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Comments on exposure draft, *Comprehensive Long-Term Projections for the U.S. Government*

Q1. This exposure draft proposes reporting that would support FASAB Objective 3, Stewardship, and in particular, Sub-Objective 3B:

Objective 3: Federal financial reporting 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 condition has changed and may change in the future.¹

Sub-Objective 3B: Federal financial reporting should provide information that helps the reader to determine whether future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due.²

More detailed discussion of the reporting objective and the objectives of fiscal sustainability reporting can be found in paragraphs 1 through 8.

Do you believe that the proposed reporting adequately supports the above objectives? Are there different reporting requirements that might better support the above objectives or that you believe should be added to the proposed requirements in this exposure draft? If so, please explain.

[In paragraph 6 of the exposure draft, the thrust of the Statement is characterized as "Fiscal Sustainability Reporting." The paragraph further indicates that reporting should address whether future budgetary resources will likely be sufficient to sustain public services and meet obligations as they come due. Paragraph 8 indicates that the reporting should be "easily understandable to the 'average citizen' who has a reasonable understanding of federal government activities and is willing to study the information with reasonable diligence."](#)

[With these stated objectives, Illustration 3 in Appendix 3 comes by far the closest to meeting these criteria. This example compares on a year-by-year basis the projected revenues and obligations of the federal government under "current policy without change." However, the example has two shortcomings that are highly misleading and](#)

¹ SFFAC 1, par. 134.

² SFFAC 1, par. 139.

should be changed. The first is simple. The obligations should not be described as spending. The ED indicated understanding that much of the shortfalls of revenue would in fact preclude spending, particularly in the OASDI and HI programs, once their Trust Fund assets are exhausted under current law. Thus, the full obligations cannot be referred to as spending per se, and the obligations should be referred to as such, "obligations."

The second problem with Illustration 3 is the inclusion of interest accruals in the graph as if they are "spending." This is highly misleading. The comparison in the graph should be actual expected tax (and premium) revenue to expected obligations for services of the government. In the scenario depicted, the "interest" would not in fact be "spending" at all, but rather borrowing. The difficulty of the presentation with the interest included can be seen by considering the case where non-interest obligations were met by relatively modest increases in receipts after 2010. In this case, the large growth in interest accruals would not occur. Thus, by including these accruals, the graph is in effect double counting, or more, the extent of the fiscal shortfalls that must be met on an annual basis in order to avoid overwhelming growth in debt and interest. These changes should be made to Illustration 3, and then this could be the principal illustration of the sustainability of federal obligations: it will show both the extent of the obligations as a percent of the GDP on a year-by-year basis and the level of expected receipts on an annual basis under current policy.

Given the stated objectives, measures summarizing large amounts of receipts and obligations over a number of years on a present-value basis should be either eliminated entirely or greatly deemphasized. Such summary numbers that run into trillions of dollars have little meaning to the average citizen, as does the concept of present value. Relationships of receipts and obligations, one year at a time, are far more accessible and understandable. In addition, they illustrate the timing and trend in projected obligations, shortfalls, and surpluses that are critical to any concept of "sustainability."

Q2. In this proposed Statement, projections are prepared not to predict the future, but rather to depict results that may occur under various conditions. Accordingly, projections require assumptions to be made about the future. This exposure draft proposes broad and general guidance for selecting policy, economic, and demographic assumptions for long-term projections with a primary focus on the future implications of the continuation of current policy without change for federal government public services and taxation. The guidance begins at paragraph 19. Paragraph 28 explains that although current law is a reasonable starting point in selecting policy assumptions, a simple projection of "current law" would not always reflect current policy without change. Examples are provided.

Do you believe that the guidance for assumptions is appropriate? If not, please suggest alternative guidance. Please provide the rationale for your response.

Overall, the guidance for allowing the preparer to use judgment in selecting the assumptions is appropriate. The statement that "projections are not forecasts or predictions; they are designed to depict results that may occur under various conditions"

provides a clear distinction between the goals of projections and the role of assumptions in developing those long-term projections. The definitions and examples provided for policy, economic, and demographic assumptions are very clear and understandable, specifically the examples of the assumptions applied to the Social Security program in paragraph 26.

