AICPA

March 30, 2009

Ms. Wendy M. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mailstop 6K17V
441 G Street, NW, Suite 6814
Washington, DC 20548

Dear Ms. Payne:

The American Institute of Certified Public Accountants (AICPA) has reviewed the Federal Accounting Standards Advisory Board (FASAB) Exposure Draft (ED), *Accounting for Social Insurance, Revised*, and is pleased to offer its comments. While there are certain aspects of the ED that may provide some marginal improvement in the level of information provided on social insurance, there are several significant aspects of the ED that concern us. First, there was no move forward by the Board to change the expense and related liability recognition requirements in Statement of Federal Financial Accounting Standard (SFFAS) 17, *Accounting for Social Insurance,* as we had recommended in our previous comment letter on the related Preliminary Views (PV) document. Second, the large number of Board members supporting various alternative views is unusual for such a significant ED and appears to have led to compromises that restrict the degree of improvement in the information provided.

We continue to believe that the social insurance programs covered by the ED are currently executed and publicized as exchange programs and that there should be expense and liability recognition. It also continues to be our view that with each period of covered employment, workers and their employers exchange a commitment to pay earmarked taxes for a promise from the government to provide social insurance benefits in the future. That approach incorporates measurement and attribution qualities similar to those used in the financial reports of business enterprises, as well as state and local governments in the United States.

As noted in our previous comment letter on the PV, the recognition question that continues to be deliberated by the Board goes to the very heart of what financial statements should be—in this case, the financial statements of a sovereign national government. Financial statements have the purpose of serving their users. In the world of commerce, they are used to assist providers of capital in making their decisions as to how that capital shall be allocated and deployed. For governments, financial statements are used to monitor performance and stewardship, but perhaps even more importantly, to assist citizens, their elected representatives, and civil servants to formulate economic, social, and political policy. Generally, financial statements should provide information in a neutral, unbiased manner to allow users to make key decisions, including policy decisions. A critical issue involves determining where to draw the line between financial reporting versus analysis and decision-making. We believe that the expense and liability recognition for social insurance benefits that we support would be more consistent with the overall objectives of general purpose financial statements and also provide better information for users to make decisions.

As noted above, we are also concerned about the continued disagreement among various members of the Board on the core issues relating to the proposal as exemplified by the large number of Board members supporting alternative views. Clearly the ED is another compromise

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among Board members on this topic. While such compromises sometimes result in incremental progress, they do not always result in the most sound accounting practices, nor do they provide the most benefit to financial statement users. Assuming the Board decides to move forward on this project without expense and liability recognition and that additional compromises are needed to finalize the standard, we suggest that the Board seriously look at what can ultimately be agreed upon and whether it merits the issuance of a final standard. For example, if after final deliberations, the result of this project would be to issue a final standard that would add only a few additional Management's Discussion and Analysis (MD&A) disclosures, and not much else, we seriously question the benefit that would result from moving forward.

With all of this said, if the Board can agree on certain aspects proposed in the ED, it may result in a worthwhile step forward by the Board with respect to federal accounting and financial reporting for social insurance programs and make at least a modicum of new and useful information available to readers and users of federal government financial statements.

Finally, we understand there are numerous policy issues surrounding federal social insurance programs and their funding. Our purpose in providing this response to the Board is only to provide feedback on what we believe to be the appropriate accounting and financial reporting for these transactions and not to provide any commentary on the underlying policy issues themselves.

As requested by the Board, we considered the questions raised in the ED. However, the Board should keep in mind when reviewing our responses that we recommend liability and expense recognition for social insurance programs. We are responding to the ED questions in the event that the Board does not accept our recommendation to move towards such recognition. Our responses are included in the following section of this letter. We provide several other comments on the ED in the final section of this letter.

Responses to ED Questions

Q1. The Board proposes to require social insurance component entities and the governmentwide entity to discuss and analyze key measures from the basic financial statements in their management's discussion and analysis ("MD&A"). See paragraphs 26–30 in the proposed standard and paragraphs A75—A79 in the basis for conclusions. ***Do you believe that key measures should be presented in the MD&A as described in this exposure draft? Please provide the rationale for your answers.***

Generally, we support showing the key measures and changes in amounts reported for key items in the MD&A as we believe that it will result in an improvement in the understanding of social insurance programs. Paragraphs 26 – 30 go into much detail about what the MD&A should include both for social insurance programs and other more general areas (for example, costs, net position, and key budgetary amounts). We question the need for the proposed social insurance standard to go into so much detail on MD&A requirements, particularly in the areas that are unrelated to social insurance programs. SFFAS 15, *Management's Discussion and Analysis*, is the underlying FASAB standard that dictates the content of MD&A. In our view, based on what SFFAS 15 already requires, much of the social insurance information described in paragraphs 26

– 30 would be and should be disclosed in MD&A. Therefore, we recommend that the final social insurance standard discuss (at a high level) the expectation that under SFFAS 15 requirements, certain social insurance information would be discussed in the MD&A. Several examples could be provided in the final standard and a reference made to SFFAS 15 for more information.

