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ARTHUR
ANDERSEN
& CO.

*Sound Financial Reporting
In the U.S. Government*

A Prerequisite to Fiscal Responsibility



Preface

In 1975, Arthur Andersen & Co. prepared the first set of consolidated financial statements for the U.S. Government in accordance with generally accepted accounting principles (GAAP) and included them in a booklet that was distributed in the public interest. We reported that the U.S. Government was then incurring a deficit substantially larger than what was reflected by the cash basis of accounting and that the U.S. Government had an accumulated deficit of \$814 billion, considerably greater than the \$344 billion national debt. In the intervening decade, the U.S. Government has incurred ten consecutive annual cash-basis and GAAP-basis deficits that have increased the national debt to \$1.3 trillion and the accumulated GAAP-basis deficit at September 30, 1984, to \$3.8 trillion.

For the past ten years, the U.S. Treasury, using the financial statements Arthur Andersen & Co. developed as a guide in 1975, has prepared GAAP-basis prototype financial statements for the U.S. Government. These statements are not usually released until a year after the September 30 fiscal yearend, and no program yet exists to disseminate them widely or to explain them to the American people.

As independent public accountants and consultants to business and government, we have seen how a lack of accountability caused by inadequate information and the failure to account properly for the full cost of Government programs can help produce a fiscal crisis.

Many state and local governments, including those which have experienced fiscal crises since 1975, have adopted GAAP-basis reporting. The U.S. Government, as part of the program to solve the budget crisis, should use GAAP-basis accounting in its management and reporting to the public.

This booklet compares current GAAP-basis financial statements for the U.S. Government with those we prepared a decade ago, and it describes a number of critical issues that political leaders and concerned citizens need to consider.

A democratic system derives its greatest strength from informed citizens free to express their views. That strength depends upon providing citizens timely and accurate information. //

ARTHUR ANDERSEN & CO.

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Summary Observations

The national debate over the disposition of U.S. Government deficits is narrowly focused on cash deficits without reference to financial statements that reflect the Government's financial condition and the real cost of programs. We believe that a proper assessment of the Government's fiscal problems should start with analysis of its financial condition and the cost of its existing programs.

The U.S. Government requires publicly held companies to prepare financial statements in accordance with generally accepted accounting principles (GAAP), which recognizes all economic events as they occur. Similarly, Congress recently compelled state and larger local governments to report whether they prepare their financial statements according to GAAP.

Yet the U.S. Government continues to ignore GAAP and instead uses obligation-oriented, cash-basis accounting in its budgeting and related reports to the public. This hides the costs of current programs, and results in misinformation and misunderstanding. Cash-basis accounting can lead to misallocation of national resources, jeopardize sound programs and burden future taxpayers. Sound financial management will require a commitment to a series of reforms:

- ☐ Adoption of financial reports in accordance with GAAP as the official financial statements of the U.S. Government.
- ☐ Preparation of the Annual Budget on a GAAP basis.
- ☐ Design and installation of accounting systems to support improved reporting and budgeting.
- ☐ Annual audit of the U.S. Government's financial statements by the U.S. General Accounting Office.
- ☐ Concentration of central financial reporting functions in a single agency.

While each of these reforms is important, this booklet focuses on the need for GAAP-basis financial reporting as a *prerequisite* to meaningful reform and fiscal responsibility. Sound financial reporting will help the U.S. Government to realize significant benefits in the management of its affairs:

- ☐ Improved accountability of elected officials.
- ☐ More informed decision-making.
- ☐ Avoidance of crises.
- ☐ Better measurement of performance.

Improving public confidence in Government is vital if Government officials expect the public to provide adequate resources to meet the needs of society. Effective management of the public sector has become a central issue of our time. It is not simply a matter of dollars, but of whether a nation of 240 million free people can govern themselves effectively.

Observations Concerning U.S. Government Financial Reporting Practices

U.S. Government Doesn't Follow Financial Reforms It Imposes on Others

In 1975, Arthur Andersen & Co. noted that governments at every level faced fiscal crises unless they improved their financial management and reporting practices. Shortly thereafter, New York City and several other large local governments experienced well-publicized fiscal problems. In return for its financial assistance, the U.S. Government directed New York City to undertake a number of reforms, including adoption of GAAP for financial reporting and budgetary purposes and annual financial audits. Subsequently, Congress made it mandatory for all recipients of federal financial assistance to submit audited financial statements, preferably prepared on a GAAP basis. The U.S. Government, now facing a budget crisis of its own, has yet to implement the reforms it imposed upon New York City, and other state and local governments.

Financial Management Functions Are Fragmented

At present, the U.S. Treasury compiles data and reports the status of funds and certain other accounting statistics, and, since 1975, has prepared prototype consolidated financial statements. The General Accounting Office establishes the standards for accounting principles and the design of accounting systems for U.S. Government agencies. The Office of Management and Budget has responsibility for budget policy and procedures. The Joint Financial Management Improvement Program, representing the above organizations and others as well, has the objective of improving financial management practices. While the Government has made progress

toward better financial management during this decade, fragmentation of financial management functions has hindered development of a government-wide financial reporting system.

Accrual Accounting Is Required by Existing Law

Both Hoover Commissions recommended accrual accounting for the U.S. Government. In 1950, this led to passage of legislation — supplemented by related Treasury regulations — that requires U.S. Government agencies to prepare GAAP-basis financial reports like those required of business. Succeeding Administrations and Congresses have largely ignored these laws and regulations. However, recent actions by GAO (in its revised Title II) and OMB (in its Circulars A-123 and A-127) may result in greater compliance with the 1950 legislation.

No Requirement to Publish Financial Statements Exists

Current law does not require the U.S. Government to disseminate financial statements to the public. For over 200 years, the Government has attempted to incorporate the concept of accountability into the Constitutional system of checks and balances. A missing link in this system is a comprehensive report on the financial position and results of operations prepared in accordance with generally accepted accounting principles.

Costs and Value for Money Are Not Reported to the Public

Citizens should be concerned about whether their Government can continue the current level of services without raising taxes, whether the Government's capital will be sufficient for the future, and whether Government renders its services efficiently and effectively. The current system neither reports costs nor provides other information that citizens need to determine whether they have received value for their money.

Programs Are Adopted Without Adequate Consideration of Costs

Currently, the U.S. Government essentially budgets on an obligation-oriented cash basis of accounting. Budgeting program costs on a GAAP basis would identify all program costs. Used with projected performance data, this

would enable a more valid evaluation of costs and expected benefits to be made before programs are adopted.

Accountability Is Needed

Cash-basis financial reporting and budgeting allows elected officials to adopt programs which provide benefits currently without providing the funding until later years. GAAP-basis financial reporting and budgeting would promote accountability of elected officials because expenses under GAAP are recorded when liabilities are incurred, not simply when cash payments are made.

A Proper Definition of "Balanced Budget" Is Needed

Many have advocated a "balanced budget amendment" as a solution to the deficit crisis, but the proper definition of "balanced budget" remains an open question. It could be counterproductive to adopt a Constitutional amendment without an appropriate definition.

Observations Concerning U.S. Government Financial Position and Operations

Introduction

This section highlights certain significant points that emerge from considering the accompanying Consolidated Financial Statements, particularly those items where GAAP-basis accounting portrays information differently from the cash basis. A subsequent section refers to certain of these items, explaining the benefits of sound financial reporting.

There Has Been a Decade of Persistent Deficits

GAAP-basis deficits were a fairly constant percentage of GNP from 1975 to 1984, whereas cash-basis deficits as a percentage of GNP fluctuated more widely during this period. The high level of cash-basis deficit for 1984 occurred during a period of relatively strong performance of the U.S. economy, whereas the 1975 and 1976 deficits occurred during recession years. The table below presents a comparison of GAAP-basis and cash-basis annual deficits in nominal and 1984 dollars.

Deficits Are Significant in Relation to Savings

The accumulated GAAP-basis deficit of \$3.8 trillion as of September 30, 1984, compares with the \$2.0 trillion aggregate market value of securities listed on the New York and American Stock Exchanges, and on the over-the-counter market on that date. The cash-basis deficit for 1984 as a percentage of GNP approximated the nation's personal savings rate. Financing the deficit consumed two-thirds of the total assets added to the savings pool by individuals and businesses.

Accumulated Deficit Excludes Certain Unfunded Liabilities

The GAAP-basis deficit reflects only a portion of the unfunded liability for Social Security, which is being amortized for financial reporting purposes over 30 years. The present value of the unamortized portion of the benefits which

(\$ Billions)	Cash Basis Annual Deficit			GAAP Basis Annual Deficit		
	Nominal \$	% GNP	1984 \$	Nominal \$	% GNP	1984 \$
1974	\$ 6.1	0.4%	\$ 12.2	\$ 95.1	6.9%	\$190.4
1975	53.2	3.6	97.7	152.1	10.3	279.4
1976	73.7	4.5	126.4	188.8	11.5	323.7
1977	53.6	2.9	85.9	224.6	12.1	359.8
1978	59.0	2.8	88.4	215.8	10.3	323.2
1979	40.2	1.7	55.5	256.8	10.9	354.9
1980	73.8	2.9	93.5	322.2	12.5	408.3
1981	78.9	2.7	91.3	264.7	9.2	306.3
1982	127.9	4.2	138.5	314.0	10.3	339.9
1983	207.8	6.4	215.6	395.3	12.3	410.1
1984	185.3	5.2	185.3	333.4	9.3	333.4

current and future beneficiaries are promised under current law, would, if added to the accumulated deficit, increase the accumulated deficit from \$3.8 trillion to \$6.1 trillion.

Annual Deficit Exceeds Individual Income Taxes

The GAAP-basis deficit for the 1984 fiscal year exceeded total revenue from individual income taxes, the largest single source of Government revenue. Thus, if no other deficit-reduction actions had occurred, a 113% increase in individual income taxes would have been needed to balance the budget, assuming that such an increase had no depressive effect on the economy. Even on a cash basis, a 63% increase in individual income taxes would have been needed.

Liabilities for Pension Plans and Social Security Exceed National Debt

There is considerable attention given by the public to the national debt, which, after excluding \$0.3 trillion held by Government trust funds, was \$1.3 trillion as of September 30, 1984. However, the liabilities for various military and civilian retirement plans, and for Social Security, including the unamortized amount of the unfunded liability, aggregated \$5.5 trillion as of September 30, 1984.

