United States Government Notes to the Financial Statements for the Fiscal Years Ended September 30, 2019, and 2018

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

The government includes the executive branch, the legislative branch, and the judicial branch. This *Financial Report* includes the financial status and activities related to the operations of the government. SFFAS No. 47, *Reporting Entity* provides criteria for identifying organizations that are included in the *Financial Report* as “consolidation entities” and “disclosure entities.” Consolidation entities are consolidated into the government’s financial statements. For disclosure entities, information is disclosed in the notes to the financial statements concerning (a) the nature of the federal government’s relationship with the disclosure entities, (b) the nature and magnitude of relevant activity with the disclosure entities during the period and balances at the end of the period, and (c) a description of financial and non-financial risks, potential benefits and, if possible, the amount of the federal government’s exposure to gains and losses from the past or future operations of the disclosure entity or entities.

Disclosure entities have a greater degree of autonomy than consolidation entities. Disclosure entities may maintain a separate legal identity, have a governance structure that vests most decision-making authorities in a governing body to insulate the organization from political influence, and/or have relative financial independence. These entities may include, but are not limited to, quasi-governmental and/or financially independent entities and organizations owned and/or controlled by the federal government as a result of (a) regulatory actions (such as organizations in receivership or conservatorship) or (b) other federal government intervention actions if the relationship with such entities is not expected to be permanent.

SFFAS No. 47 also provides guidance for identifying related parties and in determining what information to provide about related party relationships of such significance that it would be misleading to exclude such information (see Appendix A—Reporting Entity, for a more detailed discussion).

Based on the criteria in GAAP for federal entities, the assets, liabilities, and results of operations of Fannie Mae and Freddie Mac are not consolidated into the government's consolidated financial statements. However, the values of the investments in such entities, changes in value, and related activity with these entities are included in the government's consolidated financial statements. Although federal investments in Fannie Mae and Freddie Mac are significant, these entities do not meet the GAAP criteria for consolidation entities.

Under SFFAS No. 47 criteria, Fannie Mae and Freddie Mac were owned or controlled by the federal government as a result of (a) regulatory actions (such as organizations in receivership or conservatorship) or (b) other federal government intervention actions. Under the regulatory or other intervention actions, the relationship with the federal government is not expected to be permanent. These entities are classified as disclosure entities based on their characteristics as a whole (see Note 25—Disclosure Entities and Related Parties for additional information on these disclosure entities).

Also, under GAAP criteria, the FR System is not consolidated into the government's consolidated financial statements (see Note 25—Disclosure Entities and Related Parties for further information concerning the FR System).

For further information regarding Reporting Entity, see Appendix A—Reporting Entity.

B. Basis of Accounting and Revenue Recognition

Consolidated Financial Statements

The consolidated financial statements of the government were prepared using GAAP, primarily based on FASAB's SFFAS. Intragovernmental transactions are eliminated in consolidation, except as described in the Other Information–Unmatched Transactions and Balances. See Note 1.R—Unmatched Transactions and Balances for detailed information. The consolidated financial statements include accrual-based financial statements and sustainability financial statements, which are discussed in more detail below, and the related notes to the consolidated financial statements. Collectively, the accrual-based financial statements, the sustainability financial statements, and the notes represent basic information that is deemed essential for the financial statements and notes to be presented in conformity with GAAP.

Accounting standards allow certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information. Accordingly, modifications may have been made to certain presentations and disclosures.

Accrual-Based Financial Statements

The accrual-based financial statements were prepared under the following principles:

- Expenses are generally recognized when incurred.
- Non-exchange revenue, including taxes, duties, fines, and penalties, are recognized when collected and adjusted for the change in net measurable and legally collectible amounts receivable (modified cash basis). Related refunds and other offsets, including those that are measurable and legally payable, are netted against non-exchange revenue.
- Exchange (earned) revenue is recognized when the government provides goods and services to the public for a price. Exchange revenue includes user charges such as admission to federal parks and premiums for certain federal insurance.

The basis of accounting used for budgetary purposes, which is primarily on a cash basis (budget deficit) and follows budgetary concepts and policies, differs from the basis of accounting used for the financial statements which follow GAAP. See the Reconciliations of Net Operating Cost and Budget Deficit in the Financial Statements section.