Note that we are also concerned about so much detail being provided in the proposed standard in that it could, in some cases, be viewed as inconsistent with SFFAS 15. Paragraph 10 of the ED states that the proposed social insurance standard "supplements" SFFAS 15. We are unclear on this point and are also concerned that the proposed ED could actually be perceived as changing existing requirements in SFFAS 15. For example, paragraph 3 of SFFAS 15 indicates that MD&A "may" also include forward-looking information about anticipated future events. Statement of Federal Financial Accounting Concepts No. 3, *Management's Discussion and Analysis*, also reiterates that the reporting of anticipated future events should be presented "if feasible and appropriate." However, paragraph 26 states that the MD&A "should" encompass the possible future affects of future events, conditions, and trends. If the Board retains the detailed requirements and guidance in paragraphs 26 – 30, a careful review and comparison between the final standard and SFFAS 15 should be made to ensure that there is consistency.

Finally, if the Board decides to retain so much detail on MD&A requirements in the final standard, we recommend that additional guidance be added to reinforce the concepts already discussed in SFFAS 15 that MD&A be clear and concise as it relates to the requirements discussed in paragraphs 26 – 30. Currently, the Social Security Administration (SSA) and Centers for Medicare and Medicaid Services (CMS) already provide a significant amount of data regarding "changes" within the existing required supplementary information. However, this information is often lengthy and difficult to read. Therefore, a reminder emphasizing that MD&A should be concise and meaningful would be helpful.

Q2. The Board is proposing to add a line for the closed group measure to the balance sheet below assets, liabilities, and net position and not included in the totals for these classifications. See paragraphs 31—32 in the proposed standard and paragraphs A81—A100 in the basis for conclusions. Two members have submitted alternative views on this issue. See paragraphs A139—A142 in the basis for conclusions for Mr. Patton's view. Mr. Patton and other members believe that a liability greater than the due and payable amount should be recognized on the balance sheet. See paragraph A144 in the basis for conclusions for Mr. Werfel's view. Mr. Werfel and other members believe that the closed group measure should not be presented on the balance sheet. ***Do you believe that the balance sheet should present a line item for the closed group measure as described in this exposure draft? Please provide the rationale for your answers.***

As stated in our previous comment letter on the related PV, we believe that these social insurance programs are currently executed and publicized as exchange programs and that there should be expense and liability recognition in the basic financial statements and that the obligating event that gives rise to the liability is when participants begin work in covered employment. With regard to the compromise position taken in the ED of adding a line for the closed group measure to the balance sheet below assets, liabilities, and net position, we do not support it for the following two reasons. First, FASAB concepts do not define a "bottom of the page" addition to the balance sheet as an element of financial statements. Second, as noted earlier, compromises do not always result in sound accounting and financial reporting. Social insurance programs either result in a liability or not. The addition of a number at the bottom of the page does not improve the usability of the balance sheet. Further, placing such a significant number at the bottom of the balance sheet in an undefined area will be confusing. Users will likely wonder why it is not reported as a liability and what the significance is of its placement at the bottom of the page. The Board should not move forward with this proposal. However, if it does, we believe that the measure provided should only be the closed group measure because it is most appropriate for accounting and financial reporting purposes. While the open group measure may be useful for other purposes, it is not appropriate for accounting and financial reporting.

Q3. The Board proposes to add a new summary section of the statement of social insurance ("SOSI") to present the closed and open group measures. See paragraphs 34—35 in the proposed standard and paragraphs A114—A116 in the basis for conclusions. ***Do you believe that the SOSI should have a summary section as described in this exposure draft? Please provide the rationale for your answers.***

We agree with the proposal to require a summary section in the statement of social insurance (SOSI) for both component entities and the governmentwide entity that presents closed and open group measures. Doing so would provide financial statement users with more information which we believe is beneficial. However, as noted in our response to Question 2, we believe open group information is not appropriate for financial reporting. Therefore, we recommend that as the project on sustainability proceeds, information about the open group may possibly be better disclosed as part of that project. Also, we were unclear on one point. Paragraph 35 states that the standard should not be construed to preclude presenting by age cohort. This seems inconsistent with paragraph A114 which states that the "summary section will provide present value information for all age cohorts, with subtotals for the closed and open group measures."