Social Security Costs Have Changed Dramatically

Beginning in 1975, beneficiaries received an automatic adjustment to compensate for inflation. Because Social Security taxes are based on wages, the "stagflation" years of the late 1970s created the anomaly of benefits increasing much faster than tax revenues. In 1977, Congress took action to restrain uncontrolled benefit

increases and substantially increased taxes in an attempt to restore fiscal soundness. It was necessary for Congress again to take similar action in 1983. Despite these reductions in benefits and increased taxes, the unfunded liability for Social Security increased from \$2.5 trillion as of September 30, 1974, to \$4.2 trillion as of September 30, 1984. The impact of the "stagflation" years is clearly shown in the GAAP-basis deficits as a percent of GNP, while the cash-basis data hide this.

Social Security Taxes Are Scheduled to Rise

The unfunded liability for Social Security of \$4.2 trillion assumes an increase in the combined employee and employer tax rate from 14.0% in 1984 to 15.3% in 1990; the taxable wage base increases from \$37,800 in 1984 to an estimated \$46,800 in 1990 (if 1986-1990 increases are the same as 1984-85). Thus, these tax increases already legislated will not be available to otherwise reduce the deficit.

Medicare Outlays Have Grown Dramatically

Outlays under Medicare increased from \$11 billion in 1974 to \$63 billion in 1984, and are expected to increase further as the population ages. No accrual for future commitments, however, has been made for the unfunded liability.

Trends in National Defense Costs Are Illuminated Under GAAP

Outlays for defense grew in real terms from 1974 to 1984 by 43%, compared with 20% on a GAAP basis. Defense costs on a GAAP basis relative to GNP declined during the decade.

The following table shows that pension costs were a greater factor in the growth of defense costs than the increase in both operating expenses and depreciation of hardware.

National Defense Commitments

Augur Cost Increases

Recent weapons systems commitments, together with the cost of operating them, will result in an increase in future defense costs. As in the case of entitlements, these commitments limit the Government's flexibility in the budget process.

Interest Expense Is of Growing Importance

In constant dollars, interest expense constituted the largest single growth category during the decade through 1984, accelerating from 5.5% of total expenses on a GAAP basis in 1974 (8.0% on a cash basis) to 11.0% in 1984 (13.0% on a cash basis). When interest expense represents such a high proportion of the budget and interest rates are often volatile, budget plans can go awry.

Entitlement Programs Pose a Special Problem

Similarly, expenditures mandated under individual entitlement and retirement programs

have become an increasing portion of the budget, and were 54% of the GAAP-basis expenses in 1984 (47% on a cash basis). Together with interest, these "noncontrollable" costs have complicated the budgetary process because they are difficult to contain and can vary significantly from estimates.

Major Portion of U.S. Debt Is Short-Term

Debt management has become a major Treasury effort. Of the \$1.3 trillion of debt held by the public at September 30, 1984, \$520 billion was refinanced in 1985, in addition to the approximately \$200 billion of net new debt to finance the 1985 deficit. The new debt represented approximately 25% of such U.S. credit market activity in 1985.

Foreign Holdings of U.S. Government Debt Are Significant

As of September 30, 1974, 16.5% of the debt was held directly by non-U.S. interests and, as of September 30, 1984, 13.5% was held directly by non-U.S. interests. During 1984, non-U.S. interests financed 8.4% of the annual cash-basis deficit. Foreign inflows to U.S. financial markets in recent years have also indirectly supported the financing of U.S. Government deficits.

	1984		1974 (\$ Billions)		
	\$ Billions	% of GNP	1984 Dollars	Nominal Dollars	% of GNP
Cash-basis defense outlays	\$227.4	6.35%	\$158.9	\$79.3	5.75%
GAAP-basis defense costs:					
Operating expense, before depreciation and pension costs	\$143.3	4.00%	\$130.6	\$65.1	4.72%
Depreciation of weapons and other plant and equipment	27.2	0.76	22.2	11.1	0.80
Total before pension costs	\$170.5	4.76%	\$152.8	\$76.2	5.52%
Pensions	48.3	1.35	29.0	14.5	1.05
Total defense costs	\$218.8	6.11%	\$181.8	\$90.7	6.57%

Benefits of Sound Financial Reporting

Improved Accountability

Given the existing practice of cash-basis budgeting and reporting, programs can be adopted and promises can be made without knowledge of their full cost. This lack of accountability creates an incentive for elected officials to curry favor with today's voters at the expense of tomorrow's taxpayers. This lack of accountability has long been a root cause of fiscal mismanagement within the U.S. Government. In fact, excluding interest expense, nearly all growth in Government spending *as a percentage of GNP* since World War II is related to programs that involve *promises to make future payments*.

GAAP improves accountability because GAAP recognizes costs when they occur. Among other benefits of GAAP, it is superior to cash-basis accounting because it provides for:

- **Accrual of pensions and Social Security costs** for the current period according to a sound actuarial method.
- **Capitalization of expenditures for long-term assets**, e.g., major weapons systems and the national infrastructure, and spreading their cost through depreciation charges over the future years that the assets are in service. This would facilitate public debate over program costs and would require accountability on a continuing basis for the remaining useful lives of those assets.
- **Consolidated reporting**, which would eliminate much confusion about the scope of the U.S. Government's operations and its related debt.
- **Economic substance over form**, which would require any measure to resolve the deficit problem to be genuine, not meaningless number juggling. For instance, sales of U.S. Government assets do *not* impact the GAAP-basis deficit if those assets are sold for their carrying amount. Various techniques to

postpone payment of incurred costs similarly fail to reduce the GAAP-basis deficit.

A persistent failure of accountability can undermine the public's confidence in their leaders. Sound financial reporting will contribute to confidence in governance, and provide a vehicle for fair, objective reporting on government activities. Therefore, responsible elected officials must provide the leadership necessary to improve accountability.

Informed Decision-Making

The focus of public debate is now on the cash-basis deficit. With GAAP-basis financial statements, the debate might be broadened to include the significance of the U.S. Government's accrued obligations and the generators of extraordinary cost growth. Had GAAP-basis reporting and budgeting been in effect over the years, Government officials would have better understood the consequences of their actions. It is equally important that the citizenry be in a position to understand the consequence of actions taken by elected officials. Following are a few examples of how GAAP-basis reporting would provide better information:

- **Pensions and Social Security**, and other obligations, are not fully reflected in the cash-basis deficit of \$185 billion for fiscal 1984. When these obligations are considered, the GAAP-basis deficit for 1984 totals \$333 billion. This amount exceeded all personal savings of the American people in 1984.
- **National Defense** programs, measured on a GAAP basis, are growing at a lower rate than is shown by cash-basis accounting. The fact that costs are growing more slowly than actual cash outlays can be explained by capitalization of newly procured equipment that will be depreciated over the periods it is in service; capitalization would require DOD to review annually its capital assets

and to write down those which have declined in utility. Defense costs on a GAAP basis are also affected by higher accruals for pensions that are not yet reflected in cash outlays.

- **National Debt** as typically referred to in the media actually includes substantial amounts of debt held by various U.S. Government Trust Funds. Moreover, the net debt of \$1.3 trillion held by the public is largely offset by assets owned by the U.S. Government, but the total of other obligations — mostly the present value of the future payments (net of related program revenues) to program beneficiaries — greatly exceeds the debt held by the public, and results in an accumulated deficit of \$3.8 trillion as of September 30, 1984.
- **Trust Funds** for program beneficiaries generally purchase U.S. Government debt and do not set aside adequate resources to assure future payments. Payment of the unfunded liabilities for Social Security assumes future payroll tax increases as well as increases in real wages and reduced unemployment levels. Failure of these assumptions to materialize would create pressures for still higher tax rates or unplanned cuts in benefits.

Citizens should recognize that the accumulated GAAP-basis deficit of the Government represents a claim upon the future standard of living of the American people.

Avoidance of Crises

Many elected officials apparently believe that an organization whose budgets provide sufficient cash receipts to cover cash disbursements will never get into financial difficulty. But, while every organization must indeed manage its cash flow in a way that assures liquidity, it must also manage its costs and commitments. Organizations managed on a cash basis tend to defer payments and accelerate receipts, whereas management on a GAAP basis provides for all costs and recognizes revenues only when earned. GAAP reduces the chance that an unforeseen crisis will arise.

Many programs involve promises to pay benefits many years into the future. In many of these programs actual costs have risen much higher than anticipated. A few major examples:

- **Social Security** is being funded on a pay-as-you-go basis. The unfunded liability for

Social Security was \$4.2 trillion as of September 30, 1984. This liability exists even though scheduled tax-rate and taxable-wage-base increases through 1990 and beyond, and projected growth in real wages, were considered in the actuarial calculations.

- **Medicare** is being funded on a pay-as-you-go basis, and no accrual for future commitments has been made in the financial statements. Outlays have risen from \$11 billion in 1974 to \$63 billion in 1984. Because of the aging population, demand for services under this program is expected to increase.

Information to avoid crisis goes beyond management of cash flow, but bears on the financial strength of a nation and its ability to respond forcefully to short-term problems and long-term threats to the viability of the nation. GAAP-basis financial statements can provide useful information to help determine whether a nation is jeopardizing its future.

Performance Measurement

People generally work more effectively when their performance is measured and rewarded. And because they tend to concentrate their efforts on those things that have high value in the measurement process, any organization that wants to be effective must develop a way to measure performance of both management and workers. This measurement process can best be accomplished by integrating systems that capture output with the organization's financial reporting systems.

Performance measurement usually involves a comparison of costs and benefits. In order to develop a sound performance measurement system, an organization must maintain GAAP-basis cost data rather than rely exclusively on potentially misleading cash-basis data.

Although many Government agencies maintain information systems to measure their performance, there is a need to develop Governmentwide standards of measurement and systems that integrate performance reporting with Governmentwide financial reporting and budgeting systems. Such systems would bring about higher productivity, contribute to greater understanding of Government operations by both officials and private citizens, and, perhaps most important, foster more confidence in the Government.

Critical Issues

Sound financial reporting is essential for informed decision-making. GAAP-basis reports and budgets would not only improve understanding of financial transactions, but would also help to identify and illuminate emerging issues. GAAP-basis reporting would contribute to broader discussion of current issues such as:

- **Whether the nation's capital is being consumed.** Do people who expect to receive substantial retirement benefits from the U.S. Government reduce their personal savings and thereby contribute to the nation's low personal savings rate? The U.S. Government's GAAP-basis accumulated deficit of \$3.8 trillion at September 30, 1984, breaks down to \$16,000 per capita and \$44,500 per household. If the entire unfunded liability for Social Security obligations were recorded, the accumulated deficit would be \$2.3 trillion higher, and the deficit per capita and per

household would rise to \$25,700 and \$71,400, respectively.