Sustainability Financial Statements

The sustainability financial statements were prepared based on the projected present value of the estimated future revenue and estimated future expenditures, primarily on a cash basis, for a 75 year period.[1] They include the SLTFP, covering all federal government programs, and the SOSI and the SCSIA, covering social insurance programs (Social Security, Medicare, Railroad Retirement, and Black Lung programs). These estimates are based on economic as well as demographic assumptions presented in Notes 22—Social Insurance and 23—Long-Term Fiscal Projections. The sustainability financial statements are not forecasts or predictions. The sustainability financial statements are designed to illustrate the relationship between receipts and expenditures, if current policy is continued. For this purpose, the projections assume, among other things, that scheduled social insurance benefit payments would continue after related trust funds are projected to be depleted, contrary to current law, and that debt could continue to rise indefinitely without severe economic consequences.

By accounting convention, General Fund transfers to Medicare Parts B and D reported in the SOSI are eliminated when preparing the governmentwide consolidated financial statement. The SOSI shows the projected General Fund transfer(s) as eliminations that, under current law, would be used to finance the remainder of the expenditures in excess of revenues for Medicare Parts B and D that is reported in the SOSI. The SLTFP include all revenues (including general revenues) of the federal government.

New Standards Issued in Prior and Current Years and Implemented in Current Year

Beginning in fiscal year 2019, the government implemented the requirements of new standards for: P3s, Insurance Programs, BAR, Amending Inter-Entity Cost Provisions, and Omnibus Amendments. The new standards implemented are:

- SFFAS No. 49, *Public-Private Partnerships: Disclosure Requirements*. P3s are defined as "risk sharing" arrangements or transactions lasting more than five years between public and private sector entities. SFFAS No. 49 requires for P3s that meet its criteria to disclose a general description of P3 arrangements or transactions, the consolidated amounts the government received and paid during the reporting period(s) and consolidated amounts the government estimated to be received and paid in aggregate over the expected life of the P3s, and a reference to

[1] With the exception of the Black Lung program, which has a rolling 25-year projection period that begins on the September 30 valuation date each year.

applicable component entity reports for additional information in the *Financial Report*. SFFAS No. 49 became effective in fiscal year 2019.

- SFFAS No. 51, *Insurance Programs*. SFFAS No. 51 establishes accounting and financial reporting standards for insurance programs. It identifies three categories: 1) exchange transaction insurance programs other than life insurance, 2) non-exchange transaction insurance programs and 3) life insurance programs. For each category, SFFAS No. 51 provides specific accounting and reporting requirements. SFFAS No. 51 requires certain disclosures including, a broad description of insurance programs and related liabilities, in the *Financial Report*. SFFAS No. 51 became effective in fiscal year 2019.
- SFFAS No. 53, *Budget and Accrual Reconciliation; Amending SFFAS No. 7, and 24 and Rescinding SFFAS No. 22*. SFFAS No. 53 amends component entity requirements for a reconciliation between budgetary and financial accounting information established by SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. To increase informational value and usefulness, and to support the governmentwide financial statement reconciling net operating cost to the budget deficit, this Statement provides for the BAR to replace the Statement of Financing. The BAR explains the relationship between the entity's net outlays on a budgetary basis and the net cost of operations during the reporting period. The BAR starts with net cost of operations and is adjusted by components of net cost that are not part of net outlays, components of net outlays that are not part of net cost, and other temporary timing differences, which reflect some special adjustments. SFFAS No. 53 became effective in fiscal year 2019.
- SFFAS No. 55, *Amending Inter-Entity Cost Provisions*. SFFAS No. 55 revises SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts* (including Interpretation 6*, Accounting for Imputed Intra-departmental Costs: An Interpretation of SFFAS No. 4*). SFFAS No. 4 required component reporting entities to recognize the full costs of services received from other federal reporting entities even if there was no requirement to reimburse the providing entity for the full cost of such services. This Statement revises SFFAS No. 4 to provide for the continued recognition of significant inter-entity costs by business-type activities and rescinds the following: a) SFFAS No. 30, *Inter-Entity Cost Implementation: Amending SFFAS No. 4, Managerial Cost Accounting Standards and Concepts* and b) Interpretation 6*, Accounting for Imputed Intra-departmental Costs: An Interpretation of SFFAS No. 4*. Recognition of imputed inter-entity costs by activities that are not business-type activities is not required with the exception of imputed inter-entity costs for personnel benefits and the Treasury Judgment Fund settlements or as otherwise directed by the OMB. Notwithstanding the absence of a requirement, non-business-type activities may elect to recognize imputed cost and corresponding imputed financing for other types of inter-entity costs. Component reporting entities should disclose that only certain inter-entity costs are recognized for goods and services that are received from other federal entities at no cost or at a cost less than the full costs. SFFAS No. 55 does not have a significant impact on the U.S. government's consolidated financial statements. SFFAS No. 55 became effective in fiscal year 2019.
- SFFAS No. 57, *Omnibus Amendments 2019*. SFFAS No. 57 revises paragraph 26 of SFFAS No. 6, *Accounting for Property, Plant and Equipment* to remove the reference of "material amounts" from the last bulleted item. Materiality applies to all of the bulleted items in SFFAS No. 6, paragraph 26. This portion of SFFAS No. 57 was effective upon issuance in fiscal year 2019, but it does not have a significant impact on the U.S. government's consolidated financial statements.

