of their relationship with the government (see paragraphs 39 through 50) are such that their exclusion would cause the Federal Government's financial statements to be misleading or incomplete.

CRITERIA FOR INCLUDING COMPONENTS IN A REPORTING ENTITY

- 39 Regardless of whether a reporting entity is the U. S. Federal Government, or an organization, suborganization, or program, there can be uncertainty as to what should be included and inconsistency as to what is included in the reporting entity. The identification and application of specified criteria can reduce this uncertainty and inconsistency.
- 40 The Governmental Accounting Standards Board (GASB) has established criteria for what would be included in a state or local government reporting entity. These criteria relate to financial accountability, which includes appointment of a voting majority of the organization's governing board, together with imposition of will, and financial benefit to or burden on a primary government. These criteria, while in part relevant, must be tailored to the Federal Government environment. First, there are not as many different types of entities in the Federal Government as there are in state and local governments. Second, the Congress and others with oversight authority frequently establish explicit rules for what to include as part of a Federal reporting entity. Finally, as indicated, with the exception of the Federal

assigned to the indicative criteria. Thus, while the indicative criteria are presented in descending order of importance, judgment must be based on a consideration of all of the indicative criteria.

44. The indicative criteria for determining whether an organization not listed in the "Federal Programs by Agency and Account" section of the budget is nevertheless part of a financial reporting entity are as follows:
- It exercises any sovereign power of the government to carry out Federal functions. Evidence of sovereign powers are the power to collect compulsory payments, e.g., taxes, fines, or other compulsory assessments; use police powers; conduct negotiations involving the interests of the United States with other nations; or borrow funds for Government use.
 - It is owned by the Federal Government, particularly if the ownership is of the organization and not just the property. Ownership is also established by considering who is at risk if the organization fails, or identifying for whom the organization's employees work.
 - It is subject to the direct or continuing administrative control of the reporting entity, as revealed by such features as (1) the ability to select or remove the governing authority or the ability to designate management, particularly if there is to be a significant continuing relationship with the governing authority or management with respect to carrying out important public functions (in contrast to selections and designations in which there is little continuing communication with, or accountability to, the appointing official); (2) authority to review and modify or approve budget requests, budgetary adjustments, or amendments or rate or fee changes; (3) ability to veto, overrule, or modify governing body decisions or otherwise significantly influence normal operations; (4) authority to sign contracts as the contracting authority; (5) approval of hiring, reassignment, and removal of key personnel; (6) title to, ability to transfer title to, and/or exercise control over facilities and property; and (7) right to require audits that do more than just support the granting of contracts. (While many of these criteria exist in a client-contractor relationship, it is not necessarily intended that an entity's contractor be considered as part of the reporting entity.)

would not be considered part of the government-wide reporting entity. Payments made to or collections received from the Federal Reserve System would be reported in the financial statements of the Federal Government. Certain other disclosures might also be appropriate in the financial statement for the entire government.

Government Sponsored Enterprises

- 48 There are also several Federally chartered but privately owned and operated financial institutions that have been established as financial intermediaries to facilitate the flow of investment funds to specific segments of the private sector. These entities are called government sponsored enterprises (GSE). Examples are the Federal National Mortgage Association, the Farm Credit Banks, and the Federal Home Loan Banks. By law, each of these GSEs is subject to oversight from a specific Federal agency. However, they are not included in the Federal budget section entitled "Federal Programs by Agency and Account." Nor, as currently constituted, do they function in a manner consistent with the indicative criteria presented in paragraph 44. Thus they would not be considered part of the government-wide reporting entity nor the reporting entity to which they have been assigned for oversight.
- 49 On the other hand, there are "political expectations" associated with the GSEs, the most significant of which is an expectation that legislation would be enacted to support a GSE experiencing severe financial difficulties. (Political expectations are different than "moral obligations" established by many states. There is no statutory authority that defines whether and how a political expectation would be met. With a moral obligation, the manner in which it may be met is usually explicitly defined in statute.) Therefore, agencies assigned oversight responsibility for a GSE(s) would need to consider making disclosures of the government's relationship with the GSE(s) and other information that would provide an understanding of the possibility of a contingent liability.⁵

⁵The term government sponsored enterprise is also sometimes used in a broader manner to encompass other entities established by the Federal Government to further a public policy and that are also not included in the budget section "Federal Programs by Agency and Account." Examples are the Financing Corporation, Resolution Funding Corporation, Amtrak, and even, on occasion, the American National Red Cross. These entities have varied characteristics and

(continued...)

provided by other reporting entities, such as computer services provided by another unit.

- 52 A process in which the reporting entity is billed and pays for the amounts attributable to its activities is normally the most desirable approach for recording and reporting these amounts. However, when this type of direct debiting or crediting is not done, the decision as to whether to capture and report attributable amounts would be based on such criteria as the magnitude of the attributable amounts, the decision usefulness of the information to its likely users, the costs of capturing the data, whether a decision would be made differently as a result of having the information, and whether the information would have a policy impact.⁶
- 53 It might be appropriate to consider the interest expense inherent in devoting a sum of capital to an organization or program as part of the total costs incurred in operating the organization or performing the program. This principle has already been adopted for the accounting for loans and loan guarantees, whereby a loan program is charged for the cost of capital provided by the U. S. Treasury.⁷

DISPLAYING FINANCIAL INFORMATION

- 54 Financial information is typically provided by or for a reporting entity through financial statements. Financial statements represent the principal means of communicating accounting information about an entity's resources, obligations, revenues, costs, etc. to those outside the entity. However, financial statements, and particularly those prepared for governmental and other not-for-profit organizations, may also contain information from sources other than accounting records. Also, management may communicate information to those outside the entity by means of financial reporting other than financial statements, either because the information is required to be disclosed by statute,

⁶The Board is developing a Statement of Managerial Cost Accounting Concepts and Standards. This document, when finalized, will address recognition of these amounts.

⁷The Board has decided to undertake a project addressing the types of capital for which it might be appropriate for a reporting entity to disclose the costs, the reasons thereof, and the manner in which to determine and report these costs. A determination of the appropriateness of considering interest expense as part of the costs incurred by an organization or program will be made by that project.

