>>> "Sopper, Dale " <Dale.Sopper@ssa.gov> 4/16/2007 4:02 PM >>>
NOTE TO WENDY COMES

Wendy,

Attached are SSA's comments on the Preliminary Views document on Accounting for Social Insurance. Thank you for the opportunity to comment.

Dale Sopper

Accounting for Social Insurance
Preliminary Views Document

1. *Which obligating event do you believe creates a liability and expense that should be recognized?*

   Recognizing and measuring liabilities and expenses for social insurance programs should occur when all eligibility criteria are met and the benefits become due and payable. Future scheduled benefits are not current obligations but rather are intended to provide recipients with resources in specific time periods and are properly regarded as expenses of those time periods. These scheduled future benefits do not represent a fixed legal contractual obligation - Congress can change the law at any time and the government would not be bound to make a payment - and therefore should not be classified as a liability until amounts are due and payable.

   Another consideration for social insurance payments is the existence of a non-exchange transaction. We believe there should continue to be a fundamental distinction in the reporting of exchange and non-exchange transactions. Benefit payments are not directly tied to the taxes paid and are not considered exchange transactions. Because benefits are classified as non-exchange transactions, the event that creates an obligation must be when the benefits actually become due and payable. Therefore we strongly believe that because of the nature of social insurance obligations, only benefits due and payable should be recognized as a liability. This is consistent with the nature of the financing of, and the obligation to provide, scheduled benefits on a pay as you go basis.

2. *Do you believe that Social Security and Medicare obligations are measurable for purposes of recording a liability after 40 quarters or equivalent of work in covered employment as proposed in the Primary Views (see paragraphs 16-18 and especially subparagraph 16g in the standard; also see A54-S55 in basis for conclusions.*

   Using 40Quarters of Coverage (QC) as the obligating event still warrants a heavy reliance on complex and uncertain numbers. These programs have unique benefits, different eligibility requirements, and different financing arrangements. Present values and other long range estimates are inherently uncertain, particularly for estimates based on current law since future changes to law could alter future benefits.

   Even at 40QC, there are still many things that could change in the future and could affect the existence of a liability (demographic assumptions, changes in valuation period, economic assumptions and legislation).

The government is not bound to make payment until all criteria for program eligibility are met and therefore the only valid liability measure for Social Security and Medicare is the amount of the payments at the time when they are due and payable.

3. *The primary view proposes to change the SOSI by (1) adding line items tying to (or articulating with) the revised expense and liability amounts reported on the SNC and BS; and (2) adding a new section to the SOSI that would explain the changes in the SOSI amounts from the beginning to the end of the reporting period. (Paragraph 16 and Appendix B for illustration).*

   The Alternative View proposes to leave the SOSI unchanged but to add a new principle financial statement entitled "statement of changes in social insurance" which could be combined with the SOSI. The new statement would provide an explanation for changes to the present value amount included in the statement of social insurance.

   Do you believe that the Primary View proposal to add line items to the SOSI that tie to revised expense and liability amounts reported on the statement of net cost and the balance sheet, respectively, should be adopted?

   No, the primary view proposal to add line items to the SOSI that tie revised expenses and liabilities amounts to the Balance Sheet and Statement of Net Cost should not be adopted. Recording social insurance obligations as liabilities on the balance sheet would not be an accurate depiction of the Federal Government's financial position. Since social insurance obligations do not meet the definition of a liability, showing these amounts on the balance sheet would be misleading to the users of financial reports. Social insurance information is financial information based on actuarial projections extending far into the future, and thus are subject to a high degree of uncertainty. To record these as liabilities on the balance sheet could compromise the integrity of the statements. The degree of precision and certainty of amounts reported on financial statements could be potentially misunderstood. We believe that these estimates are useful to analyze the financial outlook of social insurance programs but would be misrepresented as liabilities on the balance sheet.

   Finally, the projections for future benefits payable can be found in a variety of documents and reports throughout the government (SOSI, Trustees Reports). These documents provide the forum for further explanation and analysis of program sustainability, which is critical to providing useful information to users of this information. To simply put such large numbers on the balance sheet and statement of net cost without further analysis is not appropriate and could lead to a highly questionable interpretation about the financial condition of the US Government.