In fiscal year 2016, the government began implementing the requirements of new standards related to the reporting for Inventories and Related Property and PP&E. The standards being implemented are:

- FASAB issued SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials.* SFFAS No. 48 permits a reporting entity to apply an alternative valuation method in establishing opening balances and applies when a reporting entity is presenting financial statements or one or more line items addressed by this statement. This standard can be applied for the first time or after a period during which existing systems could not provide the information necessary for producing GAAP-based financial statements without use of the alternative valuation methods. This is intended to provide an alternative method to adoption of GAAP when historical records and systems do not provide a basis for valuation of opening balances in accordance with SFFAS No. 3, *Accounting for Inventory and Related Property.* This application is available to each reporting entity only once per line item addressed in this statement. Reporting entities that meet either condition and elect to apply this statement should follow the guidance in SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles.* SFFAS No. 48 was effective beginning in fiscal year 2017. Early implementation was permitted. DOD did partially implement in 2016 and select component entities have continued to implement in 2017, 2018, and 2019. DOD has not declared full implementation yet.

- FASAB issued SFFAS No. 50, *Establishing Opening Balances for General Property, Plant and Equipment.* SFFAS No. 50 permits a reporting entity to apply an alternative valuation method in establishing opening balances and applies when a reporting entity is presenting financial statements or one or more line items addressed by this statement. This standard can be applied for the first time or after a period during which existing systems could not provide the information necessary for producing GAAP-based financial statements without use of the alternative valuation methods. This is intended to provide an alternative method to adoption of GAAP when historical records and systems do not provide a basis for valuation of opening balance in accordance with SFFAS No. 6, *Accounting for Property, Plant, and Equipment*. This application is available to each reporting entity only once per line item addressed in this statement. Reporting entities meeting the conditions and electing to apply this statement should follow the guidance in SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles.* SFFAS No. 50 was effective beginning in fiscal year 2017. Early implementation was permitted. DOD did partially implement in 2016 and select component entities have continued to implement in 2017, 2018, and 2019. DOD has not declared full implementation yet.

New Standards Issued and Not Yet Implemented

FASAB issued the following new standards that are applicable to the *Financial Report*, but are not yet implemented at the governmentwide level for fiscal year 2019:

- In April 2018, FASAB issued SFFAS No. 54, *Leases: An Amendment of SFFAS No. 5, Accounting for Liabilities of the Federal Government, and* SFFAS No. 6*, Accounting for Property, Plant, and Equipment*. SFFAS No. 54 revises the financial reporting standards for federal lease accounting. It provides a comprehensive set of lease accounting standards to recognize federal lease activities in the reporting entity's financial statements and includes appropriate disclosures. This Statement requires that federal lessees (for other than intragovernmental leases) recognize a lease liability and a leased asset at the commencement of the lease term, unless it meets any of the scope exclusions or the definition/criteria of short-term leases, or contracts or agreements that transfer ownership, or intragovernmental leases. A federal lessor would recognize a lease receivable and deferred revenue, unless it meets any of the scope exclusions or the definition/criteria or short-term leases, contracts or agreements that transfer ownership, or intragovernmental leases. SFFAS No. 54 is effective in fiscal year 2021 and early implementation is not permitted.
- In September 2019, FASAB issued SFFAS No. 57, *Omnibus Amendments 2019*. SFFAS No. 57 eliminates the RSSI category by rescinding SFFAS No. 8, *Supplementary Stewardship Reporting* in its entirety. The elimination of the RSSI category is effective in fiscal year 2020. Early adoption is not permitted.