- **Whether the ability to moderate recessions has been eroded.** For many years the U.S. Government has followed a practice of attempting to moderate the effects of recession by adopting a stimulative fiscal policy. Given the present level of liabilities shown by the GAAP-basis financial statements, will the U.S. Government's traditional approach be able to moderate future recessions?
- **Whether growth in interest expense and entitlements threatens the U.S. Government's ability to effectively manage the budget.** In 1984, 60% of cash outlays were dedicated to interest expense and various entitlement programs. They may grow to an even greater share of the budget since the corresponding GAAP-basis percentage was 65% in 1984 and GAAP-basis financial statements serve as an indicator of future outlays.

Recommendations

Establish Sound Financial Reporting as a Priority	The President and Congress should establish a goal to achieve sound financial reporting for the United States before 1990.
Publish Annual Report	Each year, the U.S. Government should publish an annual report that includes consolidated financial statements prepared on an accrual basis in accordance with GAAP.
Widely Distribute Timely Annual Report	The U.S. Government should establish a goal of publishing the annual report within 90 days of its fiscal yearend and distribute it widely to the public.
Audit Financial Statements	Financial statements included in the U.S. annual report should be audited by the U.S. General Accounting Office.
Develop Performance Measures	The U.S. Government should develop relevant performance indicators for major programs and include such information in the annual report to help citizens evaluate the Government's success in achieving value for money.
Use GAAP for Management Purposes	OMB should prepare the annual budget on a GAAP basis and include a GAAP-basis forecast of the following four years to show the impact of policy recommendations contained in the President's budget. This information would be in addition to the cash-basis budget and forecast presently prepared.
Establish Central Financial Reporting Function	Legislation should be adopted to centralize the financial reporting function within a single agency. That agency would be responsible for implementing accounting policies and reporting standards, designing and installing accounting systems, preparing financial statements, and publishing the annual report. Other governmental agencies would provide consolidated information to the central reporting agency.

United States Government Illustrative Consolidated Financial Statements September 30, 1984, and June 30, 1974

The accompanying consolidated financial statements have not been audited and, accordingly, Arthur Andersen & Co. does not express an opinion on them. Although these financial statements are not complete and accurate in all respects, they do provide background for discussion of the issues involved.

The 1984 financial data are taken from a publication of the Financial Management Service — U.S. Department of the Treasury, *Consolidated Financial Statements of the United States Government — Fiscal Year 1984-Prototype*, available through the U.S. Government Printing Office. Certain reclassifications have been made to the published financial data, including the reclassification to the statement of operations of the direct charge to the accumulated deficit of the provision for accrued non-cash Social Security costs as described in Note 11.

The 1974 data are drawn from a 1975 publication, by Arthur Andersen & Co., *Sound Financial Reporting in the Public Sector — A Prerequisite to Fiscal Responsibility*. Because certain accounting principles have evolved since publication of the 1975 study, a number of reclassifications and adjustments have been made to the 1974 data. These adjustments are not material to the financial statements.

United States Government
Consolidated Balance Sheets (Unaudited)
September 30, 1984, and June 30, 1974

(\$ Billions)

Assets:	1984	1974
Cash and Monetary Reserves (Note 2)	\$ 72.8	\$ 29.6
Receivables, net of allowances:		
Accounts receivable	31.9	5.5
Taxes receivable (Note 3)	30.2	15.0
Loans receivable (Note 4)	229.1	64.5
	<u>291.2</u>	<u>85.0</u>
Inventories, at cost (Note 5):		
Military and other supplies	53.8	28.0
Materials and supplies for government use	81.1	11.1
Stockpiled materials and commodities	16.5	11.5
	<u>151.4</u>	<u>50.6</u>
Property and Equipment, at cost:		
Land (Note 6)	10.3	6.6
Buildings, structures, and facilities (Note 7)	137.0	88.5
Military hardware (Note 8)	330.2	119.9
Equipment (Note 8)	88.6	39.7
Construction in progress	37.5	19.3
Leasehold improvements and other	8.0	2.1
	<u>611.6</u>	<u>276.1</u>
Accumulated depreciation (Note 9)	(299.5)	(128.9)
	<u>312.1</u>	<u>147.2</u>
Deferred Charges and Other Assets	109.8	15.0
Total	<u>\$937.3</u>	<u>\$327.4</u>

The accompanying notes are an integral part of these balance sheets.

Liabilities and Deficit:	<u>1984</u>	<u>1974</u>
Accounts Payable	\$ 161.5	\$ 43.7
Unearned Revenue	31.8	6.7
Borrowing from the Public (Note 10)	1,299.5	343.6
Accrued Pension, Retirement and Disability Plans (Note 11):		
Military personnel	476.1	80.4
Civilian employees	542.7	108.0
Veterans' compensation	221.8	111.0
Other	29.4	—
	<u>1,270.0</u>	<u>299.4</u>
Accrued Social Security (Note 11)	1,911.8	416.0
Contingent Liabilities for Guarantee and Insurance Programs (Note 12)	3.5	—
Other Liabilities	<u>58.5</u>	<u>31.6</u>
Total Liabilities	<u>4,736.6</u>	<u>1,141.0</u>
Accumulated Deficit:		
Balance, beginning of period	(3,465.9)	(718.5)
Current period deficit	<u>(333.4)</u>	<u>(95.1)</u>
Balance, end of period	<u>(3,799.3)</u>	<u>(813.6)</u>
Total	<u>\$ 937.3</u>	<u>\$ 327.4</u>

United States Government
Consolidated Statements of Operations (Unaudited)
For the Years Ended September 30, 1984, and June 30, 1974

(\$ Billions)

Revenues:	1984	1974
Levied under the Government's sovereign power —		
Individual income taxes	\$ 296.0	\$119.0
Corporate income taxes	59.9	40.7
Social insurance taxes and contributions	242.1	76.8
Excise taxes	37.4	16.8
Estate and gift taxes	6.0	5.0
Miscellaneous	28.3	10.8
Total	669.7	269.1
Earned through U.S. Government business-type operations —		
Sale of goods and services	72.0	24.0
Interest	12.1	1.2
Other	8.1	2.4
Total	92.2	27.6
Total revenues	761.9	296.7
Expenses by Function:		
Social Security and Medicare —		
Social Security (including accrued provision of \$133.4 and \$75.1, respectively)	311.9	131.1
Medicare	62.7	11.3
National defense (including military pensions of \$48.3 and \$14.5, respectively)	218.8	90.7
Interest	120.2	21.5
Public assistance and other income security	79.7	19.7
Civilian employees pensions	46.3	16.4
Commerce, Post Office and housing	37.8	13.9
Health, other than Medicare	30.3	10.7
International affairs	28.7	9.2
Education, training, etc.	25.2	12.3
Transportation	23.8	9.6
Agriculture	23.1	3.2
Veterans' benefits and services	13.8	6.6
Veterans' compensation	13.3	7.0
General government	12.0	3.3
Natural resources and environment	11.1	6.0
Community and regional development	9.7	4.2
General science, space and technology	7.3	4.5
Energy	7.0	0.5
General purpose fiscal assistance	6.9	7.6
Administration of justice	5.7	2.5
Total expenses	1,095.3	391.8
Current Period Deficit	\$ (333.4)	\$ (95.1)

The accompanying notes are an integral part of these statements.

United States Government
Consolidated Statements of Changes in Cash and Monetary Reserves (Unaudited)
For the Years Ended September 30, 1984, and June 30, 1974

(\$ Billions)

Sources of Cash and Monetary Reserves:	1984	1974
Increases in borrowing from public	\$169.1	\$ 2.8
Net changes in other assets and liabilities	14.3	(1.2)
Total sources of cash	183.4	1.6
Uses of Cash and Monetary Reserves:		
Current period operating deficit	333.4	95.1
Add (deduct) charges not requiring cash outlay:		
Depreciation	(29.6)	(13.2)
Non-cash provision for Social Security	(133.4)	(75.1)
Non-cash provision for other pensions	(60.9)	(20.5)
Cash used in (provided by) operations	109.5	(13.7)
Additions to property and equipment	71.9	16.0
Increase in loans receivable	8.9	2.8
Total uses of cash	190.3	5.1
Decrease in Cash and Monetary Reserves	(6.9)	(3.5)
Cash and Monetary Reserves at Beginning of Year	79.7	33.1
Cash and Monetary Reserves at End of Year	\$ 72.8	\$29.6

The accompanying notes are an integral part of these statements.

(1) Summary of General Accounting Policies

Basis of Presentation

Generally accepted accounting principles for national governments are in a state of evolution. The accounting principles followed in the preparation of these consolidated financial statements are generally accrual-basis accounting principles which are followed in the private sector in the United States. In 1975, Arthur Andersen & Co. published the first consolidated financial statements prepared for the U.S. Government (the "Government"), and, subsequently, an Advisory Committee was appointed to study and refine the accounting principles initially developed by Arthur Andersen & Co. During the intervening years, the U.S. Treasury has prepared prototype consolidated financial statements generally based on the initial accounting principles with appropriate modifications for new information identified in subsequent years.

There are a number of uncertainties associated with these consolidated financial statements.

- **Omitted Assets** — Certain strategic military inventories have been omitted because relevant information is classified. The value of the outer continental shelf and related mineral rights, and certain land originally owned by the Government, has been omitted pending further study on appropriate valuation of these assets. See Notes 5 and 6 for further information.
- **Undervalued Assets** — Gold reserves have been valued in the consolidated financial statements at \$42.22 per ounce at both September 30, 1984, and June 30, 1974, while world prices exceed this amount. The carrying amount of certain land, buildings and equipment has been estimated and, accordingly, may be understated. See Notes 2, 6 and 7 for further information.
- **Understated Reserves** — Reserves for uncollectible loans and receivables, and the Government's liability for certain outstanding commitments, guarantees and contingencies is probably understated in these consolidated financial statements. See Notes 4 and 12 for further information.

During the course of preparing this booklet, various observations were made regarding the accounting principles applied and the procedures followed in preparing the consolidated financial statements. These have been provided to the U.S. Treasury for future consideration. Certain matters relating to accounting principles could have a significant impact on these financial statements and are summarized in Appendix 7.

Notwithstanding the foregoing, the accompanying consolidated financial statements, although unaudited, represent the best available information concerning the financial position and results of operations of the U.S. Government.