The guidance in paragraph 31 regarding the selection of economic and demographic assumptions for the Social Security and Medicare programs is also appropriate. The assumptions used in the SOSI have been thoroughly vetted and audited and are therefore a practical and sound choice for the basic financial statement.

However, selection of policy assumptions using the “current policy without change” concept is quite problematic in some cases relative to the law. In cases where discretionary spending authority expires, the concept is clear. But where current law is explicit on limitations on spending, such as in OASDI and HI, obligations beyond what the law can support for spending must be qualified as only obligations and cannot be depicted as spending per se. Similarly, where the tax law is specific, as in the indexation of personal income tax brackets, this specific legal guidance must be reflected, in this case with increasing receipts as a percent of GDP per the CPI indexing of brackets. This projection of the “obligations” for payment of personal tax liability under current law is analogous to the depiction of the obligation to provide benefits under Social Security and Medicare at an increasing level relative to GDP. In both cases, the law specifies that these increases and the obligations can be altered only with a change in law. To depict only one of these increases in obligations and not the other would be highly misleading and biased in representation. If, for example, current policy were deemed to maintain the receipts and obligations of each element at their current level as a percent of GDP, then the depiction of sustainability would show no change through time. Such clear changes through time as in the benefit obligations of a defined benefit program like Social Security and the tax obligations of a well-defined tax schedule like that for personal income tax should be reflected directly and should not be presumed to be representable as a simple constant percent of GDP in either case.

Q3. This exposure draft proposes a basic financial statement³ and disclosures. (Description begins at paragraph 35 and an illustrative example of the basic financial statement is provided in Appendix B.) The Board has indicated that the primary audiences for the consolidated financial report of the U.S. Government (CFR) are citizens and citizen intermediaries such as journalists and public policy analysts.

Do you believe that the basic financial statement and disclosures would be understandable and meaningful for the primary audiences of the CFR? Please note any changes that you believe should be made to the proposed requirements for the basic financial statement and/or the disclosures.

³ The basic financial statement will be presented as RSI for a period of three years and subsequently as a basic financial statement.

First, this report should not be classified as a basic financial statement. The information is based on projections and assumptions and should not be held to the same audit standards as conventional financial reports.

One specific change is essential, as described above in response to Question 1. The obligations indicated must not be referred to as “spending” because of the recognized limitations on spending in certain programs (OASDI and HI) under current law. In addition, as described above, the “Rest of Federal Government” category must reflect the obligation under current law and must not be limited to the current percent of GDP as some concept of current policy.

However, the information proposed to be presented is understandable and meaningful to the primary audiences of the CFR, even if not to the general public. Particularly, the breakout of receipts and spending between Medicare, Medicaid, and Social Security is valuable, as these programs generally draw the most media attention and concern. The use of “% of GDP” is a useful measure and can be understood by the basic user. Likewise, the comparison to the prior year is a useful measure for the basic user. However, the concept of “present value” is complex and may not be understood by many users. The calculations that are involved in developing a present value figure, such as selection of interest rates and the time value of money, are detailed and complex for the average citizen to understand.

Q4. The Board is proposing that the basic financial statement display the difference between projected revenue and projected spending, and that the fiscal gap (the change in non-interest spending and/or revenue that would be necessary to maintain public debt at or below a target percentage of gross domestic product (GDP)) must be reported either on the face of the basic financial statement or in a disclosure. Also, the fiscal gap may be reported for a specific debt level or over a range of debt levels (see paragraph 38). Both options for reporting fiscal gap are illustrated in Appendix B (see pages 51 (narrative on the face of the financial statement) and 61 (disclosure)). See paragraphs A60-A63 in the Basis for Conclusions for an explanation of the pros and cons of the options.

a. Do you agree with the flexible requirements for reporting fiscal gap?