C. Accounts and Taxes Receivable

Accounts receivable represent claims to cash or other assets from entities outside the government that arise from the sale of goods or services, duties, fines, certain license fees, recoveries, or other provisions of the law. Accounts receivable are reported net of an allowance for uncollectible amounts. An allowance is established when it is more likely than not the receivables will not be totally collected. The allowance method varies among the entities in the government and is usually based on past collection experience and is reestimated periodically as needed. Methods include statistical sampling of receivables, specific identification and intensive analysis of each case, aging methodologies, and percentage of total receivables based on historical collection.

Taxes receivable consist primarily of uncollected tax assessments, penalties, and interest when taxpayers have agreed or a court has determined the assessments are owed. Taxes receivable do not include unpaid assessments when taxpayers or a court have not agreed that the amounts are owed (compliance assessments) or the government does not expect further collections due to factors such as the taxpayer's death, bankruptcy, or insolvency (write-offs). Taxes receivable are reported net of an allowance for the estimated portion deemed to be uncollectible. The allowance for uncollectible amounts represents the difference between gross taxes receivable and the amounts estimated to be collectible.

D. Loans Receivable and Loan Guarantee Liabilities

Direct loans obligated and loan guarantees committed after fiscal year 1991 are reported based on the present value of the net cash flows estimated over the life of the loan or guarantee. The difference between the outstanding principal of the direct loans and the present value of their net cash inflows is recognized as a subsidy cost allowance. The present value of estimated net cash flows of the loan guarantees is recognized as a liability for loan guarantees.

The subsidy expense for direct or guaranteed loans disbursed during a fiscal year is the present value of estimated net cash flows for those loans or guarantees. For the fiscal year during which new direct or guaranteed loans are disbursed, the components of the subsidy expense of those new direct loans and loan guarantees are recognized separately among interest subsidy costs, default costs, fees and other collections, and other subsidy costs. Credit programs reestimate the subsidy cost allowance for outstanding direct loans and the liability for outstanding loan guarantees, by taking into account all factors that may have affected the estimated cash flows. Any adjustment resulting from the reestimates is recognized as a subsidy expense (or a reduction in subsidy expense).

Direct loans obligated and loan guarantees committed before fiscal year 1992 are valued under two different methodologies within the government: the allowance-for-loss method and the present-value method. Under the allowance-for-loss method, the outstanding principal of direct loans is reduced by an allowance for uncollectible amounts; the liability for loan guarantees is the amount the entity estimates would more likely than not require future cash outflow to pay default claims. Under the present-value method, the outstanding principal of direct loans is reduced by an allowance equal to the difference between the outstanding principal and the present value of the expected net cash flows. The liability for loan guarantees is the present value of expected net cash outflows due to the loan guarantees.

E. Inventories and Related Property

Inventory is tangible personal property that is (1) held for sale, principally to federal entities, (2) in the process of production for sale, or (3) to be consumed in the production of goods for sale or in the provision of services for a fee. OM&S is tangible personal property to be consumed in normal operations and stockpile materials are strategic and critical materials being held due to statutory requirements for use in national defense, conservation, or national emergencies.

SFFAS No. 3, *Accounting for Inventory and Related Property*, requires that inventories, OM&S, and stockpile materials to be valued using either historical cost or a method that reasonably approximates historical cost. Historical cost methods include first-in-first-out, weighted average, and moving average. Any other valuation method may be used if the results reasonably approximate one of the historical cost methods. FASAB issued additional guidance SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*, which permits a reporting entity to apply an alternative valuation method in establishing opening balances for inventory, OM&S, and stockpile materials and is intended to provide an alternative valuation method when historical records and systems do not provide a basis for valuation of opening balances in accordance with SFFAS No. 3.

As the largest contributor of inventories and related property, DOD values substantially all of its inventory available and purchased for resale using the moving average cost method as of September 30, 2019. OM&S are valued using various methods including moving average cost, standard price, historical cost, replacement price, and direct method. DOD uses both the consumption method (expensed when issued to an end user for consumption in normal operations) and the purchase method (expensed when purchased) of accounting for OM&S. Stockpile Materials are accounted for using actual cost or the lower of cost or market method. DOD continues to implement SFFAS No. 48, permitting alternative methods in establishing opening balances.

F. Property, Plant, and Equipment

PP&E consists of tangible assets that have an estimated useful life of two or more years, are not intended for sale in the ordinary course of business and are intended to be used or available for use by the entity. These tangible assets may include land, land rights, assets acquired through capital leases, buildings and structures, furniture and fixtures, equipment, and vehicles.