Principles of Consolidation

The statements include the accounts of all significant agencies and funds of the Government. Many independent and business-type agencies such as the U.S. Postal Service and the Federal Financing Bank, which the Congressionally approved budget does not include, have been included in the statements because they are wholly owned by the Government and within the scope of Government operations. However, some quasi-governmental corporations, such as Conrail, are not included.

Intragovernmental transactions have been eliminated in consolidation.

These statements exclude Government-sponsored enterprises, such as the Federal Land Banks, because they are privately owned. The Federal Reserve System, owned by private banks throughout the United States, is excluded. If the Federal Reserve Banks were included in the consolidated balance sheets as of June 30, 1974, and September 30, 1984, the effect would be as follows.

(\$ Billions)	1984	1974
Increase in total assets	\$ 39.5	\$ 3.1
Increase in total liabilities		
Reduce debt	\$(155.0)	\$(80.6)
Eliminate gold certificate liability	(11.1)	(11.5)
Add Federal Reserve Notes	160.1	64.3
Add deposits of member banks	23.6	26.7
Increase other liability accounts	18.4	2.3
	36.0	1.2
Reduce accumulated deficit	3.5	1.9
	\$ 39.5	\$ 3.1

Fiscal Year

The fiscal year of the Government ended on September 30 in 1984 and June 30 in 1974. The fiscal year was changed in 1976, when a "transition quarter" was reported for July 1 through September 30, 1976.

Reclassifications and Adjustments

For comparability, certain 1974 data have been reclassified where appropriate to conform to the financial statement presentation for 1984. Certain changes were made in the accounting policies used in preparing these statements for 1984 vs. 1974. These changes are described in Notes 11 and 15.

(2) Cash and Monetary Equivalents

(\$ Billions)	September 30, 1984	June 30, 1974
Gold (at \$42.22 per ounce, the statutory price at which gold is monetized by issuance of gold certificates to the Federal Reserve System)	\$11.1	\$11.6
U.S. Treasury operating cash and monetary assets	31.3	10.4
U.S. reserve position in the International Monetary Fund	11.6	1.1
Foreign currencies	6.7	1.9
Cash outside the U.S. Treasury held by fiscal officers	6.5	2.4
Special drawing rights, an international reserve asset	5.6	2.2
	<u>\$72.8</u>	<u>\$29.6</u>

(3) Accrued Taxes Receivable

The September 30, 1984, total for taxes receivable represents \$26.0 billion for delinquent taxes (net of allowance for the estimated uncollectible portion) and \$4.2 billion of accrued corporate taxes. The totals at June 30, 1974, were \$5 billion for delinquent taxes and \$10 billion for accrued corporate taxes.

(4) Loans Receivable

Outstanding loans and allowances for losses have been recorded as reported by the various Government lending agencies. The allowances for losses are believed to be understated and they are under study at September 30, 1984.

Interest rates and loan repayment terms vary considerably for outstanding loans, with terms from as short as five days in 1984 (90 days in 1974) to over 35 years for both years. Interest rates ranged up to 17.9% in 1984 and 12.0% in 1974. Loans outstanding by creditor are presented below.

(\$ Billions)	September 30, 1984	June 30, 1974
Federal Financing Bank*	\$144.8	\$ 0.6
Office of the President	20.5	15.3
Department of Agriculture	20.0	9.2
Export-Import Bank of the United States	17.5	7.9
Department of Housing and Urban Development	14.0	9.8
Rural Electrification Administration	11.4	7.3
Other departments and agencies	32.9	15.9
	<u>261.1</u>	<u>66.0</u>
Less intergovernmental loans and allowance for estimated uncollectible loans	<u>(32.0)</u>	<u>(1.5)</u>
Net receivable	<u>\$229.1</u>	<u>\$64.5</u>

*The Federal Financing Bank acts as a clearinghouse for Federal agencies and Federally assisted borrowing from the public. At September 30, 1984, the Federal Financing Bank has loans receivable relating to the following programs.

Rural housing	\$ 26.8
Farmers Home Administration — agricultural credit	22.5
Rural Electrification Administration	20.6
Foreign Military Sales Credit	17.1
Other loans to the public	27.2
	<u>114.2</u>
Loans to Government agencies	30.6
Total	<u>\$144.8</u>

(5) Inventories

Inventories include nondepreciable personal property and are generally stated at cost. The September 30, 1984, total for inventories comprises \$109.6 billion for the Department of Defense and \$41.8 billion for other agencies. The comparable amounts as of June 30, 1974, were \$43.5 billion and \$7.1 billion, respectively.

The inventory accounts do not include the weapons stockpile since the extent of this inventory is classified information.

(6) Land

Land is valued at the cost paid by the Government. The cost of land acquired through donation, exchange, bequest, forfeiture, or judicial process is estimated by the General Services Administration at amounts the Government would have paid if purchased at the date of acquisition.

Pending study of valuation methods, the outer continental shelf and other offshore land, and the 670 million acres of public domain land (land vested in the United States by virtue of its sovereignty) have not been included. In 1972, a Committee of the House of Representatives estimated the value of public domain land (92% of the total onshore acreage owned by the Government) to be \$29.9 billion.

(7) Buildings, Structures and Facilities

Buildings, structures and facilities consists of all real property owned by the Government except land. The total reflects the cost of acquiring or erecting buildings, dams, utility systems, monuments, roads and bridges, except for interest costs during construction. The September 30, 1984, total represents \$58.5 billion for the Department of Defense, excluding the Corps of Engineers, and \$78.5 billion for other agencies. The amounts as of June 30, 1974, were \$40.9 billion and \$47.6 billion, respectively.

(8) Depreciable Personal Property

Equipment and military hardware are recorded at acquisition cost and include only depreciable property currently in use or in usable condition. The major components of each category are summarized below.

(\$ Billions)	1984	1974
Military hardware —		
Aircraft and related equipment	\$140.0	\$ 51.0
Ships and surface craft	89.8	36.3
Combat and technical vehicles	67.9	16.9
Missiles and related equipment	27.0	9.8
Other	5.5	5.9
Total	<u>\$330.2</u>	<u>\$119.9</u>
Equipment —		
Department of Defense		
Industrial plant equipment	\$ 20.8	\$ 14.0
Other	33.5	7.7
Other agencies	34.3	18.0
Total	<u>\$ 88.6</u>	<u>\$ 39.7</u>

(9) Depreciation

Most Government agencies do not calculate depreciation on property and equipment. Using a straight-line basis, accumulated depreciation has been estimated from available information.

The useful lives applied to each classification of asset are as follows.

- ☐ Buildings, structures, and facilities — 50 years.
- ☐ Ships and surface craft — 30 years.
- ☐ Industrial plant equipment — 20 years.
- ☐ All other depreciable assets — 10 years.

(10) Borrowing from the Public

As of September 30, 1984, the gross amount of Government debt outstanding, net of unamortized premiums and discounts, was \$1,563.2 billion. This amount was reduced by \$263.7 billion for intragovernmental holdings, \$111.4 billion of which is held by the Civil Service Retirement System Trust Fund.

The amount of debt outstanding, net of unamortized premiums and discounts, as of June 30, 1974, was \$483.7 billion. This amount was reduced by \$140.1 billion for intragovernmental holdings.

As of September 30, 1984, foreign and international investors held approximately \$175.5 billion of the debt outstanding with the public. The amount as of June 30, 1974, was \$56.8 billion.

Maturities and interest rates of debt outstanding at September 30, 1984, are summarized below.

	Total Debt (\$ Billions)	Average Interest Rate (Percent)	Maturity (\$ Billions)					
			Within 1 Year	1-5 Years	5-10 Years	10-20 Years	20 Years or Longer	Various
Marketable								
Bills	\$ 345.6	11.069%	\$345.6	—	—	—	—	—
Notes	660.5	11.647	166.8	\$364.6	\$129.1	—	—	—
Bonds	152.8	10.746	0.8	0.6	33.7	\$117.7	—	—
	<u>1,158.9</u>	<u>11.362</u>	<u>513.2</u>	<u>365.2</u>	<u>162.8</u>	<u>117.7</u>	<u>—</u>	<u>—</u>
Nonmarketable								
Foreign government series	8.9	9.562	5.3	3.6	—	—	—	—
Government account series	1.0	6.510	0.7	0.2	0.1	—	—	—
U.S. savings bonds	72.8	7.150	0.6	3.4	12.7	—	—	\$56.1
Other	41.8	8.749	—	—	—	—	—	41.8
	<u>124.5</u>	<u>7.583</u>	<u>6.6</u>	<u>7.2</u>	<u>12.8</u>	<u>—</u>	<u>—</u>	<u>97.9</u>
Other								
Agency securities	3.4	6.198	*	1.4	1.8	—	—	0.2
Other	12.7	—	*	—	—	—	\$ 12.0	0.7
	<u>16.1</u>	<u>6.198</u>	<u>*</u>	<u>1.4</u>	<u>1.8</u>	<u>—</u>	<u>12.0</u>	<u>0.9</u>
Net borrowing from the public								
Current period	1,299.5		519.8	373.8	177.4	117.7	12.0	98.8
Prior period	1,130.4		464.6	377.2	107.4	50.4	40.4	90.4
Net Increase	<u>\$ 169.1</u>		<u>\$ 55.2</u>	<u>\$ (3.4)</u>	<u>\$ 70.0</u>	<u>\$ 67.3</u>	<u>\$(28.4)</u>	<u>\$ 8.4</u>

*Less than \$100 million.

(11) Accrued Pension, Retirement and Disability Plans

The accounting for accrued pension, retirement and disability plans is subject to several different assumptions, definitions and methods of calculation. Public Law 95-595 became effective in fiscal year 1979 and covers military, civilian and other pension plans. The Law requires an annual actuarial determination of the plan liability, generally in accordance with provisions of Statement of Financial Accounting Standards No. 35. Due to the adoption of this law, a prior period adjustment totalling \$245 billion was made in 1979, which principally related to accruing non-vested benefits.

Military Personnel and Civilian Employees

The liabilities under these two pension plans represent a major portion of the total unfunded liability under Public Law 95-595. In prior prototype Consolidated Financial Statements, the accrued pension liabilities for September 30 represented the actuarial present value of accumulated plan benefits and were calculated in accordance with instructions developed jointly by the General Accounting Office and the Office of Management and Budget under the provisions of Public Law 95-595.

The actuarial liabilities as of September 30, 1984, were not available for either plan as of the date the Consolidated Financial Statements were prepared. The liabilities were estimated by the Treasury by calculating a simple average of the change in reported liability for each of fiscal years 1981, 1982, and 1983.