Flow Statements

- 58 Another type of financial statement provides information on an entity's flows of revenues, receipts, expenditures, expenses, gains, losses, and/or other changes of the entity's net resources during a period, however they are measured, i.e., budgetary, cash, or accrual. This type of financial statement is frequently characterized as a flow statement. The traditional flow statement is a statement of operations and changes in net position issued by private sector, profit seeking organizations. It presents the results of an entity's operations for a reporting period, including the changes in the entity's net position from the end of the prior reporting period. This type of statement is particularly useful for private sector, profit seeking organizations since their objective is to generate earnings and returns on investment. The statement of operations and changes in net position presents the revenues the entity receives, the expenses incurred to generate the revenues, the amount left for the entity's owners, and the resulting effect on the owners' equity.
- 59 The Federal Government and most of the other reporting entities in the Federal Government are spending entities whose objective is to provide services, some of which are financed by revenues received from the recipients of the service, and some of which, if not all or most of which, are financed by taxes and other unearned revenues.⁸ Thus, the most useful information a flow statement could present is the total and net costs of the services, i.e., how much of the services provided by the entity was financed by the taxpayers. This type of statement, which would be a **statement of net costs**, would support the achievement of Federal financial reporting objective 2A. Objective 2A states that "Federal financial reporting should provide information that helps the reader to determine the costs of providing specific programs and activities and the composition of, and changes, in these costs."
- 60 As indicated, revenues provided in exchange for the services, i.e., earned revenues, are not the only manner in which a Federal Government entity finances the services it provides. Other sources of financing are the appropriations received from the Congress, and

⁸The Board is currently developing an Exposure Draft entitled "Revenue and Other Financing Sources" which addresses more fully the types of revenues (i.e., exchange versus non-exchange and earned versus unearned revenues) discussed here.

- other legal requirements pertaining to the account have been met, and
 - the amounts are properly classified and accurately reported.
- 64 This information is provided in other reports, but there needs to be auditor involvement to provide assurance as to the reliability of the information. The assurance as to reliability of the information could be accomplished by including a **statement of budgetary resources** in the reporting entity's financial statements, recognizing that the statement will likely be subject to audit. The presentation of data could be for the reporting entity as a whole, for the major suborganization units (assuming there is congruity among the major suborganization units and the budget accounts), or for the aggregations of the major budget accounts, rather than for the individual budget accounts of the entity or other types of entities. Violations of budgetary integrity at the account level occurring during the current year could be disclosed on an exception basis. (Many violations of budgetary integrity would also be violations of the Anti-Deficiency Act. Disclosure in the financial statements notwithstanding, these violations would also have to be reported as required by the Act.)

Performance Measures Statement

- 65 The second objective of Federal financial reporting states, in part, that Federal financial reporting should provide information that helps readers of the financial reports determine the efforts and accomplishments associated with Federal programs and the changes over time and in relation to costs. This suggests that a **statement of program performance measures**,⁹ i.e., one or more statements presenting service efforts and accomplishments measures for each of a reporting entity's significant programs, is necessary.
- 66 The Federal Government is increasing its interest in measuring and reporting program performance, as evidenced by the enactment of the Government Performance and Results Act and increasing

⁹The Board does not consider the Statement of Program Performance Measures to be a basic financial statement.

information the agency head or CFO considers necessary to fully and fairly provide an understanding of the entity's financial affairs. This type of information is typically presented in what has come to be known as a **management discussion and analysis** or **overview** of the reporting entity.

- 70 The third objective of Federal financial reporting is that it "should assist report users in assessing the impact on the country of the government's operations and investments for the period and how, as a result, the government's and the nation's financial conditions have changed and may change in the future."¹⁰ This objective requires a reporting of information concerning investments in education, training, research, and development and certain types of property, plant, and equipment that can affect the nation's future wealth, and to the claims on future budgetary resources resulting from prior decisions and actions.
- 71 The information pertaining to the aforementioned investments, certain types of property, plant, and equipment,¹¹ and claims on future budgetary resources is maintained in part in the entities' general ledgers and, in part, external to the general ledgers. Some of the information is recorded in units other than dollars, e.g., acres, millions of square feet. Finally, some of the information is not subject to the types of controls present in a system of double entry recordkeeping. Accordingly, a more suitable way to fulfill the third reporting objective would be to display the appropriate information as **required supplemental information** rather than attempting to include it in financial statements.¹²

¹⁰A complete discussion of the third objective for Federal financial reporting, which is called the "stewardship objective," is contained on pages 41-45 in Statement of Federal Financial Accounting Concepts No. 1, "Objectives of Federal Financial Reporting."

¹¹The Board is currently considering accounting standards for Federally-owned property, plant, and equipment. These standards will address placement of information related to various types of PP&E. The Board is considering placing information about some types of PP&E in footnotes with information about other types in required supplemental information. The Board's proposals will be presented in an exposure draft on stewardship reporting.

¹²Required supplemental information is information that would be reported outside the principal financial statements that the Federal Accounting Standards Advisory Board considers an essential part of a reporting entity's financial reporting, and therefore recommends authoritative guidelines for the measurement and presentation of the information. It is analogous to the required supplementary information discussed in Statement on Auditing Standards-AU

(continued...)

- statement of net costs;
- statement of changes in net position;
- statement of custodial activities, when appropriate;
- statement of budgetary resources;
- statement of program performance measures;¹³
- accompanying footnotes;
- required supplemental information pertaining to physical, human, and research and development capital and selected claims on future resources, when appropriate; and
- other supplemental financial and management information, when appropriate.

75 With some organizations, and even suborganizations, the activities of one or more programs or other components are as important to the readers of the financial statements as are the activities of the entity as a whole. This would be particularly true for a Department composed of many bureaus, administrations, agencies, services, etc., and particularly if their programs are dissimilar. In those instances, consideration should be given to the preferability of reporting the assets, liabilities, revenues, expenses, etc. of both the significant components individually and of the entity in its entirety. Hence, larger organizations, and particularly those composed of many bureaus, administrations, agencies, etc., would prepare not only consolidated financial statements for the organizational entity, but also provide information pertaining to their individual significant components.¹⁴ The information for the individual components could be provided with

¹³The statement of program performance measures is not a basic financial statement. Nevertheless, it is an important component of the financial reports.

¹⁴Such components are similar to responsibility segments as referred to in FASAB Exposure Draft, "Managerial Cost Accounting for the Federal Government" (see pages 26-30). Responsibility segments are used to accumulate costs and outputs for major lines of activity.

information for the entity in its entirety if the intra-entity balances are not eliminated, the misunderstanding that might result if the balances are not eliminated, and the cost-benefit of making the eliminations.¹⁷

- 78 Some of a reporting entity's components are likely to be required by law or policy to prepare and issue financial statements in accordance with accounting standards other than those recommended by FASAB and issued by OMB and GAO, e.g., accounting standards issued by the Financial Accounting Standards Board or accounting standards established by a regulatory agency. Those components should continue to issue the required reports. The reporting entities of which the components are a part can issue consolidated, consolidating, or combining statements that include the components' financial information prepared in accordance with the other accounting standards. They need to be sensitive, however, to differences resulting from applying different accounting standards that could be material to the users of the reporting entity's financial statements. If these differences are material, the standards recommended by FASAB and issued by OMB and GAO should be applied. The components would need to provide any additional disclosures recommended by FASAB and included in the OMB-issued standards that would not be required by the other standards.