SFFAS No. 6, *Accounting for Property, Plant, and Equipment* requires general PP&E to be recorded at cost. Cost shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use. PP&E used in government operations are carried at acquisition cost, with the exception of some DOD equipment. FASAB issued additional guidance, SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment,* which states that a reporting entity may choose one of three alternative methods for establishing an opening balance for PP&E. The alternative methods include: using deemed cost to establish opening balances of general PP&E, selecting between deemed cost and prospective capitalization of internal use software, and allowing an exclusion of land and land rights from opening balances with disclosure of acreage information and expensing of future acquisitions.

By excluding land and land rights from the opening balance of general PP&E future land and land right acquisitions should be expensed. An entity electing to exclude land and land rights from its general PP&E opening balances must disclose, with a reference on the balance sheet to the related disclosure, the number of acres held at the beginning of each reporting period, the number of acres added during the period, the number of acres disposed of during the period, and the number of acres held at the end of each reporting period. DOD generally records PP&E at the estimated historical cost. However, when applicable DOD will continue to adopt SFFAS No. 50.

Costs to acquire PP&E, extend the useful life of existing PP&E, or enlarge or improve its capacity, that exceed federal entities' capitalization thresholds should be capitalized and depreciated or amortized. Depreciation and amortization expense should be recognized on all capitalized PP&E, except land and land rights of unlimited duration. In the case of constructed PP&E, the PP&E shall be recorded as construction work in process until it is placed in service, at which time the balance is transferred to PP&E.

For financial reporting purposes, heritage assets (excluding multi-use heritage assets) and stewardship land are not recorded as part of PP&E. Since heritage assets are intended to be preserved as national treasures, it is anticipated that they will be maintained in reasonable repair and that there will be no diminution in their usefulness over time. Many assets are clearly heritage assets. For example, the National Park Service manages the Washington Monument, the Lincoln Memorial and the Mall. Heritage assets that are predominantly used in general government operations are considered multi-use heritage assets and are included in PP&E. Stewardship land is also consistent with the treatment of heritage assets in that much of the government's land is held for the general welfare of the nation and is intended to be preserved and protected. Stewardship land is land owned by the government but not acquired for or in connection with general PP&E. Because most federal land is not directly related to general PP&E, it is deemed to be stewardship land and accordingly, it is not reported on the Balance Sheet. Examples of stewardship land include national parks and forests. For more details on stewardship assets, see Note 24—Stewardship Land and Heritage Assets.

G. Debt and Equity Securities

Most debt and equity securities are held by component entities that apply FASB standards and are not converted to FASAB standards in consolidation. Certain other securities held by component entities that apply FASB standards are classified as held-to-maturity, available-for-sale, and trading. Held-to-maturity debt and equity securities are reported at cost, net of unamortized premiums and discounts. Available-for-sale debt and equity securities are reported at fair value. Trading debt and equity securities are reported at fair value. The investment categories are classified by security type; Non-U.S. government, mortgage/asset backed, commercial, corporate and other bonds, unit trust and common stocks. Entities that apply FASB standards are reported by fair value measurement hierarchy levels 1, 2, 3, and "other" category.

H. Investments in Government-Sponsored Enterprises

The senior preferred stock and associated warrants for the purchase of common stock in the GSEs (Fannie Mae and Freddie Mac) are presented at their fair value. SPSPAs, which Treasury entered into with each GSE when they were placed under conservatorship, can result in payments to the GSEs when, at the end of any quarter, the FHFA, acting as the conservator, determines that the liabilities of either GSE exceed its respective assets. Such payments result in an increase to the investment in the GSEs' senior preferred stock, with a corresponding decrease to cash held by Treasury. In addition, the investments in the GSEs will increase, based on the quarterly earnings of the GSEs, up to the adjusted capital reserve amounts set for each GSE.

The valuation to estimate the investment's fair value incorporates forecasts, projections, and cash flow analyses. Changes in valuation, including impairments, are deemed usual and recurring and thus are recorded as exchange transactions on the Statement of Net Cost and investments in GSEs on the Balance Sheet. The government also records dividends related to these investments as exchange transactions and accrues when declared.

The potential liabilities to the GSEs, if any, are assessed annually and recorded at the gross estimated amount. For more detailed information on investments in GSEs, refer to Note 8—Investments in Government-Sponsored Enterprises.