While “fiscal gap” is appealing at a conceptual level, it introduces a complication that requires additional explanation and care in calculation. Maintaining public debt to GDP at a constant ratio would be simple if GDP itself rose at the rate used for interest discounting, or, in other words, if the present value of GDP for any future year were a constant value, equal to this year’s GDP. In this special case, maintaining annual revenue exactly equal to annual obligations would precisely maintain the current ratio of public debt to GDP. But in a world where real GDP is projected to grow at roughly 2 percent in the future, and where interest discounting is done at a real rate of about 3 percent, the present value of GDP is smaller the farther we look into the future. Thus, to maintain public debt at a constant percentage of GDP in the future, we would need annual receipts to exceed annual obligations by the amount needed to slow the growth of public debt to the growth rate of GDP. The additional receipts over annual

obligations would be roughly 1 percent of the amount of public debt each year. While this is analytically straightforward, it is a complication that requires explanation.

In order to show what is necessary to “maintain” public debt at a given percent of GDP, the “fiscal gap” should be considered on an annual basis. It would indicate the small adjustment to the gap between receipts and obligations needed to adjust the public debt level to maintain debt at the target percentage of GDP. However, the cost and complexity of presentation would be large in relation to the added value of the measure.

On a summary level for a period of many years, there is a perfect analog to the fiscal gap concept that has been in long use for OASDI and HI programs. The Social Security and Medicare Trustees have targeted generally a trust fund level equal to a constant 100 percent of expected annual obligations. Because annual obligations, like GDP, grow at a rate different from the annual interest (discount) rate, the relationship between annual cash-flow balance (receipts minus obligations) and the ratio of the trust fund assets to annual outgo is complicated. To address this complication, the Trustees use the concept of “actuarial balance,” which when precisely achieved, will result in having a ratio of trust fund assets to annual expenditures at the end of the summary period at the target level (100 percent).

For total federal government operations, a summary “fiscal gap” concept could be derived that is analogous to the actuarial balance. For a given period (say a 75-year projection period), this would be equal to the PV of projected obligations over the period minus the PV of projected receipts over the period plus the current amount of public debt minus the PV of the target level of public debt at the end of the period. Thus, the difference between this “fiscal gap” measure for a period and the more usual balance between the PV of receipts and obligations for the period is just the difference between the amount of the current-year public debt and the PV of the “ending year” target level of public debt. This difference is likely to be fairly small relative to the balance between receipts and obligations, and so it may be questionable whether the complication is on balance desirable for the financial statement. If this concept is to be included as a summary measure at any level, then the precise nature of the measure, in relation to starting and ending levels of public debt, must be made clear and explicit. Moreover, if this summary measure for a substantial time period is presented, it must be clear that attaining the target level of public debt to GDP is only assured for a single point in time (the end of the period), and that maintaining the target level is in no way indicated by reducing the fiscal gap to zero for the period as a whole. If “maintaining” a fiscal gap at a given level is desired, then an annual presentation of the fiscal gap is essential.

- b. Do you believe that the illustrative disclosure (Illustration 8 in Appendix B) is clear and understandable?

Illustration 8 would be confusing to the target audience. The graphs show a varying fiscal gap (Illustration 8a) and varying needed changes in revenue or non-interest spending (Illustration 8b) based on a range of debt to GDP ratios. Both graphs present a significant amount of complex information in a not particularly useful or easily understandable way. Moreover, these illustrations do nothing to indicate the actual

changes over time that would be needed to maintain a constant ratio of public debt to GDP.

A far simpler illustration of the fiscal gap concept that would actually be related to sustainability would be to show the annual amount needed each year in addition to projected receipts to cover annual obligations and to maintain the public debt at the current level as a percentage of GDP. As indicated above, this would, in general, be about the difference between projected obligations and revenues for each year, plus about 1 percent of the amount of public debt that is targeted for the year. This illustration, while somewhat complex, would at least have relevance to sustainability as it would show both the timing and trend in annual gaps.