Financial Reporting for the Entire Government

- 79 Readers of the financial statements for the entire government are likely to be concerned primarily with whether the government has been a proper steward. This can best be achieved with the preparation and issuance of the following:

- management discussion and analysis;

¹⁷A reporting entity that eliminates none of the intra-entity transactions or balances and still desires to present the information for its individual components in separate columns could do so by preparing and issuing a **combining financial statement**. If the individual columns are added to a total column without elimination of the intra-entity transactions or balances, the total column would have to be labeled "Memorandum Only" to signify that it is not net of eliminations.

Recognizing that the U. S. Standard General Ledger does not presently provide accounts for identifying intra-entity transactions, the decision as to when the information for a reporting entity other than the Federal Government as a whole should be presented in a consolidating financial statement rather than a combining financial statement would be specified by OMB in a Form and Content Bulletin.

consolidated financial statement, in accompanying footnotes, and/or as supplemental information.

RECOMMENDED CONTENTS FOR THE RECOMMENDED DISPLAYS

Balance Sheet

- 84 The elements most likely to be presented in the balance sheet of a Federal suborganization/organization, program, or the entire government would be as follows:
- **Fund Balance with Treasury.** This represents the amount in the entity's accounts with the Treasury that is available only for the purposes for which the funds were appropriated. It would also include balances held by the entity in the capacity of a banker or agent for others. (This classification would not be included in the financial statements of the U. S. Government.)
 - **Cash and other monetary assets.** Cash consists of coins, paper currency and readily negotiable instruments, such as money orders, checks, and bank drafts on hand or in transit for deposit, amounts on demand deposit with banks or other financial institutions, cash held in imprest funds, and foreign currencies.
 - **Investments.** While Federal agencies have the authority to invest, they are typically limited to investing in securities issued by the Department of the Treasury or other Federal entities. There could be instances, however, when an agency owns property or securities issued by state or local governments, private corporations, or government sponsored enterprises, primarily for the purpose of obtaining a monetary return.
 - **Receivables.** These are the amounts that the entity claims for payment from others. Receivables can result from such activities as the sales of goods or services, the non-payment of taxes, the making of loans or loans assumed from defaults on previously made loan guarantees, the earning of interest, the advance or prepayment of monies, etc.

expended, including undelivered orders. Included in the latter would be the amounts accumulated over the years by the entity from its financing sources less its expenses and losses, which would include donated capital and transfers in the net investment of the Government in the reporting entity's assets; and an amount representing the entity's liabilities for such things as accrued leave, credit reform subsidies, and actuarial liabilities not covered by available budgetary resources.

- 85 Assets the reporting entity holds and has the authority to use in its operations should be displayed separately from assets the entity holds but does not have the authority to use. Likewise, liabilities for which budgetary authority has been received for liquidating the liabilities should be displayed separately from liabilities for which budget authority has not been received (even if the authority is expected). Assets and liabilities arising from transactions among Federal entities should be displayed separately from assets and liabilities arising from transactions with non-Federal entities.

Statement of Net Costs

- 86 The main purpose of a statement of net costs is to provide an understanding of the net costs of each organization and each program that the government supports with taxes and other unearned monies. Another important purpose for the statement is to provide gross and net cost information that can be related to the amounts of outputs and outcomes for the programs and/or organization. Thus the statement of net costs should present the amounts paid, the consumption of other assets, and the incurrence of liabilities as a result of rendering services, delivering or producing goods, or carrying out other operating activities.
- 87 The costs can be classified in a reporting entity's statement of net costs by sub-organization (assuming the reporting entity is an organization), by program, or by object class, or any combination thereof. Object class, also referred to as a "natural" classification, represents the nature or types of goods or services acquired without regard to the organization involved or the program for which they were used. Reporting of the sub-organization incurring the costs and/or the purposes for which the costs were incurred generally

- 92 Earned revenues that are insignificant in amount can be netted into the costs of the programs with the amounts disclosed in accompanying footnotes, if appropriate.
- 93 An organization or sub-organization could receive different types of revenues for different purposes and/or reasons. Each of the revenues and associated costs would be displayed in accordance with the concepts presented in paragraphs 89 through 92.
- 94 The costs associated with and displayed for each program should reflect costs that can be directly traced to the program, assigned to the program based on cause and effect, or allocated to the program on a reasonable and consistent basis, consistent with the premise that any costs reported for a program should be controllable by the program to at least some degree. Those costs that are not directly traceable, assignable, or allocable could be considered program or management support costs that are incurred by the reporting organization or another organization to administer the reporting organization's or program's activities. For example, in a reporting entity that provides social services, the program costs would be the cash payments and the salary and other costs, e.g., rent, supplies, directly associated with persons providing counseling to the recipients of the cash payments. The organizational support costs would be the costs of the organizational structure required to administer the organization, i.e., not directly attributable to the programs provided by the organization.
- 95 Organizational and program management costs are necessary costs of operating an organization and programs. Not displaying these costs because of a belief that an allocation for these activities would be eliminated or reduced in order to obtain a reduction of the cost of the entire organization or program is illogical. The alternative concept, which is burying the management costs with the program costs, increases the likelihood that the management activity will be subject to reductions imposed on the program delivery activities. Separately identifying the management costs enables the use of resources for these activities to be justified on their own merit. The costs for managing the organization and/or program can therefore be displayed on the face of the financial statements or in accompanying footnotes, particularly when it would assist in evaluating operating performance and is cost-effective. Disclosure of what the support costs entail would be appropriate.

- **Transfers in** are amounts of cash or other capitalized assets received by one Government entity from another Government entity without reimbursement.
- **Transfers out** are amounts of cash or other capitalized assets provided by one Government entity to another without reimbursement.
- **Imputed financing sources** are of two types: amounts equal to the costs that have been incurred by the reporting entity but financed by another entity, e.g., retirement costs; and amounts representing costs that are attributable to the reporting entity's activities but that do not require a direct out-of-pocket payment, e.g., the interest costs associated with carrying inventory or investing in physical assets.¹⁹
- **Prior period adjustments** are corrections of prior period results of operations.
- **Increase (decrease) in unexpended appropriations** is the change in appropriated capital, including transferred budgetary resources, that does not affect the net cost of operations but does affect net position.
- **Net position-beginning of the period** is the total unexpended appropriations and cumulative results of operations held by the entity at the beginning of the reporting period.
- **Net position-end of the period** results from adding and netting the various amounts associated with the operations of the entity during the reporting period, including the net position-beginning of the period and any prior period adjustments. The amount will thus equal the total unexpended appropriations and cumulative results of operations held by the entity at the end of the period.