Do you believe that the reasons for changes in SOSI amounts during the reporting period should be reported and, if so, do you favor such reporting (1) as proposed by the Primary View (2) as proposed by the alternative view or (3) some other approach?

We believe it is important to highlight the changes in social insurance amounts during the reporting period and we are in favor of the alternative view's position of developing a Statement of Changes in Social Insurance. This new statement would better serve the Stewardship objective in SFFAC 1, "*Assessing the impact on the country of the government's operations and investments for the period, and how, as a result, the governments and the nation's financial condition has changed and may change in the future*".

4. *The Alternative View proposes that a statement of fiscal sustainability be presented in the consolidated Financial Report of the United States Government. The statement would provide sustainability information on the entire Government, including information on intergenerational equity (See paragraphs 43 in the standard and A163 in the basis for conclusions for a discussion of the proposal and Appendix C for an illustration). Do you believe the proposal should be adopted?*

   We agree that a Statement of Fiscal Sustainability should be developed. This reporting would enable users to better assess the government's ability to fund programs in the future, the extent of the government's responsibilities for these programs and the government's ability to adjust these responsibilities. Sustainability is a matter that is in the forefront of government and the public's concerns. Providing sustainability information with proper explanations will assist users in understanding the measures of sustainability, the assumptions used to determine the financial implications and the future outlook of the programs. This is important in fulfilling the Stewardship Objective of SFFAC 1.

   The specific table presented in the Alternative Views to address the "Statement of Fiscal Sustainability" provides useful information that has some bearing on sustainability. In particular the values for the 75 year period are relevant, but far from complete. The values for infinite period are not useful in this context and should be deleted. While the financial adequacy of revenue for the next 75 years as a whole is useful, sustainability is more a question of whether the level of cost and adequacy of financing are being maintained through time on a sustainable trend. Trends in cost levels and financial adequacy can only be assessed by considering annual projections. An assessment of sustainability should be principally focused on the trend in annual cost of the program relative to the appropriate tax base or source of financing (Gross Domestic Product) and the trend in trust fund levels relative to annual program cost. The concept of 'sustainable solvency' used by the trustees would serve as an excellent measure.

5. *Do you believe the Board should consider recognizing deferred revenue for earmarked revenues in excess of related program costs?*

   We believe that any further research into the merits of recognizing deferred revenue for earmarked revenues in excess of benefit payments may be beneficial. However, we do believe that this should be done as a separate project.

6. *The Primary and Alternative Views include detailed guidance on measurement (including selection of assumptions), display, disclosure and required supplementary information (paragraphs 15-37 Primary view; 64-84 Alternative view). Please make any comments that you wish on both views.*

   SSA believes that the treatment of social insurance information is of primary importance to the government's stewardship responsibilities to the American public. While we recognize the importance of communicating the financial condition of the Federal Government, recording social insurance obligations as liabilities on the balance sheet would not be an accurate depiction of the Federal Government's financial position.

   We strongly disagree with the Primary View position of adding line items to the Balance Sheet and Statement of Net Cost. Emphasizing a new and different liability calculation in financial statements would create confusion. Besides, the balance sheet is a snapshot of an entity's financial status at a certain point in time and shows what a government owes as a result of past operations, which would include only liabilities that are present obligations of the Government. The Statement of Net Cost should reflect the principle of matching costs of government operations during a particular year with services provided by the government during that year. Showing expenses for future scheduled benefits would not match this principle. Therefore, recording amounts for <u>future</u> social insurance benefits that are subject to a wide degree of uncertainty compromises the integrity of the financial statements. It is questionable whether adequate information concerning social insurance could be presented by means of a single, point in time number on a balance sheet or statement of net cost.

   Social insurance information displayed in government financial statements should be consistent with the information presented in the annual Trustees Report, SOSI and individual benefit statements provided by SSA. Therefore we believe a Statement of Changes in Social Insurance would better serve the objective of consistency in financial reporting.

   There are several reasons that due and payable is the only supportable and viable option for recording social insurance obligations: social insurance obligations are not present obligations of the government and are non-exchange transactions; future payments are uncertain due to the power of Congress to change current law; and determining the present value of future benefit payments involves estimates and is subject to a high degree of uncertainty.