Subsequent to the issuance of the 1984 Treasury-prepared Consolidated Financial Statements, the final actuarial reports of the military and civilian pension plans were completed for the fiscal year ended September 30, 1984. Due to increases for both plans in the interest rate utilized in the 1984 actuarial assumptions, the subsequently issued actuarial reports reflected a future obligation for these two plans of \$959.3 billion as compared with \$1,018.8 billion reflected in the accompanying financial statements. It would not be appropriate to record the full impact of this \$59.5 billion actuarial "gain," due principally to the changed actuarial assumption for interest, in 1984 operations. This issue will be considered by the Treasury in future prototype Consolidated Financial Statements.

Other Plans

Annual pension reports received from other plans covered by Public Law 95-595 are reported in the same manner as plans for military personnel and civilian employees described above. This consists of Federal employees' compensation liability as well as 31 separate plans, of which the largest are the U.S. Coast Guard, Foreign Service, Tennessee Valley Authority and the Commissioned Corps of Public Health Service retirement plans. At September 30, 1984, \$11.2 billion related to the Federal Employees Compensation Act, which provides payments to injured workers, and \$18.2 billion related to the remaining 31 plans. Because information prior to the issuance of Public Law 95-595 is not reliable or, in some cases, not available, a liability is not reported at June 30, 1974.

Social Security

The liability equals the amortized portion of the unfunded liability for the program. The unfunded liability represents the present value of the projected excess of future benefit payments to present participants over the contributions still to be made by the same group and their employers for the next 75 years.

The unfunded liability is determined annually and the change is amortized over a 30-year period. This amortization is reported as the non-cash provision for Social Security in the consolidated statements of operations (\$133.4 billion in 1984 and \$75.1 billion in 1974) and is reported as a liability on the consolidated balance sheet.

As of September 30, 1984, the unfunded liability for Social Security was \$4.2 trillion, of which \$1.9 trillion has been recorded through amortization and shown as a liability on the consolidated balance sheet.

Veterans' Compensation

Veterans' Compensation liability was computed in 1974 using the present value of projected payments for the next 25 years. In 1984, this liability was computed using the present value of projected payments for the next 20 years.

(12) Contingent Liabilities for Guarantee and Insurance Programs

Several Government agencies insure businesses and individuals against various risks. The amount of insurance coverage in force, representing the maximum risk exposure to the Government, was \$2.6 trillion at September 30, 1984, and \$1.0 trillion at June 30, 1974.

The Government also guarantees certain loans made by private lenders. Loan guarantees in force totaled \$615 billion at September 30, 1984, and \$160 billion at June 30, 1974.

Several Government agencies make no provision for estimated losses on loan guarantees or insurance while others do not provide an estimate. Agencies estimated that an allowance of \$3.5 billion would be necessary to cover anticipated losses on loan guarantees and insurance in force at September 30, 1984. A comparable estimate for June 30, 1974, is not readily available.

The loan guarantee and insurance programs and other contingent liabilities and commitments of the Government are outlined below.

(\$ Billions)	Amounts Outstanding	
	September 30, 1984	June 30, 1974
Commitments:		
Long-term contracts —		
Tennessee Valley Authority	\$ 7.8	\$ 2.4
General Services Administration	3.0	2.0
Other	18.5	5.3
	<u>29.3</u>	<u>9.7</u>
Undelivered orders —		
Housing and Urban Development	248.1*	8.6
Defense	88.5**	28.8**
Transportation	32.4	10.4
Funds appropriated to the President	31.9	9.6
Health and Human Services	22.6	12.3
Environmental Protection Agency	10.4	4.5
Education (included in HHS in 1974)	9.2	—
Other	42.4	17.4
	<u>485.5</u>	<u>91.6</u>
	<u>\$514.8</u>	<u>\$101.3</u>

*Amount includes rental and housing assistance commitments over the next forty years.

**Amount excludes significant amounts of future hardware deliveries.

(\$ Billions)	Estimated Loss at September 30, 1984	Contingent Liability Maximum Risk Exposure	
		September 30, 1984	June 30, 1974
Contingencies:			
Government loan and credit guarantees —			
Housing	\$0.2	\$ 212.3	\$ 107.2
Government National Mortgage Assoc.	—	175.5	—
Veterans' benefits	—	57.6	26.6
Rural development	0.2	44.6	6.4
Education	—	37.4	2.4
Farm ownership	0.2	26.8	2.6
Small business loans	0.3	10.6	3.9
Shipbuilding and operations	—	7.7	3.8
Export-Import Bank	—	6.5	3.4
Other	—	36.0	3.4
	<u>0.9</u>	<u>615.0</u>	<u>159.7</u>
Insurance in force —			
Federal Deposit Insurance Corp.	1.8	1,322.4	441.8
Federal Savings & Loan Insurance Corp.	—	751.2	220.3
Department of Transportation	—	222.7	69.6
Federal Emergency Management Agency	—	147.2	183.6
National Credit Union Administration	—	75.1	16.5
Nuclear Regulatory Commission	—	68.0	60.0
Veterans Administration	0.1	29.0	35.6
Other	0.7	21.2	13.4
	<u>2.6</u>	<u>2,636.8</u>	<u>1,040.8</u>
Unadjudicated claims	—	48.6	7.3
Other contingencies	—	15.8	19.2
	<u>\$3.5</u>	<u>\$3,316.2</u>	<u>\$1,227.0</u>

(13) Open-Ended Programs and Fixed Costs

The Government commits itself to provide services by passing laws that make spending mandatory. Since a significant amount of future spending is fixed by law, it is very probable that the Government will pay for these programs in future years. Listed below are the net cash expenditures for programs that will continue and can be terminated only if current laws are changed.

(\$ Billions)	1984	1974
Payments to individuals —		
Social Security and Railroad Retirement	\$179.3	\$ 57.6
Federal Employees Retirement and Insurance	49.0	10.8
Unemployment Assistance	16.9	6.5
Medicare and Medicaid	79.9	17.2
Public Assistance and related programs	21.0	11.5
All other	11.3	11.8
Individual entitlements	357.4	115.4
Net interest	111.1	21.5
General Revenue Sharing	4.6	6.1
Other open-ended programs and fixed costs	5.7	7.8
Total	<u>\$478.8</u>	<u>\$150.8</u>

(14) Reconciliation of Accrual-Basis Operating Results to Cash-Basis Budget

A reconciliation of the cash-basis deficit to the GAAP-basis deficit for fiscal year 1984 and fiscal year 1974 is summarized below.

(\$ Billions)	1984	1974
Reported budget outlays over receipts (cash basis)	\$175.3	\$ 4.7
Net expense of off-budget agencies	10.0	1.4
Total budget deficit (cash basis)	185.3	6.1
Add:		
Non-cash provision for Social Security	133.4	75.1
Non-cash provisions for retirement and disability benefits	60.9	20.5
Depreciation	29.6	13.2
Other	5.0	(1.0)
	228.9	107.8
Deduct:		
Capital outlays	71.9	16.0
Net loan disbursements	8.9	2.8
	80.8	18.8
Current period deficits (expenses over revenues) on accrual basis per consolidated statement of operations	<u>\$333.4</u>	<u>\$ 95.1</u>

(15) Changes in Accumulated Deficit

The deficit increased during the ten-year period ended September 30, 1984, as follows.

(\$ Billions)	Prior Period Adjustments	Current Period Deficit	Accumulated Deficit, Ending Balance
Year:			
Balance, June 30, 1973			\$ 716.6
1974	\$ 1.9	\$ 95.1	813.6
1975	—	152.1	965.7
1976	14.9	188.8	1,169.4
Transition Quarter	—	57.3	1,226.7
1977	(0.9)	224.6	1,450.4
1978	(12.5)	215.8	1,653.7
1979	259.2	256.8	2,169.7
1980	—	322.2	2,491.9
1981	—	264.7	2,756.6
1982	—	314.0	3,070.6
1983	—	395.3	3,465.9
1984	—	333.4	3,799.3

The prior period adjustment in 1979 increased pension liabilities by \$245.2 billion (see Note 11) and corrected an overstatement of materials and commodities.

Certain Economic and Social Questions

This booklet is directed toward providing a basis to more realistically assess the real financial position of the U.S. Government. Providing these financial statements is the accountant's professional contribution. The more difficult questions remain for all of us as citizens to answer: What are the implications of the information presented in these financial statements? What public policy issues are raised by this information?

Of course, GAAP-basis reporting alone cannot assure that these policy choices will be addressed; that is the responsibility of citizens and legislators. As this book has tried to show, however, use of GAAP promises to improve and broaden — among other things, by careful estimation of future liabilities — the information on the full, long-range cost of any public undertaking. This comprehensive information is essential to maintaining the informed public choice that our nation's founders were anxious to preserve.

Like our 1975 publication, this one includes a list of economic and social questions arising from information presented in the consolidated financial statements. The following questions suggest the importance of having complete financial information in resolving critical issues. The list is illustrative, not exhaustive, and it includes issues raised by observers with different (and often conflicting) political perspectives.

Debt Capacity — The Government's public debt (debt owed to investors other than the Government's agencies) increased from \$214 billion in 1949 to \$346 billion in 1974 and to \$1.3 trillion in 1984. As a percentage of GNP, Government debt declined from 82% in 1949 to 25% in 1974, but had increased to 36% in 1984 and continues to grow.

- ☐ Will this create a serious situation for the economy in the light of other demands for capital by the private sector, and state and local governments?

- ☐ Has the total debt already reached a level where the carrying cost is unduly burdensome?
- ☐ What would be the implications for the Government's credibility and defense posture if the level of debt relative to GNP were to rise to immediate post-World War II levels?

Debt Held Outside the United States — The amount of Government debt owned by non-U.S. interests increased from \$3 billion in 1949 to \$57 billion in 1974 and \$176 billion in 1984.

- ☐ What would be the implications if U.S. Government securities became a less attractive investment for non-U.S. investors?
- ☐ Does interest paid to non-U.S. investors for funds borrowed to finance current operations weaken the economy's ability to improve the standard of living for American workers?

Debt Held by the Government Itself — The amount of Government debt held by Government trust funds increased from \$38 billion in 1949 to \$140 billion in 1974 and to \$264 billion in 1984.

- ☐ Is it prudent for an organization to invest funds held in trust in its own securities?
- ☐ Could the Government invest large sums of trust fund monies in the private capital markets without disturbing these markets?