Statement of Custodial Activities

¹⁹The Board plans to undertake a project on the interest cost associated with investing in operating assets. At this time, no decision has been made on the recognition by individual entities of these types of costs.

offsetting collections credited to an appropriation or fund account) and adjustments (e.g., recoveries of prior year obligations).

- **Status of Budgetary Resources** displays the disposition of the budgetary resources made available. It consists of the obligations incurred; the unobligated balances of multi-year and no-year budget authority that are available; and the unobligated balances of one-year and multi-year lapsed budget authority that are not available, but have been carried forward to be used only to record, adjust, or liquidate obligations chargeable to the appropriation. The total amount displayed for status should be equal to the total amount displayed as being made available.
- **Outlays** are payments to liquidate obligations, net of offsetting collections. Obligations are usually liquidated by means of cash payments (currency, checks, or electronic funds transfers), but in certain cases obligations are liquidated and outlays recorded even though no cash is disbursed. It would be appropriate, in displaying outlay information, to tie it to the obligations incurred by also displaying the transfers of obligations and the obligated balances at the beginning and end of the period.

- 105 Budgetary resources, obligations, outlays, and receipts are reported in the Treasury's Annual Report and Monthly Treasury Statement and in the President's Budget, although not all these publications report all these measures. These documents are usually issued prior to the issuance of financial statements prepared in accordance with generally accepted accounting principles applicable to the Federal Government. In preparing these statements, significant differences should be noted between amounts reported in the former documents and amounts reported in the subsequently prepared financial statements. Such differences should be adjusted in the records of the reporting entity and in the related records maintained by the central agencies, and the correct amounts reported in the financial statements. It would also be desirable to provide a reconciliation for significant differences appearing in the two types of statements.

Statement of Program Performance Measures

- 106 The statement of program performance measures should include measures for each of the major programs the reporting entity

109 Other characteristics to consider for reporting program performance measures are as follows :

- **Completeness.** The measures, in the aggregate, should cover all aspects of the reporting entity's mission.
- **Legitimacy.** The measures should be accepted as relevant both inside the reporting entity and by the external stakeholders and others, e.g., the central management agencies, Congress, interest groups, the public.
- **Understandability.** The measures should communicate the performance of the entity in a readily understandable manner to any reasonably informed and interested party.
- **Comparability.** The measures should provide a frame of reference for assessing, and comparing, if appropriate, the performance of the entity and entities with similar programs for both the immediate period and over time.
- **Ability to relate to cost.** The measures should be such that a cost can be defined for each unit of output, outcome, input, etc.
- **Timeliness.** The measures should be available to users of the financial statements before they lose their capacity to be of value in assessing accountability and making decisions. The value of timeliness should not preclude the use of important measures for which results are not immediately available.
- **Consistency.** The measures should be reported consistently from period to period to allow users to have a basis for comparison and to gain an understanding of the measures being used and their meaning (recognizing that the measures should be reviewed regularly and modifications made to reflect changing circumstances).

EXAMPLE FINANCIAL STATEMENT FORMATS

BALANCE SHEET
as of September 30, 19X4

ASSETS

	Suborgani- zation A	Suborgani- zation B	Suborgani- zation C	Total FY 19X4	Total FY 19X3
Entity assets:					
Fund balance with Treasury	\$xxx	\$xxx	\$xxx	\$xxx	\$xxx
Cash (and other monetary assets)	xxx	xxx	xxx	xxx	xxx
Investments:					
Intragovernmental	xxx	---	xxx	xxx	xxx
With the public	xxx	xxx	xxx	xxx	xxx
Receivables:					
Intragovernmental	xxx	xxx	xxx	xxx	xxx
With the public	xxx	---	xxx	xxx	xxx
Inventories and related properties	xxx	xxx	xxx	xxx	xxx
Physical assets	xxx	xxx	xxx	xxx	xxx
Total entity assets	xxx	xxx	xxx	xxx	xxx
Non-entity assets:					
Fund balance with Treasury	xxx	xxx	xxx	xxx	xxx
Cash	xxx	xxx	xxx	xxx	xxx
Receivables:					
Intragovernmental	xxx	xxx	xxx	xxx	xxx
With the public	xxx	xxx	xxx	xxx	xxx
Total non-entity assets	xxx	xxx	xxx	xxx	xxx
Total assets	\$xxx	\$xxx	\$xxx	\$xxx	\$xxx

EXAMPLE FINANCIAL STATEMENT FORMATS

STATEMENT OF NET COSTS
For the year ended September 30, 19X4

	Sub- organi- zation A	Sub- organi- zation B	Sub- organi- zation C	Total FY 19X4	Total FY 19X3
COSTS:					
Program A:					
Intragovernmental	\$xxx	\$---	\$---	\$xxx	\$xxx
With the public	xxx	---	---	---	---
Total	xxx	---	---	---	---
Less earned revenues	xxx	---	---	xxx	---
Net program costs	xxx	---	---	xxx	xxx
Program B:					
With the public	---	xxx	xxx	xxx	xxx
Less earned revenues	---	xxx	xxx	xxx	xxx
Net program costs	---	xxx	xxx	xxx	xxx
Program C:					
Intragovernmental	xxx	xxx	---	xxx	xxx
With the public	xxx	xxx	---	xxx	xxx
Net program costs	xxx	xxx	---	xxx	xxx
Program D:					
Costs with the public	---	xxx	---	xxx	xxx
Cost not allocated to programs	xxx	xxx	xxx	xxx	xxx
Less other earned revenues	---	---	xxx	xxx	xxx
NET COST OF OPERATIONS	\$xxx	\$xxx	\$xxx	\$xxx	\$xxx