A summary measure of fiscal gap might be useful, but requires care in description and explanation. The measure should be analogous to the actuarial balance used for the OASDI and HI Trust Funds. That is, it should be equal to the PV of projected obligations over the period minus the PV of projected receipts over the period plus the current amount of public debt minus the PV of the target level of public debt at the end of the period. But as with the “actuarial balance,” this value should not be presented in present value dollar terms. To show a summarized gap for many years in PV dollars provides no useful context to the average citizen. The PV dollar gap should be presented only as a percentage of a similar summary measure over the same period, which would most usefully be the PV of GDP over the period. The measure would thus be interpreted as “the average gap as a percent of GDP over the period as a whole.” Care would need to be taken to assure the reader understood that reducing this gap to zero with either a flat percentage change in future tax rates or in future benefit levels would not suffice to maintain a constant ratio of public debt to GDP. It would only serve to assure that the ratio of public debt to GDP would be the same at the end of the summary period as at the beginning, with no assurance at all as to the levels of public debt through the period, and not to the trend in the ratio of public debt to GDP at the end of the period. Thus, such a summary measure must be understood not to relate to sustainability, and so should not be included on the face of the financial statement.

- Q5. Finite and infinite time horizons for fiscal projections are discussed in the Basis for Conclusions, paragraphs A53 through A59. This exposure draft proposes the following requirements regarding time horizons for projections: (a) the projections presented in the basic financial statement should be “sufficient to illustrate long-term sustainability” (for example, traditionally the Social Security program has used a projection period of 75 years for long-term projections); (b) projections for both a finite and an infinite horizon should be provided, one in the basic financial statement and the other in the disclosures; and (c) either the basic financial statement or the disclosures should include projections for Social Security and Medicare based on the time horizon used for long-term projections for Social Security and Medicare in the Statement of Social Insurance (SOSI).
- a. Do you believe that the above requirements for time horizons are appropriate to meet the reporting objectives of Fiscal Sustainability Reporting?

Specifically, do you believe that data for both finite and infinite horizon projection periods should be reported? If not, please explain.

Neither the finite nor the infinite summary measure is useful in assessing sustainability because neither addresses the timing or trend in levels of cost or shortfalls or surpluses. These can only be discerned from the annual estimates of receipts and obligations (exclusive of interest), or from a series of annual gap measures described above. The summary measures over the next 75 years provide a useful indication of the expected adequacy of future receipts to provide for obligations over the period as a whole. However, failure of this summary measure to indicate the time within the period for which resources may be adequate and the time for which resources are expected not to be adequate renders the measure a highly limited indicator. In effect, the measure provides only one unambiguous indication: that is, whether the accumulated account between receipts and obligations over the entire period will be in balance at the very end of the period. The status at any point within the period cannot be determined or suggested by the value for the summary measure. As limiting as this is for the usefulness of the summary measure over 75 years, it clearly renders the summary measure over the infinite future period useless and effectively meaningless.

Therefore, to the extent that any summary measure is included, it should be limited to at most the 75-year period used by Social Security and Medicare in the SOSI. Infinite period measures should be eliminated from any serious consideration. Moreover, in order to address sustainability, it is critical to have a measure that actually addresses the timing and trend in any gaps and thus can illustrate where and how much change is needed. Here an analog to the Social Security test of "sustainable solvency" would be useful. The analog for the federal government consolidated account would be the combination of (1) the 75-year summary measure (fiscal gap), indicating the overall adequacy of receipts to cover obligations for the period as a whole with the targeted level of public debt at the end of the period, and (2) the sequence of annual levels of public debt as a percent of annual GDP, in order to see if the trend in the ratio is stable, and thus sustainable. By far the most critical part of the measure is the latter portion. To address sustainability of the financing of the federal government consolidated operations, a graph of the projected annual gaps between expected receipts minus obligations and the necessary excess of receipts over obligations to maintain the target level of public debt would be necessary and sufficient. Anything more would only serve to complicate the presentation.

- b. Do you believe that there should be a specific time horizon requirement (for example, 75 years) for the basic financial statement for Fiscal Sustainability Reporting and/or the SOSI? If so, what time horizon do you believe should be required?

There should be a specific time horizon requirement of 75 years for the basic financial statement for Fiscal Sustainability and/or the SOSI. This is consistent with the 75-year period used in both the Social Security and Medicare Trustees Reports, and has a long history of acceptability and usefulness. With the annual gap concept presented as a percent of GDP for this period, the average citizen would have a simple, straightforward

presentation of the magnitude and timing of the gaps that the country faces for the future.