The Growing Deficit — The accumulated deficit on a GAAP basis has increased from \$814 billion in 1974 to \$3.8 trillion in 1984.

- ☐ Does this deficit place an unmanageable burden on current and future generations of American taxpayers?
- ☐ Would wide distribution of the U.S. Government's annual report affect individual financial planning?

Revenues — Tax revenues on a GAAP basis are essentially equivalent to cash basis receipts and were 19.1 % of GNP in 1974, 20.8 % of GNP in 1981 and 18.6 % of GNP in 1984.

- ☐ What would be the impact on the national economy if attempts were made to increase revenues at this stage of the economic cycle?
- ☐ Would reductions in progressivity of individual income tax rates increase or decrease the overall level of tax collections?
- ☐ If the U.S. Government were to limit deductibility of certain state and local taxes, or transfer certain programs to state and local governments, what actions would state and local governments take and what impact, in turn, would these actions have on U.S. Government revenue?

Pensions — Retirement benefits for Government employees are a significant portion of the total cost of Government.

- ☐ Does the promise to pay future retirement benefits substantially restrict the future financial flexibility of the Government?
- ☐ Can the Government retain the qualified workers it needs without offering them an attractive, competitive compensation package? And, can the Government reduce its pension costs, as some have proposed, without offsetting increases in salaries?

Social Security — The unfunded liability of the Social Security program was \$4.2 trillion in 1984 (including \$1.9 trillion recorded as a liability in the accompanying consolidated financial statements). This liability is the present value of future payments to present participants, net of the amounts that participants and their employers are expected to pay into the system over their working lives.

- ☐ Is the low personal savings rate in the United States — now among the lowest of major industrialized nations — partially explained by a public perception that the Government will provide significant retirement benefits during their retirement years?
- ☐ Do current retirees have a right to expect more generous benefits than were received by prior generations?
- ☐ What would be the effect on private pension systems of changes in Social Security benefits?
- ☐ Will future workers and their employers pay the higher Social Security taxes currently scheduled?

- ☐ If the Government levies sufficient taxes to fund Social Security benefits on a sound actuarial basis, will it end up owning all the means of production in the United States?

Health Care — The Medicare and Medicaid programs, enacted in the 1960s, have grown from \$17.2 billion per year in 1974 to \$82.8 billion in 1984. Under the Government's current accounting principles, the full cost of these programs is not recorded — or even well understood. Many project these programs to continue growing at a rate faster than GNP.

- ☐ How can the U.S. Government balance the cost of its health care program with its desire to provide access to good medical care to all its citizens?
- ☐ What are the economic, social and political consequences of channeling an increasing share of the nation's resources to the elderly when unemployment continues at a high level and when unemployment among minority teenagers is reaching new highs?

Domestic Programs — As the American people have sought to alleviate poverty, reduce pollution, make travel safer and meet other national goals, the Government has assumed a larger role. While many doubt the effectiveness of this role, others argue that increasing Government involvement is essential if national objectives are to be reached.

- ☐ How effective are the various Government programs in meeting major national needs?
- ☐ Is the Government maintaining and replacing its infrastructure at a level sufficient to support continued economic growth?

Defense — Some observers maintain that the defense budget is excessive and extravagant. Others argue that any perceived weakness on the part of the United States invites war. While the debate has continued, the level of military outlays has fluctuated widely. On a GAAP basis, defense costs, exclusive of accruals for pensions, were 5.5 % of GNP in 1974 and 4.8 % in 1984.

- ☐ Should the Department of Defense attempt to quantify the cost of achieving each major national security objective?
- ☐ Does the U.S. military place the greatest amount of resources in those programs which do the most to ensure the national security?

- ☐ Does increased reliance on career personnel in the armed forces provide a more cost-effective method of keeping the peace?

Debt of Developing Nations — U.S. private banks had loaned approximately \$105 billion to the non-OPEC, developing countries as of June 30, 1985. Several of these countries have experienced extreme difficulties in meeting interest and principal payments to U.S. banks. The loans in question exceed two-thirds of the total net worth of all U.S. private banks.

- ☐ Have large U.S. Government deficits worsened the developing nations' debt crisis?
- ☐ Should Government-supported institutions loan money to countries that do not prepare audited financial statements?
- ☐ Would a requirement for audited financial statements encourage better planning and instill discipline in the financial management of developing countries?

- ☐ Can the Government reasonably expect debtor nations to prepare audited financial statements when it does not do so itself?

Trade Deficit — The value of the U.S. dollar increased relative to other key currencies between 1974 and 1984. Some economists have attributed this rise in part to high real interest rates they say resulted from increased U.S. Government borrowing. Many economists also believe that the strong dollar has adversely impacted the U.S. trade balance. In 1984, the United States ran a trade deficit of \$123 billion.

- ☐ Will continued unfavorable trade balances result in new Government commitments to protect American industries, thus creating liabilities for the Government?
- ☐ Will the trade deficit create pressure to impose revenue-producing tariffs?
- ☐ Would a reduced Government deficit improve the competitive position of American industries in international markets?

Appendices

Appendix 1

United States Government

Consolidated Statements of Operations

For the Years Ended September 30, 1984, and June 30, 1974, in 1984 Dollars

(\$ Billions)	1974			Real Percentage Change
	1984	Restated in 1984 \$	Nominal \$	
Revenues:				
Levied under sovereign power —				
Individual income taxes	\$ 296.0	\$ 238.5	\$ 119.0	24.1%
Corporate income taxes	59.9	81.6	40.7	(26.6)
Social insurance taxes and contributions	242.1	153.9	76.8	57.3
Excise taxes	37.4	33.7	16.8	11.0
Estate and gift taxes	6.0	10.0	5.0	(40.0)
Miscellaneous (includes customs duties)	28.3	21.6	10.8	31.0
Total	669.7	539.3	269.1	24.2
Earned through U.S. Government business-type operations —				
Sale of goods and services	72.0	48.1	24.0	49.7
Interest	12.1	2.4	1.2	404.2
Other	8.1	4.8	2.4	68.8
Total	92.2	55.3	27.6	66.7
Total revenues	761.9	594.6	296.7	28.1
Expenses by Function:				
Social Security and Medicare —				
Social Security	311.9	262.8	131.1	18.7
Medicare	62.7	22.6	11.3	177.4
National defense	218.8	181.8	90.7	20.4
Interest	120.2	43.1	21.5	178.9
Public assistance and other income security	79.7	39.5	19.7	101.8
Civilian employees pensions	46.3	32.9	16.4	40.7
Commerce, Post Office and housing	37.8	27.9	13.9	35.5
Health, other than Medicare	30.3	21.4	10.7	41.6
International affairs	28.7	18.4	9.2	56.0
Education, training etc.	25.2	24.6	12.3	2.4
Transportation	23.8	19.2	9.6	24.0
Agriculture	23.1	6.4	3.2	260.9
Veterans' benefits and services	13.8	13.2	6.6	4.5
Veterans' compensation	13.3	14.0	7.0	(5.0)
General government	12.0	6.6	3.3	81.8
Natural resources and environment	11.1	12.0	6.0	(7.5)
Community and regional development	9.7	8.4	4.2	15.5
General science, space and technology	7.3	9.0	4.5	(18.9)
Energy	7.0	1.0	0.5	600.0
General purpose fiscal assistance	6.9	15.2	7.6	(54.6)
Administration of justice	5.7	5.0	2.5	14.0
Total expenses	1,095.3	785.0	391.8	39.5
Current Period Deficit	\$ (333.4)	\$(190.4)	\$ (95.1)	75.1%

Appendix 2

United States Government Financial Trends — 1974-1984 (\$ Billions)

Fiscal Year	Cash Basis				Surplus (Deficit)					
	Receipts		Disbursements		Cash Basis		GAAP Basis			
	Amount	% GNP	Amount	% GNP	Nominal Dollars	% GNP	1984 Dollars	Nominal Dollars	% GNP	1984 Dollars
1974	\$263.2	19.1%	\$269.4	19.5%	\$ (6.1)	0.4%	\$ (12.2)	\$ (95.1)	6.9%	\$(190.4)
1975	279.1	18.9	332.3	22.5	(53.2)	3.6	(97.7)	(152.1)	10.3	(279.4)
1976	298.0	18.2	371.8	22.7	(73.7)	4.5	(126.4)	(188.8)	11.5	(323.7)
1977	355.6	19.1	409.2	22.0	(53.6)	2.9	(85.9)	(224.6)	12.1	(359.8)
1978	399.7	19.1	458.7	21.9	(59.0)	2.8	(88.4)	(215.8)	10.3	(323.2)
1979	463.3	19.7	503.5	21.4	(40.2)	1.7	(55.5)	(256.8)	10.9	(354.9)
1980	517.1	20.1	590.9	22.9	(73.8)	2.9	(93.5)	(322.2)	12.5	(408.3)
1981	599.2	20.8	678.2	23.5	(78.9)	2.7	(91.3)	(264.7)	9.2	(306.3)
1982	617.7	20.3	745.7	24.5	(127.9)	4.2	(138.5)	(314.0)	10.3	(339.9)
1983	600.6	18.6	808.3	25.1	(207.8)	6.4	(215.6)	(395.3)	12.3	(410.1)
1984	666.5	18.6	851.8	23.8	(185.3)	5.2	(185.3)	(333.4)	9.3	(333.4)

Details may not add to the totals due to rounding.