EXAMPLE FINANCIAL STATEMENT FORMATS

STATEMENT OF CUSTODIAL ACTIVITIES
For the year ended September 30, 19X4

	FY 19X4	FY 19X3
Collections:		
Income taxes	\$xxx	\$xxx
Estate and gift taxes	xxx	xxx
Excise taxes	xxx	xxx
Employment taxes	xxx	xxx
Penalties and interest	xxx	xxx
Total collections	xxx	xxx
Refunds and other payments	(xxx)	(xxx)
Net collections	xxx	xxx
Accrual adjustment	xxx	(xxx)
Total revenues collected	xxx	xxx
Disposition of revenues collected:		
Transferred to others:		
Department of the Treasury	xxx	xxx
Department of Labor	xxx	xxx
Environmental Protection Agency	xxx	xxx
Total transfers	xxx	xxx
Retained by the entity	xxx	xxx
Increase (decrease) in amounts to be transferred	xxx	(xxx)
Total disposition of revenues collected	xxx	xxx
Net custodial collections	\$000	\$000

EXAMPLE FINANCIAL STATEMENTS FORMATS

STATEMENT OF PROGRAM PERFORMANCE MEASURES²²

For the year ended September 30, 19X4

	FY 19X4	FY 19X3	FY 19X2
Sub-organization A			
Program			
Performance Measure	xxx	xxx	xxx
Performance Measure	xxx	xxx	xxx
Program			
Performance Measure	xx%	xx%	xx%
Performance Measure	xxx	xxx	xxx
Program			
Performance Measure	xxx	xxx	xxx
Performance Measure	xx%	xx%	xx%
Sub-organization B			
Program			
Performance Measure	xxx	xxx	xxx
Performance Measure	xx%	xx%	xx%
Performance Measure	xxx	xxx	xxx
Program			
Performance Measure	xx%	xx%	xx%
Performance Measure	xxx	xxx	xxx
Program			
Performance Measure	xxx	xxx	xxx
Performance Measure	xx%	xx%	xx%

²² Although this example contains only numerical measures, the performance for some programs might be reported with other than numerical measures.

LIST OF ACRONYMS

FASAB Federal Accounting Standards Advisory Board
OMB Office of Management and Budget
SGL Standard General Ledger
SFFAC Statement of Federal Financial Accounting Concepts

FASAB Board Members

Elmer B. Staats, Chairman

James L. Blum

Donald H. Chapin

Martin Ives

Norwood Jackson

Gerald Murphy

James E. Reid

Cornelius E. Tierney

Alvin Tucker

Ronald S. Young, Executive Director

Federal Accounting Standards Advisory Board
750 First Street, NE, Room 1001
Washington, DC 20002

Telephone (202) 512-7350
Fax (202) 512-7366

TREASURY CLEARANCE SHEET

NO. 95-146366
Date _____

MEMORANDUM FOR: SECRETARY DEPUTY SECRETARY EXECUTIVE SECRETARY
 ACTION BRIEFING INFORMATION LEGISLATION
 PRESS RELEASE PUBLICATION REGULATION SPEECH
 TESTIMONY OTHER _____

FROM: Gerald Murphy

THROUGH: Deputy Secretary Newman

SUBJECT: Request to Approve Federal Accounting Standards Advisory Board Statement of Recommended Accounting Concepts, Entity and Display.

REVIEW OFFICES (Check when office clears)

- | | | |
|---|--|--|
| <input type="checkbox"/> Under Secretary for Finance
<input type="checkbox"/> Domestic Finance
<input type="checkbox"/> Economic Policy
<input checked="" type="checkbox"/> Fiscal
<input type="checkbox"/> FMS
<input type="checkbox"/> Public Debt

<input type="checkbox"/> Under Secretary for International Affairs
<input type="checkbox"/> International Affairs | <input type="checkbox"/> Enforcement
<input type="checkbox"/> ATF
<input type="checkbox"/> Customs
<input type="checkbox"/> FLETC
<input type="checkbox"/> Secret Service
<input type="checkbox"/> General Counsel
<input type="checkbox"/> Inspector General
<input type="checkbox"/> IRS
<input type="checkbox"/> Legislative Affairs
<input type="checkbox"/> Management
<input type="checkbox"/> OCC | <input type="checkbox"/> Policy Management
<input type="checkbox"/> Scheduling
<input type="checkbox"/> Public Affairs/Liaison
<input type="checkbox"/> Tax Policy
<input type="checkbox"/> Treasurer
<input type="checkbox"/> E & P
<input type="checkbox"/> Mint
<input type="checkbox"/> Savings Bonds

<input type="checkbox"/> Other _____ |
|---|--|--|

NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
INITIATOR(S)				
G. Murphy	<i>GM</i>	<i>5/10</i>	OFAS	2-0550
REVIEWERS				
John Bowman	<i>JB</i>	<i>5/17</i>	Asst. General Counsel (Banking & Finance)	2-1964
Neal Wolin	<i>NW</i>	<i>5/19</i>	Deputy General Counsel	2-0283
Dennis Foreman	<i>DF</i>			
Exec. Sec.				

SPECIAL INSTRUCTIONS

Review Officer

Date

Executive Secretary

Date

DEPARTMENT OF THE TREASURY
WASHINGTON

November 21, 1995

ACTION

ASSISTANT SECRETARY

MEMORANDUM FOR SECRETARY RUBIN

THROUGH: John D. Hawke, Jr. *JDH*
Under Secretary for Domestic Finance

FROM: Gerald Murphy *GM*
Fiscal Assistant Secretary

SUBJECT: Request to Approve Two Federal Accounting Standards Advisory Board (FASAB) Statements of Recommended Accounting Standards: "Accounting for Liabilities of the Federal Government" and "Accounting for Property, Plant, and Equipment."

ACTION FORCING EVENT:

Elmer B. Staats, Chairman, FASAB has transmitted the Board's completed action on two Statements of Recommended Accounting Standards: "Accounting for Liabilities of the Federal Government" and "Accounting for Property, Plant, and Equipment." Your approval as one of the three Principals of FASAB is requested. Requests for similar approval have been transmitted separately to the Director, Office of Management and Budget and Comptroller General of the United States.

RECOMMENDATION:

That you sign the attached FASAB approval sheets for the two Statements of Recommended Accounting Standards: "Accounting for Liabilities of the Federal Government" and "Accounting for Property, Plant, and Equipment."

Agree Disagree Let's Discuss

BACKGROUND/ANALYSIS:

This recommendation represents a significant effort in reaching FASAB consensus on providing recognition and measurement principles for Federal liabilities and property, plant, and equipment. (It should be noted that social insurance programs such as Social Security and Medicare are not included in the Statement of Recommended Accounting Standards: "Accounting for Liabilities of the Federal Government." Social insurance programs are addressed in a FASAB Exposure Draft on "Supplementary Stewardship Reporting.")