Q6. The Board's mission is to issue reporting requirements for the federal government's general purpose financial statements, and not to recommend budget policy. This exposure draft proposes a title for the basic financial statement: "Long-Term Fiscal Projections for the U.S. Government." An alternative title, "Statement of Fiscal Sustainability," might imply to some that the Board has established or plans to establish specific rules that define "fiscal sustainability" and/or budget rules that would result in fiscal sustainability. However, others have indicated that the "plain English" meaning of the words "fiscal" and "sustainability" should be adequate, and that the title "Statement of Fiscal Sustainability" might be more appropriate.

The Board's working definition of "fiscal sustainability" is explained in the Basis for Conclusions, paragraph A3. The concept of "Financial Condition" is explained in the Basis for Conclusions, paragraphs A7 and A8.

Which of the following do you believe that the basic financial statement should be titled?

- a. Long-Term Fiscal Projections for the U.S. Government
 - b. Statement of Fiscal Sustainability
 - c. Statement of Financial Condition
 - d. A title not listed above (please specify)
- Please explain the reasons for your choice.

The most appropriate title for the basic financial statement as currently written is "Long-Term Fiscal Projections for the U.S. Government." The other two titles presented include the word "statement," which is not appropriate for an illustration that consists of projections and hypotheticals, which is much different from a balance sheet or statement of budgetary resources, which present the results of operations at the current time or that have already occurred. In addition, the statement as currently written does not truly address fiscal sustainability in terms of the timing and trend of future receipts and obligations, and thus should not be titled as such.

If the measures presented were indeed modified to address timing and trend of gaps as described above, then "Statement of Fiscal Sustainability" might be appropriate.

Q7. This exposure draft proposes a minimum level of disaggregation for the basic financial statement. For projected receipts, major programs such as Medicare and Social Security would be shown separately from the rest of government. For projected spending, major programs such as Medicare, Social Security, and Medicaid would be shown separately from the rest of government. (See paragraphs 36 and A46-A49.)

- a. Do you believe that the above general guidance provides for an appropriate level of disaggregation in the basic financial statement? Please explain the basis for your view.

While showing Medicare, Medicaid, and Social Security is an excellent starting point, additional disaggregation would be useful. In the example presented in Appendix B, the “All Other Receipts” and “Rest of the Government” categories represent significant portions of total receipts and total “spending” that should be disaggregated further. By not doing so, the statement appears to be “hiding” or “burying” totals for other programs.

Moreover, combining all other programs invites oversimplification of the type that would lead to assuming that receipts or obligations might remain a constant percentage of GDP in the future. The statement should be more rigorous if it is to be useful beyond the already well-developed projections of receipts and obligations for Social Security and Medicare. Specific projections with explicit assumptions should be required for all major federal programs, including defense expenditures and health spending.

- b. Do you believe that specific line items (instead of or in addition to the “major programs” required by paragraph 36 of the ED) should be disaggregated in the basic financial statement? If so, please identify the line items and explain your reasoning.

No, disaggregation by “major programs” is sufficient. However, the “major programs” should not be limited to those listed. While projecting future costs for programs like defense may be difficult, the statement will have no significance beyond already available projections for Social Security, Medicare, Medicaid, and SSI without the further identification of specific federal programs.

Q8. This exposure draft proposes that disclosures should explain and illustrate the major factors impacting projected receipts and spending (such as the rising cost of health care) (see paragraph 42(a)). Illustrative examples in Appendix B begin on page 52).

- a. Do you believe that an explanation and illustration of the major factors impacting projected receipts and spending will be helpful to readers? Please explain the basis for your view and note any recommended changes in the requirements.

An explanation and illustrations will be helpful to users. Users of the statements should be aware of the major factors that may affect projected receipts and spending. However, with such additional disclosures goes the obligation to provide balanced and thorough analysis. Even when assumptions and projections are appropriate and balanced, wrong impressions may be conveyed by inappropriate factor analysis.

- b. Do you believe that the display of a range for major cost drivers and/or major programs, as shown in Illustrations 1a and 1b in Appendix B should be optional or mandatory? Please explain the basis for your view.