Source: The Budget in Brief, Fiscal Year 1986

Appendix 3

United States Government Components of Receipts and Outlays as a Percentage of GNP

Year	Receipts					Outlays							Surplus/ Deficit
	Individual Income Tax	Corporate Income Tax	Social Security and Medicare	Other	Total	National Defense	Social Security and Medicare	Income Security	Net Interest	Other	Offsetting Receipts	Total	
1940	0.9%	1.3%	0.8%	3.9%	6.9%	1.7%	0.0%	1.6%	0.9%	6.1%	-0.3%	10.0%	-3.1%
1945	8.5	7.4	0.7	4.2	20.8	38.2	0.1	0.5	1.4	3.1	-0.6	42.7	-21.9
1950	5.9	3.9	1.0	4.1	14.9	5.2	0.3	1.5	1.8	8.0	-0.7	16.1	-1.2
1955	7.6	4.7	1.6	3.3	17.2	11.2	1.2	1.3	1.3	3.9	-0.9	18.0	-0.8
1960	8.2	4.3	2.3	3.8	18.6	9.7	2.3	1.6	1.4	4.5	-1.0	18.5	0.1
1965	7.4	3.9	2.6	3.8	17.7	7.7	2.6	1.4	1.3	5.9	-1.0	17.9	-0.2
1970	9.3	3.4	4.0	3.2	19.9	8.4	3.8	1.6	1.5	5.8	-0.9	20.2	-0.3
1974	8.6	2.8	4.8	2.9	19.1	5.8	4.7	2.4	1.6	6.2	-1.2	19.5	-0.4
1975	8.3	2.7	5.1	2.8	18.9	5.8	5.2	3.4	1.6	7.4	-0.9	22.5	-3.6
1976	8.0	2.5	4.9	2.8	18.2	5.5	5.5	3.7	1.6	7.3	-0.9	22.7	-4.5
1977	8.5	2.9	5.0	2.7	19.1	5.2	5.6	3.3	1.6	7.1	-0.8	22.0	-2.9
1978	8.7	2.9	5.0	2.5	19.1	5.0	5.6	2.9	1.7	7.5	-0.8	21.9	-2.8
1979	9.2	2.8	5.1	2.6	19.7	4.9	5.5	2.8	1.8	7.1	-0.7	21.4	-1.7
1980	9.5	2.5	5.4	2.7	20.1	5.2	5.8	3.4	2.0	7.4	-0.8	22.9	-2.9
1981	9.9	2.1	5.7	3.1	20.8	5.5	6.2	3.5	2.4	6.9	-1.0	23.5	-2.7
1982	9.8	1.6	5.9	3.0	20.3	6.1	6.6	3.5	2.8	6.4	-0.9	24.5	-4.2
1983	9.0	1.0	5.8	2.8	18.6	6.5	6.9	3.8	2.8	6.1	-1.1	25.1	-6.4
1984	8.3	1.6	5.9	2.8	18.6	6.4	6.6	3.1	3.1	5.5	-0.9	23.8	-5.2

This Table prepared on cash basis of accounting

Source: Historical Tables Budget of the United States Government — Fiscal Year 1986

Details may not add to the totals due to rounding

Appendix 4

**United States Government
Summary of Debt (\$ Billions)**

Year	Debt Held by Public				Government Accounts	Gross Debt	% of GNP	
	Foreign	U.S. Private	Federal Reserve	Total *			Gross Debt	Public Debt
1974	\$ 56.8	\$208.6	\$ 80.6	\$ 346.0	\$140.2	\$ 486.2	35.3%	25.1%
1975	66.0	245.9	84.9	396.8	147.3	544.1	36.8	26.8
1976	69.8	315.8	94.7	480.3	151.5	631.8	38.5	29.3
1977	95.5	351.3	105.0	551.8	157.3	709.1	38.1	29.6
1978	121.0	374.5	115.5	611.0	169.4	780.4	37.3	29.2
1979	120.3	408.7	115.6	644.6	189.2	833.8	35.4	27.3
1980	121.7	472.6	120.8	715.1	199.2	914.3	35.5	27.8
1981	130.7	539.3	124.5	794.5	209.5	1,004.0	34.8	27.5
1982	140.6	654.3	134.5	929.4	217.5	1,146.9	37.7	30.5
1983	160.1	826.1	155.5	1,141.7	240.1	1,381.8	42.9	35.4
1984	175.5	982.0	155.1	1,312.6*	263.7	1,576.3	44.0	36.7

* Does not include adjustment for deferred interest, etc. (\$13.1 billion in 1984).

Appendix 5

Data Relating to Social Security

History of Tax Rates and Taxable Wage Base (A):

Period	Annual Maximum Taxable Earning	Employer and Employee, Each (B)			Individual Total	Combined Total	Maximum Tax Per Employee	Self-Employed Person (B)				Maximum Tax Per Self- Employed Person
		OASI	DI	HI				OASI	DI	HI	Total	
1937-49	\$ 3,000	1.0 %	—	—	1.0 %	2.0 %	\$ 60	—	—	—	—	\$ 0
1950	3,000	1.5	—	—	1.5	3.0	90	—	—	—	—	0
1960	4,800	2.75	.25 %	—	3.0	6.0	288	4.125 %	.375 %	—	4.5 %	216
1970	7,800	3.65	.55	.6 %	4.8	9.6	749	5.475	.825	.6 %	6.9 %	538
1971	7,800	4.05	.55	.6	5.2	10.4	811	6.075	.825	.6	7.5	585
1972	9,000	4.05	.55	.6	5.2	10.4	936	6.075	.825	.6	7.5	675
1973	10,800	4.3	.55	1.0	5.85	11.7	1,264	6.205	.795	1.0	8.0	864
1974	13,200	4.375	.575	.9	5.85	11.7	1,544	6.185	.815	.9	7.9	1,043
1975	14,100	4.375	.575	.9	5.85	11.7	1,650	6.185	.815	.9	7.9	1,114
1976	15,300	4.375	.575	.9	5.85	11.7	1,790	6.185	.815	.9	7.9	1,209
1977	16,500	4.375	.575	.9	5.85	11.7	1,931	6.185	.815	.9	7.9	1,304
1978	17,700	4.275	.775	1.00	6.05	12.1	2,142	6.01	1.09	1.00	8.10	1,434
1979	22,900(C)	4.33	.75	1.05	6.13	12.26	2,808	6.01	1.04	1.05	8.10	1,855
1980	25,900(C)	4.52	.56	1.05	6.13	12.26	3,175	6.2725	.7775	1.05	8.10	2,098
1981	29,700(C)	4.7	.65	1.30	6.65	13.3	3,950	7.025	.975	1.30	9.30	2,762
1982	32,400(D)	4.575	.825	1.30	6.7	13.4	4,342	6.8125	1.2375	1.30	9.35	3,029
1983	35,700(D)	4.775	.625	1.30	6.7	13.4	4,784	7.1125	.9375	1.30	9.35	3,338
1984	37,800(D)	5.2	.50	1.30	7.0	14.0	5,292	10.4	1.0	2.6	14.0	5,292
1985	39,600(D)	5.2	.50	1.35	7.05	14.1	5,584	10.4	1.0	2.7	14.1	5,584
Future Schedule												
1986-87	(D)	5.2	.50	1.45	7.15	14.3	(D)	10.4	1.0	2.9	14.3	(D)
1988-89	(D)	5.53	.53	1.45	7.51	15.02	(D)	11.06	1.06	2.9	15.02	(D)
1990-99	(D)	5.6	.60	1.45	7.65	15.3	(D)	11.2	1.20	2.9	15.3	(D)
2000 and thereafter	(D)	5.49	.71	1.45	7.65	15.3	(D)	10.98	1.42	2.9	15.3	(D)

(A) Source: *Social Security Bulletin Annual Statistical Supplement and 1985 Trustees' Report*, OASDI

(B) OASI = Federal Old-Age and Survivors Insurance

DI = Disability Insurance

HI = Health Insurance (Medicare)

(C) 1979-1981 amounts specified by the Social Security Amendments of 1977.

(D) These amounts reflect the application of a prescribed formula which applies a ratio of defined average wages for the previous three years. The amount of wages serving as a base will be redetermined by the Government annually; thus, the wage base and maximum tax is expected to increase annually roughly as real wages in the economy increase.

Appendix 5 (Continued)

Schedule of Non-Cash Provisions for Social Security:

(\$ Billions)

Year	Ending Present Value of Future Unfunded Benefits (D)	Annual Change in Prior Service Costs	Change in Amortization (30 Years) (B)	Annual Non-Cash Provision (E)	Cumulative Liability
Prior Years	—	—	—	—	\$ 207.5(C)
1970	—	\$ 207.5	\$ 6.9	\$ 6.9	214.4
1971	\$ 435.0	20.0	.7	7.6	222.0
1972	1,865.0	1,430.0	47.6	55.2	277.2
1973	2,118.0	253.0	8.5	63.7	340.9
1974	2,460.0	342.0	11.4	75.1	416.0
1975	2,710.0	250.0	8.3	83.4	499.4
1976	4,148.0	1,438.0	48.0	131.4	630.8
1977	5,362.0	1,214.0	40.4	171.8	802.6
1978	3,971.0	(1,391.0)	(46.4)	125.4	928.0
1979	4,225.0	254.0	8.5	133.9	1,061.9
1980	5,601.0	1,376.0	45.9	179.8	1,241.7
1981	5,858.0	257.0	8.5	188.3	1,430.0
1982	5,807.5	(50.5)	(1.6)	186.7	1,616.7
1983	5,059.0	(748.5)	(25.0)	161.7	1,778.4
1984	4,207.7	(851.3)	(28.4)	133.4	1,911.8

Assumptions:

- (A) Normal costs equal payments each year.
- (B) Select 30 years as the amortization period for prior-service costs to conform with the amortization period used by the Civil Service retirement plan.
- (C) One-half of the prior-service costs applicable to all years prior to 1970 (\$415 billion) has been fully amortized and the remainder (\$207.5 billion) is amortized over a 30-year period commencing in 1970.
- (D) The estimates of the present value of future unfunded benefits are based on the assumption that no workers would be covered in the future other than those who were age 18 and over as of September 30 of each fiscal year.
- (E) The annual non-cash provision represents the sum of the annual amortization amounts for current and prior years.

Appendix 5 (Continued)

		Percentage Increase Over Previous Year In Average Annual —				
Economic and Demographic Assumptions (A):	Year	Real GNP (B)	Earnings In Covered Employment	Consumer Price Index	Average Unemployment Rate (Percent)	Total Fertility Rates (C)
Optimistic Assumptions	1984	6.8	5.8	3.4	7.5	1.8
	1985	4.1	3.7	3.2	6.8	1.8
	1990	3.2	4.3	2.7	5.0	1.9
	2000	3.8	4.6	2.0	5.0	2.2
	2010 & Later	3.1	4.5	2.0	5.0	2.3
Intermediate II-A Assumptions	1984	6.8	5.6	3.4	7.5	1.8
	1985	3.9	3.9	3.6	6.8	1.8
	1990	2.8	4.5	3.2	5.5	1.8
	2000	3.1	5.1	3.0	5.5	2.0
	2010 & Later	2.5	5.0	3.0	5.5	2.0
Intermediate II-B Assumptions (D)	1984	6.8	5.3	3.4	7.5	1.8
	1985	3.2	3.8	3.9	6.9	1.8
	1990	2.5	5.2	4.2	6.0	1.8
	2000	2.6	5.6	4.0	6.0	2.0
	2010 & Later	2.0	5.5	4.0	6.0	2.0
Pessimistic Assumptions	1984	6.8	4.8	3.4	7.5	1.8
	1985	.7	3.1	4.8	7.4	1.8
	1990	4.0	7.1	4.6	7.9	1.7
	2000	1.9	6.1	5.0	7.0	1.6
	2010 & Later	1.4	6.0	5.0	7.0	1.6

(A) Table taken from the *Summary of the 1985 Annual Report of the Board of Trustees: Old Age Survivors, and Disability Insurance Program* issued by the Office of the Actuary, Social Security Administration.