The National Performance Review recommended prompt development of a basic set of comprehensive Federal accounting standards. These two Statements of Recommended Accounting Standards represent a considerable portion of that basic set. The entire set of basic standards is expected to be completed before the end of this

EXECUTIVE SECRETARIAT

calendar year and will allow for agency reporting to be done in accordance with accounting standards developed for the Federal Government. The government-wide implementation of the basic set of standards will allow for consistent reporting as Treasury endeavors to prepare an audited Consolidated Financial Statement for the Federal Government as required by the Chief Financial Officers Act as amended by the Government Management Reform Act of 1994.

ATTACHMENTS: FASAB Recommendation Approval Sheets for Signature and Accompanying Transmittal Sheets from Elmer B. Staats, Chairman

Tab A: Statement of Recommended Accounting
Standard: "Accounting for Liabilities of
the Federal Government"

Tab B: Statement of Recommended Accounting
Standard: "Accounting for Property, Plant,
and Equipment"

Federal Accounting Standards Advisory Board

750 First Street, NE, Room 1001
Washington, D.C. 20002
(202) 512-7350
FAX: 512-7366

September 20, 1995

To: Secretary of the Treasury
Director, Office of Management and Budget
Comptroller General of the United States

Here for your approval is the Federal Accounting Standards Advisory Board's Statement of Recommended Accounting Standards, Accounting for Liabilities of the Federal Government.

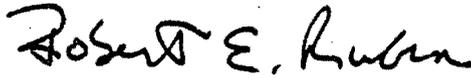
In developing the recommended standards, the Board issued an Exposure Draft to all federal agencies and to representatives of the private sector and the academic community. We also conducted a public hearing on this topic. Comments from all respondents were carefully reviewed and considered by the Board. The Board recommends that you adopt the standards contained in the enclosed statement.

The second page of the transmittal letter provides a signature block for you to indicate your approval of the statement.


Elmer B. Staats
Chairman

STATEMENT OF RECOMMENDED ACCOUNTING STANDARDS
ACCOUNTING FOR PROPERTY, PLANT, AND EQUIPMENT

APPROVED:



Robert E. Rubin
Secretary of the Treasury

November 30, 1995
Date

Signature pages for approval by Charles Bowsher, The Comptroller of the United States, and Alice M. Rivlin, Director, Office of Management and Budget, are forwarded under separate covers.

Federal Accounting Standards Advisory Board

750 First Street, NE, Room 1001
Washington, D.C. 20002
(202) 512-7350
FAX: 512-7366

September 20, 1995

To: Secretary of the Treasury
Director, Office of Management and Budget
Comptroller General of the United States

Here for your approval is the Federal Accounting Standards Advisory Board's Statement of Recommended Accounting Standards, Accounting for Property, Plant, and Equipment.

In developing the recommended standards, the Board issued an Exposure Draft to all federal agencies and to representatives of the private sector and the academic community. We also conducted a public hearing on this topic. Comments from all respondents were carefully reviewed and considered by the Board. The Board recommends that you adopt the standards contained in the enclosed statement.

The second page of the transmittal letter provides a signature block for you to indicate your approval of the statement.


Elmer B. Staats
Chairman

STATEMENT OF RECOMMENDED ACCOUNTING STANDARDS
ACCOUNTING FOR LIABILITIES OF THE FEDERAL GOVERNMENT

APPROVED:

Robert E. Rubin :

Robert E. Rubin
Secretary of the Treasury

November 30, 1995
Date

Signature pages for approval by Charles Bowsher, The Comptroller of the United States, and Alice M. Rivlin, Director, Office of Management and Budget, are forwarded under separate covers.

TREASURY CLEARANCE SHEET

NO. _____
Date _____

MEMORANDUM FOR: SECRETARY DEPUTY SECRETARY EXECUTIVE SECRETARY
 ACTION BRIEFING INFORMATION LEGISLATION
 PRESS RELEASE PUBLICATION REGULATION SPEECH
 TESTIMONY *Gm* OTHER _____

FROM: Gerald Murphy, FAS

THROUGH: Under Secretary John D. Hawke, Jr. *11/21/95*

SUBJECT: Request to Approve Two Fed. Actg. Standards Advisory

REVIEW OFFICES (Check when office clears) for Liabilities of the Fed. Govt. "Accounting for Property, Plant, and Equipment."
 Board (FASAB) Statements of Recommended Actg. Standards: "Accounting for Property, Plant, and Equipment."

- | | | |
|---|--|--|
| <input type="checkbox"/> Under Secretary for Finance
<input type="checkbox"/> Domestic Finance
<input type="checkbox"/> Economic Policy
<input checked="" type="checkbox"/> Fiscal
<input type="checkbox"/> FMS
<input type="checkbox"/> Public Debt

<input type="checkbox"/> Under Secretary for International Affairs
<input type="checkbox"/> International Affairs | <input type="checkbox"/> Enforcement
<input type="checkbox"/> ATF
<input type="checkbox"/> Customs
<input type="checkbox"/> FLETC
<input type="checkbox"/> Secret Service
<input type="checkbox"/> General Counsel
<input type="checkbox"/> Inspector General
<input type="checkbox"/> IRS
<input type="checkbox"/> Legislative Affairs
<input type="checkbox"/> Management
<input type="checkbox"/> OCC | <input type="checkbox"/> Policy Management
<input type="checkbox"/> Scheduling
<input type="checkbox"/> Public Affairs/Liaison
<input type="checkbox"/> Tax Policy
<input type="checkbox"/> Treasurer
<input type="checkbox"/> E & P
<input type="checkbox"/> Mint
<input type="checkbox"/> Savings Bonds

<input type="checkbox"/> Other _____ |
|---|--|--|

NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
INITIATOR(S)				
Gerald Murphy	<i>Gm</i>	<i>10/13</i>	Fiscal Asst. Secretary	2-0550
REVIEWERS				
John Bowman*	<i>JB</i>	<i>11/9</i>	Asst. General Counsel	2-1964
Ed Knight	<i>EN</i>	<i>11/13</i>	General Counsel	2-0287
John Hawke			Under Secretary for Domestic Finance	2-0387
Exec. Sec.				

with
 * We understand that FASAB will send a memorandum to all of the principals addressing our concern on page 50 of Appendix A P 129. Mr. Rubin's signature on the original signature page acknowledges acceptance of this change. (Draft of memorandum attached)

SPECIAL INSTRUCTIONS

PLEASE RETURN TO ROOM 2112 FOR MAILING TO FASAB.
THANKS.