Q4. The Board proposes a new basic financial statement entitled "statement of changes in social insurance amounts." The new statement would explain the changes during the reporting period in the present value amounts for the closed group measure included in the statement of social insurance. See paragraphs 36—37 in the proposed standard and paragraph A116 in the basis for conclusions. Mr. Werfel and other members have an alternative view. They believe the new statement should focus on changes in the open group measure and not the closed group measure. The question of the use of the appropriate measure is addressed in question 7 below. See paragraph A145 in the basis for conclusions. ***Do you believe there should be a new basic financial statement explaining changes to the present value amount included in SOSI? Please provide the rationale for your answers.***

In our view, in the absence of expense and liability recognition, the proposed SCSIA is a highlight of the ED. It provides financial statement users not only *how much*, but even more importantly, *why* and *how* the closed group measure changed from the end of the previous reporting period. Note that we do not agree with the position presented in the Alternative View that this statement only include open group information for the same reason cited in our responses to Questions 2 and 3 (that is, open group information is not appropriate for purposes of accounting and financial reporting).

Q5. The Board proposes to disclose an accrued benefit obligation in notes to the financial statements. This information would include a five year trend when the standard is fully implemented. See paragraph 38 in the proposed standard and paragraphs A117—A123 in the basis for conclusions. Mr. Werfel and other members have an alternative view expressing opposition to this disclosure. See paragraph A146 in the basis for conclusions. ***Do you believe that an accrued benefit obligation should be disclosed as described in this exposure draft? Please provide the rationale for your answers.***

It appears from reviewing paragraph A121 that the accrued benefit obligation being proposed would most closely relate to the Projected Benefit Obligation in private sector pension accounting. If we are correct on our assumption, we would support disclosure of an accrued benefit amount based on our belief that sovereign government financial statements are most useful when they are comparable to accounting in the private sector. However, the final standard could be improved by more clearly describing the nature of the accrued benefit obligation.

Q6. The Board considered but decided not to propose adding a line item to the statement of net cost ("SNC") for the change during the reporting period in the closed group measure that would be presented below exchange revenue and expenses and not included in the totals for these classifications. Some argue that this measure should not be presented on the SNC because it is a fundamentally different measure. Others believe the change is an economic cost that belongs on the SNC, and that including this number at the bottom of the SNC appropriately links all basic financial statements. See paragraphs A101—A113 in the basis for conclusions. ***Do you believe that the SNC should not include a line item for the change during the period in the closed group measure, which would be presented below exchange revenue and expenses and not included in the totals for these classifications? Please provide the rationale for your answers.***

We support liability and expense recognition for social insurance programs. Therefore, for the same reasons cited in our response to Question 2, we would not support adding a line item to the statement of net cost for the change during the period in the closed group measure that would be presented below exchange revenue and expenses and not included in the totals for these classifications.

Q7. The Board decided to present the closed group measure (CGM) (defined in paragraph 19) as a common thread among the proposed new reporting. The proposal requires that the CGM and other key measures from the financial statements be discussed in management's discussion and analysis; that the CGM be presented on the balance sheet below assets, liabilities and net position (without being included in the totals for those categories); and that the changes in the CGM during the reporting period be presented and explained in the new summary section of the statement of social insurance and the new statement of changes in social insurance. The Board considered the open group measure (defined in paragraph 24) instead of the closed group measure as the focus for the disclosure. This exposure draft discusses both the closed group measure and the open group measure throughout. Paragraphs A69-A74 provide the basic rationale for the Board's selection of the closed group measure. Mr. Werfel and other members *have an alternative view regarding the presentation of the closed group measure. They oppose the addition of the closed group measure to the balance sheet. Further, they believe the open group measure is the appropriate measure to use in the new statement of changes in social insurance and not the closed group measure. See paragraph A145 in the basis for conclusions.* ***Do you agree with the Board's decision to feature the closed group measure? Please provide the rationale for your answers.***

As noted in our response to Question 2, we support the Board's decision to feature closed group measure information as a common thread in the proposal. As noted in our response to Question 3, we do support the reporting of open group measures in the proposed summary section in the SOSI but also recommend that the Board consider moving such information as the sustainability project moves forward.