(B) Gross National Product (the total output of goods and services) expressed in constant dollars. The percentage increase in real GNP is assumed to change after 2010. The values for 2060 are 3.2, 2.3, 1.9, and 0.6 percent for the optimistic, intermediate II-A, intermediate II-B, and pessimistic assumptions, respectively.

(C) The number of children who would be born to a woman in her lifetime based on the birth rates at each age in the year shown (if she were to survive the entire child-bearing).

(D) These assumptions were utilized to calculate the actuarial status of OASDI.

(E) Assumptions utilized to calculate the health insurance (Medicare or HI) portion of the tax rate are not included in the above summary.

Appendix 6

History of Accounting in the United States Government

- 1789 — The Treasury Act of 1789 was the first important legislation dealing with the fiscal authority of Congress, which created the Department of the Treasury. This Act established an auditor and comptroller within Treasury. Treasury was to submit an annual report to Congress.
- 1894 — The Dockery Act strengthened the centralized accounting functions in the Treasury Department and required that the annual combined statements of receipts and expenditures be given to Congress. The financial management system established by the Dockery Act endured, substantially unchanged, until enactment of the Budget and Accounting Act of 1921.
- 1921 — The Budget and Accounting Act made a number of important changes in the financial management of the Government, the most significant being the creation of the Bureau of the Budget and the General Accounting Office. The Bureau of the Budget was established within the Treasury Department to be administered by a Director who was responsible only to the President. The GAO was established independent of the Executive Branch. It became the auditing arm of Congress and also kept the ledger accounts for disbursing and collecting offices.
- 1933 — The President proposed that accounting should be the responsibility of the Executive Branch, and that auditing should remain the responsibility of the Legislative Branch.
- 1937 — The Senate commissioned The Brookings Institution to study the financial administration of the Government. The Brookings findings noted that "there exists no control over the preparation of Government financial statements."
- 1939 — The Bureau of the Budget was transferred from Treasury to the Executive Office of the President.
- 1947 — The Joint Program for Improving Accounting in the Federal Government (JPIAFG) was established. This was the forerunner of the present Joint Financial Management Improvement Program (JFMIP) which was established in 1948.
- 1949 — The first Hoover Commission recommended the creation of an "Accountant General" in Treasury to prescribe financial and administrative controls. The first Hoover Commission also recommended use of accrual accounting. Neither recommendation was implemented.
- 1949 — The Federal Property and Administrative Services Act was passed. This Act required the Administrator of the General Services Administration to work with the Comptroller General to formulate principles and standards for accounting for property and to aid in developing this segment of the accounting system.
- 1950 — The Budget and Accounting Procedures Act mandated the establishment and maintenance of accounting systems to the individual agencies. The GAO maintained its authority to prescribe accounting principles and standards. The GAO also was given the authority to approve the accounting systems of individual agencies, and GAO prescribed accounting principles and standards for agencies which required the use of accrual accounting to supplement the "obligation" basis of accounting in Government. GAO's primary function was now auditing. GAO would make audits of operations and report to Congress.
- 1956 — The second Hoover Commission made a strong recommendation for accrual accounting, and this led to Public Law 84-863, which required all Government agencies to install accrual accounting "as soon as practical." This loophole permitted agencies to essentially ignore GAAP-basis accrual accounting.
- 1967 — The President's Commission on Budget Concepts made several recommendations. The Commission recommended against a separate capital budget, but called for a unified budget that included the trust funds. The Commission recommended getting away from the singular concern with the bottom line of the budget (surplus or deficit) and emphasized the financing of the deficit. Most of its recommendations regarding the budget were adopted. However, the Commission also recommended accrual accounting and that the annual budget be presented on an accrued-expenditure basis. This recommendation was endorsed by two Presidents but was not implemented during their Administrations. Again, the Congress appeared to prefer the "obligation" type budget. Some improvements were made in accruals for the Government's yearend statements, but not always at the agency level.

Appendix 6 (Continued)

- 1970 — The President created the Office of Management and Budget to replace the Bureau of the Budget. The Legislative Reorganization Act directed OMB and Treasury to modernize budget and fiscal management through installation of a new EDP system. To date, this project is still in the planning phase.
- 1973 — The President transferred much of the Executive Branch responsibility for accounting and financial reporting from OMB to GSA. In addition, the GSA Administrator was made a member of the JFMIP.
- 1974 — The Congressional Budget and Impoundment Act created the Congressional Budget Office and a new budget committee for each house of Congress. The new budget committees and the Congressional Budget Office were charged with overseeing the Congress' work on the budget and insuring that the budget was reviewed as a whole and not just by individual appropriation. The new Congressional Budget Office was to be the OMB of the Legislative Branch — coordinating and assisting the work of the two Congressional budget committees.
- 1975 — U.S. Consolidated Financial Statements on a GAAP basis were first published. Arthur Andersen & Co., acting on its own initiative, began a study of U.S. Government accounting practices, leading to publication of first GAAP-basis financial statements. The following year, Treasury Secretary William E. Simon appointed the Advisory Committee on Federal Consolidated Financial Statements. The Committee developed a guide for preparing annual consolidated financial statements. The guide has been largely followed during ensuing years.
- 1976 — The Inspector General Act enhanced the independence, importance and scope of internal auditing in the U.S. Government.
- 1981 — OMB began a series of Circulars providing central direction and guidance on financial management matters. Key Circulars are:
- ☐ A-123 — Internal Control Systems
 - ☐ A-125 — Prompt Payment
 - ☐ A-127 — Financial Management Systems
 - ☐ A-128 — Audit of State and Local Governments
 - ☐ A-129 — Managing Federal Credit Programs
- 1982 — The Federal Managers' Financial Integrity Act required GAO to establish standards that were to be used by the heads of agencies in establishing and maintaining their agencies' systems of internal accounting and administrative controls. Agency heads were required to report annually whether their internal control systems fully comply with the internal control standards.
- 1984 — The Single Audit Act provided for "single audit" approach for state and local government. The Act ensured consistent policy for the audit of Federal financial assistance. This Act requires state and local governments to disclose whether their financial statements are prepared on a GAAP basis.
- 1984 — GAO issued revised Title II, establishing generally accepted accounting principles for the U.S. Government and its agencies.
- 1984 — The establishment of the Government Accounting Standards Board resolved the difficult issue of standard-setting for state and local governments. GAO, among others, supported GASB. GAO remains the standard-setting agency for U.S. Government accounting principles.
- 1985 — The Comptroller General's *Managing the Cost of Government* report described the Comptroller General's views of major issues in Federal financial management and proposals for improvement.
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Appendix 7

Accounting and Reporting Issues

The consolidated financial statements included in this booklet raise a number of accounting questions that should be addressed as appropriate accounting principles and financial reporting practices for national Government are refined.

- ☐ **The reporting entity** for the Government includes all Government-owned or sponsored activities, but excludes the Federal Reserve. Do these criteria best reflect the overall financial position and operating results of the Government?
 - ☐ **Social Security obligations** of the U.S. Government are accrued in the financial statements on the basis that the benefits have been provided to beneficiaries who, for the most part, are dependent upon such benefits and who believe they have earned such benefits through lifetime contributions. A Commission established by the U.S. Treasury in 1976 unanimously concluded that GAAP-basis financial statements should record the unfunded liability for Social Security. The amount, in effect, is equivalent to the personal savings that would otherwise have to be invested at the balance sheet date by program participants if the individuals themselves had to provide for their own retirement. While many believe that the Social Security program should be accounted for no differently than a welfare program, this ignores the fact that program participants pay reasonably determinable amounts and earn benefits based on the amounts paid in. Moreover, substantially all citizens will someday retire, whereas the population of future welfare participants is uncertain and the liability, if any, is not reasonably determinable. Among unresolved questions relating to Social Security are:
 - ☐ Would it be preferable to record the entire unfunded liability on the balance sheet and increase the accumulated deficit for the full amount — recording the additional \$2.3 trillion unamortized balance?
 - ☐ Is it appropriate to amortize increments and decrements in the unfunded liability over the 30-year period used in the Consolidated Financial Statements, or should they be recorded as operating transactions in the year in which they occur?
 - ☐ **Medicare** liabilities under the Social Security program are not accrued in the Consolidated Financial Statements. Since actuarial data for Medicare are essentially the same as for Social Security, should the present value of future benefits to be paid in excess of future revenues to be received be accrued as for Social Security?
 - ☐ **Veteran healthcare benefits** are not accrued in the financial statements. Should the estimated present value of these benefits be accrued?
 - ☐ **"Open-ended" programs**, described in Note 13 to the Consolidated Financial Statements, are not recognized on an accrual basis. Do these programs constitute liabilities for which the Government should accrue a present value?
 - ☐ **Environmental problems** frequently become the responsibility of Government. Does the responsibility for environmental clean-up constitute a liability for the Government and does the Government have an appropriate methodology to estimate its liabilities?
 - ☐ **New capital additions** (such as weapon systems and dams) usually entail additional costs for operation and maintenance once they are completed and placed in service. Should the estimated level of such future costs be disclosed for all capital additions budgeted or in process?
 - ☐ **Inflation** can materially impair the usefulness of financial statements. Should the Consolidated Financial Statements be prepared on an inflation-adjusted basis, and, if so, what would be the appropriate inflation accounting methodology?
 - ☐ **Gold** is reflected in the consolidated financial statements at \$42.22 per ounce. Should changes in the value of gold be recorded at each balance sheet date?
 - ☐ **Loss reserves** against receivables, and for contingencies under litigation and guarantees, are not recorded in full. What procedures should be used by the Government to evaluate more realistically its exposure to loss for doubtful receivable collection, and under various lending and insurance programs, and other commitments?
 - ☐ **Income taxes** are recorded as revenue based upon the date when payment of the tax is due to the Government. Would it be more appropriate to account for such taxes on the basis of when the Government's right to the revenue occurs? How can this be practically determined?
 - ☐ **Infrastructure** capital grants to state and local governments (\$23 billion in 1984) are not recorded as assets by the U.S. government. Do these grants for highways, water and wastewater plants, and other purposes constitute capital assets?
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