I. Federal Debt

U.S. Treasury securities are debt instruments issued to raise money needed to operate the federal government and pay off maturing obligations. Treasury issues these debt instruments to the public in the form of marketable bills, notes, bonds, TIPS and FRNs, and in the form of non-marketable securities including Government Account Series securities, U.S. Savings

Securities, and State and Local Government Series securities. The amount of the debt, or principal, is also called the security's face value or par value. To accurately reflect the federal debt, Treasury records principal transactions with the public at par value at the time of the transaction. Certain Treasury securities are issued at a discount or premium. These discounts and premiums are amortized over the term of the security using an interest method for all long-term securities and the straight line method for short-term securities. In addition, the principal for TIPS is adjusted daily over the life of the security based on the CPI-U; and FRNs pay interest quarterly based on the interest rate at the time of payment. Accrued interest on Treasury securities held by the public is recorded as an expense when incurred, instead of when paid.

J. Federal Employee and Veteran Benefits Payable

Generally, federal employee and veteran benefits payable are recorded during the time employee services are rendered. The related liabilities for defined benefit pension plans, veterans' compensation, burial, education and training benefits, post-retirement health benefits, and post-retirement life insurance benefits, are recorded at estimated present value of future benefits, less any estimated present value of future normal cost contributions. Normal cost is the portion of the actuarial present value of projected benefits allocated as an expense for employee services rendered in the current year. Actuarial gains and losses (as well as prior service cost, if any) are recognized immediately in the year they occur without amortization.

VA also provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews, if the veteran died or was disabled for nonservice-related causes. The pension program for veterans is not accounted for as a "federal employee pension plan" under SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, due to differences between its eligibility conditions and those of federal employee pensions. Therefore, a future liability for pension benefits is not recorded. These benefits are recognized as expenses when benefits are paid rather than when employee services are rendered.

The actuarial liability for FECA benefits is recorded at estimated present value of future benefits for injuries and deaths that have already been incurred.

Gains and losses from changes in long-term assumptions used to estimate federal employee pensions, ORB, and OPEB liabilities are reflected separately on the Statement of Net Cost and the components of the expense related to federal employee pension, ORB, and OPEB liabilities are disclosed in Note 12—Federal Employee and Veteran Benefits Payable as prescribed by SFFAS No. 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*. In addition, SFFAS No. 33 also provides a standard for selecting the discount rate assumption for present value estimates of federal employee pension, ORB, and OPEB liabilities.

K. Environmental and Disposal Liabilities

Environmental and disposal liabilities are recorded at the estimated current cost of the cleanup plan, including the level of restoration to be performed, the current legal or regulatory requirements, and the current technology. Cleanup costs are the costs of removing, containing or disposing of hazardous waste. Hazardous waste is a solid, liquid, or gaseous waste that, because of its quantity or concentration, presents a potential hazard to human health or the environment. Cleanup costs include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, closure, and post-closure costs. Where technology does not exist to clean up radioactive or hazardous waste, only the estimable portion of the liability (typically monitoring and safe containment) is recorded.

L. Insurance and Guarantee Program Liabilities

Insurance programs are authorized by law to financially compensate a designated population of beneficiaries by accepting all or part of the risk for losses incurred as a result of an adverse event. Certain consolidation entities with significant insurance and guarantee programs (i.e., PBGC and FDIC) apply FASB standards, and are not converted to FASAB standards in the consolidated financial statements of the U.S. government. The two most significant FASB-based insurance and guarantee programs are provided by PBGC and FDIC.

PBGC recognizes a single-employer program liability for probable plan terminations, which represents PBGC's best estimate of the losses, net of plan assets, and the present value of expected recoveries (from sponsors and members of their controlled group) for plans that are likely to terminate in the future. PBGC recognizes a multi-employer program liability for future financial assistance to insolvent plans and to plans deemed probable to becoming insolvent.

FDIC records a liability for FDIC-insured institutions that are likely to fail when the liability is probable and reasonably estimable, absent some favorable event such as obtaining additional capital or merging. The FDIC liability is derived by applying expected failure rates and loss rates to the institutions based on supervisory ratings, balance sheet characteristics, and projected capital levels.

PBGC's exposure to losses from plan terminations and FDIC's exposure to losses from insured institutions that are classified as reasonably possible are disclosed in Note 18—Contingencies.