DOROTHY, " "

DRAFT

Date: November 9, 1995

to: Principal

From: ASAB Member

Re: Ronald S. Young, Executive Director

Sub: Statement of Recommended Accounting Standards
Accounting for Liabilities of the Federal Government

As informed by the General Counsel's office at the Department of the Treasury
to the US Constitution in Appendix A (Basis for Conclusion) is not
feasible we will be modifying one page of the final printed Statement to reflect
this change. This deletion is not a substantive change and does not affect the
substance or the point of the paragraph

The attached pages reflect 1) the deletion to be made and 2) the revised page

Your signature on the original signature page acknowledges your accepta-

tion. If you have any problems with the deletion please call me to discuss the

consequences to you in carrying this change may cause you.

50.

Appendix A Basis for Conclusions

EXCHANGE AND NONEXCHANGE TRANSACTIONS

- 126 As noted in SFFAC No. 1, *Objectives of Federal Financial Reporting*: "The accounting process begins with recording information about transactions between the government (or one of its component entities) and other entities, that is, inflows and outflows of resources or promises to provide them."⁶³ In some transactions, consideration of value is exchanged: there is a reciprocal or two-way flow. Other transactions, such as grants and other transfer payments are nonexchange transactions (i.e., there is a nonreciprocal transaction--normally a one-way flow).
- 127 The federal government is the vehicle through which citizens of the nation exercise their sovereign power. In this role, the federal government is responsible for taking collective action at the national level "to promote the general welfare." Thus the government undertakes many programs that do not involve reciprocal transfers between the government as an entity and its counterparties. Examples include disaster relief, grants to state and local governments, subsidies, and other transfer programs for individuals. The federal government has a propensity to assume such burdens because it is the agent by which the society, through its elected officials, accomplishes transfers between groups of citizens to enhance their well-being.
- 128 A taxpayer or a donor may, in fact, receive a benefit of some sort, such as the opportunity to live in a safe, secure environment; to improve one's standard of living; and to receive specific benefits, such as visits to national parks and travel over highways. But it is not ordinarily said that the benefit to the individual taxpayer or donor is of value comparable to that of the consideration given. Therefore, these are classified as nonexchange transactions. For this Statement, the significance of the distinction between exchange and nonexchange transactions arises from the nature of the obligation that is created when one party to a transaction provides a product or service to the other party in return for a promise that something of value will be exchanged for it.
- 129 Obligations become legally enforceable claims against the federal government in different ways and at different points within transaction cycles that relate to various programs. An important factor in distinguishing between various programs is whether an exchange is involved. For example, under the U.S. Constitution, the federal government may not contract for and receive goods or services and then arbitrarily decide not to honor the contract. Similarly, under

50

Appendix - Basis for Conclusions

EXCHANGE AND NONEXCHANGE TRANSACTIONS

- 126 As noted in SFFAC No. 1, *Objectives of Federal Financial Reporting*: "The accounting process begins with recording information about transactions between the government (or one of its component entities) and other entities, that is, inflows and outflows of resources or promises to provide them."¹⁰³ In some transactions, consideration of value is exchanged: there is a reciprocal or two-way flow. Other transactions, such as grants and other transfer payments are nonexchange transactions (i.e., there is a nonreciprocal transaction--normally a one-way flow).
- 127 The federal government is the vehicle through which citizens of the nation exercise their sovereign power. In this role, the federal government is responsible for taking collective action at the national level "to promote the general welfare." Thus the government undertakes many programs that do not involve reciprocal transfers between the government as an entity and its counterparties. Examples include disaster relief, grants to state and local governments, subsidies, and other transfer programs. The federal government has a propensity to assume such burdens because it is the agent by which the society, through its elected officials, accomplishes transfers between groups of citizens to enhance their well-being.
- 128 A taxpayer or a donor may, in fact, receive a benefit of some sort, such as the opportunity to live in a safe, secure environment, to improve one's standard of living; and to receive specific benefits, such as visits to national parks and travel over highways. But it is not ordinarily said that the benefit to the individual taxpayer or donor is of value comparable to that of the consideration given. Therefore, these are classified as nonexchange transactions. For this Statement, the significance of the distinction between exchange and nonexchange transactions arises from the nature of the obligation that is created when one party to a transaction provides a product or service to the other party in return for a promise that something of value will be exchanged for it.
- 129 Obligations become legally enforceable claims against the federal government in different ways and at different points with respect to transactions that relate to various programs. An important factor in distinguishing between various programs is whether a legal obligation is involved. For example, the federal government may be contractually bound to provide goods or services and then arbitrarily decide not to honor the contract. Similarly, under existing law, the federal government

1997-SE-010385



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

SEP 26 1997

INFORMATION

MEMORANDUM FOR SECRETARY RUBIN

THROUGH: Under Secretary John D. Hawke, Jr. (Signed)

FROM: Roger L. Anderson (Signed)
Deputy Assistant Secretary (Federal Finance)

SUBJECT: FASB's New Draft Accounting Standard for Derivatives

SUMMARY:

In June 1996, FASB issued an Exposure Draft on how to improve accounting standards for derivatives, after considering the topic for over ten years. For the past year, the draft has been the object of public comment and considerable criticism, particularly from the banking industry and Chairman Greenspan. FASB issued a revised draft of its proposals on August 29, and will take comments for 45 days. The rules would become effective for fiscal years beginning after December 15, 1998. FASB's new draft contains changes which should appease some in the industry, such as allowing rollovers of hedges.

DISCUSSION:

Features of FASB Proposal

The first key feature of FASB's proposal is that all derivatives would be moved out of the footnotes and on to the balance sheet and income statement. The second key feature is that derivatives would be measured at their fair value on the balance sheet. On the income statement, gains and losses would be accounted for in different ways, depending on the reason for holding the instrument.

- If a derivative is not designated as a hedge of another instrument, it would be carried at fair value on the balance sheet and changes in its fair value would be recognized currently in earnings as gains or losses. Speculative positions in derivatives would fall into this category.
- A "fair value" hedge is a derivative that is identified as hedging exposure to changes in the fair value of a recognized asset or liability or of a firm commitment. Gains or losses in the fair value of a derivative designated as a "fair value" hedge, together with the offsetting loss or gain on the hedged asset or liability, would be recognized currently in earnings.
- A "cash flow" hedge is a derivative that is identified as hedging exposure to variability in the cash flows of a recognized asset or liability or of a forecasted (but not firmly committed) transaction. The effective (hedging) aspect of a derivative designated as a

“cash flow” hedge would be reported as a component of other comprehensive income on the balance sheet but would not be recognized in earnings until the period during which the forecasted transaction affects earnings.