Q8. The Board is proposing to change the requirement currently in SFFAS 17 for specific sensitivity analysis. The standard will require the entity to provide sensitivity analysis of the closed and open group measures appropriate for its particular social insurance program but will not specify a particular approach for the analysis. See paragraphs 42—43 of the standard and paragraphs A125—A137 of the basis for conclusions. ***Do you believe that a general requirement that allows flexibility in the sensitivity analysis presented will produce better information regarding the sensitivity of social insurance programs? Please offer any comments that you wish to make on these provisions.***

We support the flexibility that the Board is proposing with regard to sensitivity analysis because it should provide preparers the ability to improve the sophistication and level of such analysis. However, if the Board moves forward with this proposal, it should monitor implementation of the requirement. If after several years it is found to have led to more confusing or less useful information, the Board should consider changing the requirement to specify a particular approach.

Other Comments on the ED

Transition Guidance. Inasmuch as this ED boils down to additional disclosure, with no changes in measurement and recognition, there are appropriately no transition matters to be addressed. However, it would be helpful if a final standard could at least recommend, not require, comparable disclosures for prior years to the extent that those data can be obtained with cost effectiveness.

Paragraph 18. The definition of the closed group population is not consistently defined throughout the document. Paragraph 2(b) includes a reference to "current" participants which is missing from the definition in paragraph 18.

Paragraph 26. See our response to Question 1 regarding concerns that we have with this paragraph being inconsistent with SFFAS 15. Additionally, this paragraph states that the discussion in MD&A should go beyond a mere description of existing conditions to include possible future effects of those factors and that it should also encompass the possible future effects of anticipated future events, conditions, and trends, including quantitative forecasts or projections. We realize that proposed requirement is consistent with an option provided in SFFAS 15 to provide future information. However, we urge the Board in its final standard to temper its proposal by noting the need for reporting entities to ground their discussion and analysis of future events, conditions, and trends by relying on observable (and auditable) data to the extent possible, and to use forecasts and predictions generated by independent and unbiased individuals and/or organizations. Although auditors provide only limited assurance on the MD&A, they would have great difficulty in doing so if the MD&A in question did not generate its forward-looking information using objective and reliable criteria that could be measured and evaluated by an external auditor.

Paragraphs 28 and 29. If the Board does not accept our recommendation to reduce the information included in the final standard relating to MD&A (see our response to Question 1), then we suggest that FASAB should be more definitive regarding the disclosures that it seeks in paragraphs 28 and 29. These paragraphs seem very permissive and use the word “may” many times. This may result in an inconsistency in practice.

Paragraph 37. This paragraph states that the SCSIA should present significant components of the change in social insurance amounts and cites interest on the obligation due as an example. In nearly all instances, the federal government does not pay interest on benefit obligations due. As such the inclusion of “interest due” in this paragraph is misleading and could result in confusion by the users of the standard.

Paragraph 40. This paragraph states that projections should be adjusted if policy reforms are enacted or other major factors change after the valuation date, *if feasible*. The use of the phrase “*if feasible”* is problematic. Generally accepted accounting principles generally require entities to value estimates as accurately as possible as of the valuation date. If information comes to the attention of preparers which impacts the valuation after the valuation date, the “feasibility” of not using it to adjust projections should not be an option. Retaining this language will also be problematic from an audit perspective particularly if preparers assert that adjusting a projection is not feasible and their auditors disagree.

Paragraph 46. We believe that the proposed effective date beginning after September 30, 2009, may be too soon. Upon issuance of a final standard, agencies should be provided at least one full year prior to the measurement date used by SSA and CMS (i.e., January 1). The Trustees Reports for 2009 (the information from which SSA and CMS derive their social insurance data) will be released in April. This standard would have to be released in final form well in advance of the time period used by the agencies to prepare the Trustees Report for the proposed effective date to be workable. The Board should reevaluate the effective date once a realistic issuance date is known.

Appendix B. In Appendix B, the columns run, left to right, from the earliest year to the most recent year. In the pro forma statements in Appendixes C and D, the columns run from most recent to latest. Appendix B would be easier to use if it conformed to Appendixes C and D.

Appendix D. In Appendix D, there are sets of highlighted column headings reading “Federal Hospital Insurance,” followed by the Medicare Part letter. We believe that only Part A is hospital insurance and that Part B is medical insurance and Part D is drug insurance. If we are correct, this distinction should be clarified.

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The AICPA appreciates the opportunity to comment on the ED. This comment letter was prepared by AICPA members with experience in federal auditing and accounting matters and was reviewed by representatives of the Accounting Standards Executive Committee (AcSEC) who did not object to its issuance. Representatives of the AICPA would be pleased to discuss these comments with you at your convenience.

Sincerely,

Peter Knutson
Chairman
FASAB Social Insurance Task Force

Mary M. Foelster
Director
Governmental Auditing and Accounting

cc: FASAB Social Insurance Task Force
Jay Hanson
Daniel J. Noll