All other insurance and guarantee programs are accounted for in the consolidated financial statements in accordance with FASAB standards. For fiscal year 2019, insurance programs are accounted for pursuant to SFFAS No. 51, *Insurance Programs.*

Programs that administer direct loans and loan guarantees, qualify as social insurance, authorized to engage in disaster relief activities, provide grants, provide benefits or assistance based on an individual's or a household income and/or assets, assume the risk of loss arising from federal government operations, that pay claims through an administrative or judicial role for individuals or organizations who claim they have been harmed by a federal entity, that indemnify contractors, agreement partners, and other third parties for loss or damage incurred while or caused by work performed for a federal entity, or workers' or occupational illness compensation programs that compensate current or former employees (or survivors) and certain third parties for injuries and occupational diseases obtained while working for a federal entity are excluded from insurance programs.

SFFAS No. 51 establishes three categories: 1) exchange transaction insurance programs other than life insurance, 2) non-exchange transaction insurance programs and 3) life insurance programs. For each category, SFFAS No. 51 provides specific accounting and reporting requirements. The implementation of SFFAS No. 51 did not have a significant effect on the beginning net position.

For exchange transaction insurance programs other than life insurance, revenues are recognized when earned over the insurance arrangement period and liabilities are recognized for unearned premiums, unpaid insurance claims, and for losses on remaining coverage. Losses on remaining coverage represent estimated amounts to be paid to settle claims for the period after year-end through the end of insurance coverage in excess of the summation of unearned premiums and premiums due after the end of the reporting period.

For non-exchange transaction insurance programs, revenue is recognized the same as other non-exchange transaction revenue, no unearned premium liability is recorded and a liability is only recognized for unpaid insurance claims.

For life insurance programs, revenue is recognized when due and liabilities are recognized for unpaid insurance claims and future policy benefits. The liability for future policy benefits represents the expected present value of future claims to be paid to, or on behalf of, existing policyholders, less the expected present value of future net premiums to be collected from those policyholders. Life insurance programs are disclosed in Note 12—Federal Employee and Veteran Benefits Payable.

In fiscal year 2018, for insurance and guarantee programs accounted for pursuant to FASAB standards, a liability is recognized for unpaid claims resulting from insured events that have occurred as of the reporting date, including contingencies meeting the recognition criteria. Life insurance programs recognize a liability for future policy benefits (a liability to current policyholders that relates to insured events, such as death or disability) in addition to the liability for unpaid claims incurred.

M. Deferred Maintenance and Repairs

DM&R are maintenance and repairs that were not performed when they should have been or scheduled maintenance and repairs that were delayed or postponed. Maintenance is the act of keeping fixed assets in acceptable condition, including preventative maintenance, normal repairs, and other activities needed to preserve the assets, so they continue to provide acceptable service and achieve their expected life. Maintenance and repairs exclude activities aimed at expanding the capacity of assets or otherwise upgrading them to serve needs different from those originally intended. DM&R are not expensed in the Statements of Net Cost or accrued as liabilities on the Balance Sheet. However, DM&R information is disclosed in the unaudited RSI section of this report. Please see unaudited RSI—Deferred Maintenance and Repairs for additional information including measurement methods.

N. Contingencies

Liabilities for contingencies are recognized on the Balance Sheet when both:

- A past transaction or event has occurred, and
- A future outflow or other sacrifice of resources is probable and measurable.

The estimated contingent liability may be a specific amount or a range of amounts. If some amount within the range is a better estimate than any other amount within the range, then that amount is recognized. If no amount within the range is a better estimate than any other amount, then the minimum amount in the range is recognized and the range and a description of the nature of the contingency is disclosed.

Contingent liabilities that do not meet the above criteria for recognition, but for which there is at least a reasonable possibility that a loss may be incurred, are disclosed in Note 18—Contingencies.

O. Commitments

In the normal course of business, the government has a number of unfulfilled commitments that may require the use of its financial resources. Note 19—Commitments describes the components of the government's actual commitments that are disclosed due to their nature and/or their amount. They include long-term leases, undelivered orders, and other commitments.

P. Social Insurance

A liability for social insurance programs (Social Security, Medicare, Railroad Retirement, Black Lung, and Unemployment) is recognized for any unpaid amounts currently due and payable to beneficiaries or service providers as of the reporting date. No liability is recognized for future benefit payments not yet due. For further information, see Note 22—Social Insurance and the unaudited RSI—Social Insurance section.