Criticism of the FASB Proposal

A torrent of criticism has been unleashed on FASB's proposal. Chairman Greenspan has sent two letters in opposition (Greenspan's letter of July 31, 1997, and FASB's response are at Tab A). FASB has dealt with many of the issues cited in Greenspan's first letter, which was dated November 1, 1996, and cosigned by the OCC and the FDIC. In addition, twenty industry CEOs sent a letter to FASB opposing the project (Tab B). Another letter in opposition was sent to Senator Gramm by the ABA Securities Association, America's Community Bankers, the American Bankers Association, ISDA, the New York Clearing House Association, and the Treasury Management Association (Tab C).

The more substantive charges are that the new standard would:

- increase balance sheet and income statement volatility;
- eliminate managers' ability to smooth financial statement volatility by recognizing changes in the value of derivatives at advantageous points in time;
- discourage managers from using derivatives to hedge risks;
- make it difficult and, in some cases, impossible to achieve hedge accounting treatment for diverse portfolio or “macro” hedges;
- represent a “piecemeal approach” to the introduction of fair value accounting; and
- place intolerable burdens on managers who are already struggling to make year 2000 systems changes.

One example of banks' concern over balance sheet volatility is that, if they use derivatives to lock in expected future funding costs, they would have to follow the “cash flow” model for forecasted transactions. If interest rates fell, banks would have to report the derivatives' loss in value under “other comprehensive income” in equity on the balance sheet. They would not be allowed to offset this loss on derivatives against the expectation of paying lower financing costs in the future.

Banks are also concerned that the proposed rules would make it more difficult to hedge the duration gap between deposits and associated investments. Banks would not be able to offset swings in the fair value of this type of hedge against swings in the banks' valuation of deposits, because, under FAS 107, the fair market value of deposits is their book value. As a result, the existence of a hedge could cause swings in the income statement. FASB responds that a bank could designate a specific investment as the object of the hedge, as long as the asset had similar maturity, risk and other features as the hedged net position, and match gains or losses on the hedge to offsetting gains or losses on the fair value of the asset. The banks argue that this is impossible to do, or that FASB is making them jump through hoops. FASB says this is necessary to resolve timing and recognition issues that would arise with a net position.

Some firms are also concerned about the consequences of hedging "held-to-maturity" assets. Under existing rules, "held to maturity" securities are carried at historical cost, so that a firm would not be able to offset the gain or loss on a derivative against the gain or loss on a security. FASB says that it will allow firms to reclassify their securities as "available for sale," which would enable firms to carry the securities at fair value. Firms counter that this could increase volatility in financial statements since not all the risks embodied in a security may be hedged by the derivative. This could be a particular problem for entities such as the Federal Home Loan Banks and Freddie Mac, who only hedge the prepayment risk on mortgage-backed securities that they hold to maturity.

Some firms may have difficulty meeting FASB's deadline for implementation (January, 1999), while they struggle to solve Year 2000 problems. There is also some concern that the new rules could affect the calculation of bank capital requirements. However, the bank regulators could negate the effect of these new accounting rules for the purposes of bank capital requirements.

Broker-dealers' financial statements should not be much affected by the FASB proposal. They are already required to mark most of their assets and liabilities to market. However, some of these firms are apparently concerned about how these rules may affect their customers' use of derivatives.

FASB has responded to the criticisms by saying that its proposal would not, by itself, "increase" volatility. Instead, the proposal would require firms to report on the balance sheet and income statement volatility that already exists in the value of their derivatives holdings.

In addition, the new standard should not discourage managers from using derivatives to hedge risks. Instead, the new requirements should clarify for investors which derivatives are effective in hedging and make it more difficult to conceal the imprudent use of derivatives.

Other groups support FASB's proposal. The Association for Investment Management and Research (AIMR) testified in favor of FASB's proposal at a March, 1997 Senate hearing. The American Institute of Certified Public Accountants supports the proposal, although it suggests a few technical changes and recommends delaying implementation for an additional year. GE, GM, McDonalds, Vanguard and T. Rowe Price have also issued written statements in support of FASB's proposal. SEC Chairman Levitt has given public support to FASB's proposal. A favorable piece from the Wall Street Journal editorial page is attached (Tab D).

The International Accounting Standards Committee (IASC) is considering whether to adopt a "core" set of U.S. standards on financial instruments as part of IASC's work towards a harmonized international standard. IASC has proposed that FASB's derivatives proposal be included in the core set. Paradoxically, U.S. firms may find IASC's core set to be very attractive for cross-border filings, because it would not include other elements of U.S. generally accepted accounting principles.

Inflation-Indexed Securities

FASB has tentatively decided to account for inflation-indexed notes by breaking them into "host" instruments and "embedded" derivatives. Each piece would be accounted for separately, according to the goal for which it was used. FASB staff is clearly open to discussion on this point. On the other hand, investors would have the option (under FAS 115) to mark the entire inflation-indexed note to market. Small investors would not be affected by FASB rules.

ATTACHMENTS:	Tab A	Letter to FASB from Chairman Greenspan dated July 31, 1997, and FASB response
	Tab B	Letter to FASB from industry CEOs
	Tab C	Letter to Senator Gramm from ABA Securities Association, America's Community Bankers, the American Bankers Association, ISDA, the New York Clearing House Association, and the Treasury Management Association
	Tab D	Wall Street Journal editorial page column

TREASURY CLEARANCE SHEET

NO. _____
Date 9/16/97

MEMORANDUM FOR: SECRETARY DEPUTY SECRETARY UNDER SECRETARY
 ACTION BRIEFING INFORMATION LEGISLATION
 PRESS RELEASE PUBLICATION REGULATION SPEECH
 TESTIMONY OTHER _____

FROM: Roger Anderson *RA*
 THROUGH _____

SUBJECT: FASB's New Draft Accounting Standard for Derivatives
 REVIEW OFFICES (Check-when office clears)

- | | | |
|--|--|---|
| <input type="checkbox"/> Under Secretary for Finance | <input type="checkbox"/> Enforcement | <input type="checkbox"/> Policy Management |
| <input type="checkbox"/> Domestic Finance | <input type="checkbox"/> ATF | <input type="checkbox"/> Scheduling |
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| <input type="checkbox"/> Under Secretary for Int'l Affairs | <input type="checkbox"/> Inspector General | <input type="checkbox"/> Mint |
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INITIATOR(S)				
AShelton	<i>AMS</i>	<i>9/16/97</i>	Policy Analysis	2-0101
REVIEWERS				
NCarleton	<i>NC</i>	<i>9/16/97</i>	Policy Analysis	2-1855

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Review Officer Date: _____ Executive Secretary Date: _____