Q. Funds from Dedicated Collections

Generally, funds from dedicated collections are financed by specifically identified revenues, provided to the government by non-federal sources, often supplemented by other financing sources that remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes, and must be accounted for separately from the government's general revenues. The three required criteria for a fund from dedicated collections are:

- A statute committing the government to use specifically identified revenues and/or other financing sources that are originally provided to the government by a non-federal source only for designated activities, benefits, or purposes;
- Explicit authority for the fund to retain revenues and/or other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and
- A requirement to account for and report on the receipt, use, and retention of the revenues and/or other financing sources that distinguishes the fund from the government's general revenues.

For more details on funds from dedicated collections, see Note 20—Funds from Dedicated Collections.

R. Unmatched Transactions and Balances

The reconciliation of the change in net position requires that the difference between ending and beginning net position equals the difference between revenue and cost, plus or minus prior-period adjustments.

The unmatched transactions and balances are needed to bring the change in net position into balance. The primary factors affecting this out of balance situation are:

- Unmatched intragovernmental transactions and balances between federal entities; and
- Errors and restatements in federal entities reporting.

As intragovernmental transactions and balances reduce to immaterial amounts, the corresponding individual lines in the Unmatched Transactions and Balances table are adjusted to remove the differences for the fiscal year. Please refer to the table of Unmatched Transactions and Balances in Other Information (Unaudited) for examples of the individual lines. Materiality for these adjustments is considered in the absolute value, when at or below $0.1 billion.

Refer to the Other Information (unaudited)—Unmatched Transactions and Balances for detailed information.

S. Adjustments to Beginning Net Position

Adjustments to beginning net position in fiscal year 2019 had a consolidated change of $13.0 billion. This $13.0 billion increase was recognized under Funds other than those from Dedicated Collections ($5.7 billion and $7.3 billion).

Adjustments to beginning net position in fiscal year 2018 had a consolidated change of $0.1 billion. This $0.1 billion net increase includes a decrease of $22.5 billion under Funds other than those from Dedicated Collections ($2.5 billion, $11.0 billion and $9.0 billion) and an increase of $22.6 billion under Funds from Dedicated Collections ($2.6 billion, $11.0 billion and $9.0 billion).

DOD reported adjustments to beginning net position impacting the financial statements. DOD reported an increase of $5.7 billion and a decrease of $2.5 billion in fiscal year 2019 and 2018, respectively, to beginning net position due to continuing implementation of SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials* and SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment*.

DOD followed SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles*, and corrected an error in its financial statements for assets and net position. During fiscal year 2019, DOD reported adjustments to beginning net position of $7.3 billion.

SFFAS No. 47, *Reporting Entity,* was implemented in fiscal year 2018. The standard requires that consolidation entities be consolidated in their entirety. Prior to fiscal year 2018, only the federal portion of Smithsonian Institution was consolidated. For fiscal year 2018, all activities (federal and non-federal portions) of Smithsonian Institution were consolidated, resulting in a $2.6 billion adjustment to the fiscal year 2018 beginning net position.

In fiscal year 2018 the adjustments to beginning net position for Smithsonian Institution of $2.6 billion related to dedicated collection funds. Note 20—Funds from Dedicated Collections had an adjustment to beginning net position for fiscal year 2018 of $11.0 billion related to DOD. Additional amounts totaling $9.0 billion were restated to improve the consistency of entities combined presentation and intradepartmental eliminations. Both adjustments were only between Funds from dedicated collections and Funds other than those from dedicated collections with no effect on the consolidated total. Refer to Note 20—Funds from Dedicated Collections for additional information.

T. Reclassifications

Certain fiscal year 2018 amounts were reclassified to conform to the fiscal year 2019 presentation. The reclassified data is addressed in Note 5—Inventories and Related Property, Net. Refer to the individual note for more information.

U. Restatements

In fiscal year 2019, the presentation methodology for Statement of Operations and Changes in Net Position and Note 20—Funds from Dedicated Collections was changed to provide consistency among all entities. For comparative purposes, fiscal year 2018 was also restated. This restatement was primarily related to an increase in the total amount of federal assets and federal liabilities reported for Funds from Dedicated Collections. Refer to Note 1.S—Adjustments to Beginning Net Position and Note 20—Funds from Dedicated Collections for more information.

In fiscal year 2019, DOD brought offline adjustments from published component AFRs into its reporting system for 2018. This correction resulted in the restatement of Balance Sheet lines Other liabilities ($0.1 billion decrease), Funds from Dedicated Collections net position ($11.0 billion increase), and Funds other than those from Dedicated Collections ($11.0 billion decrease). The Net position, beginning of period on the Statement of Operations and Changes in Net Position was restated by $0.1 billion. The Other Liabilities ($0.1 billion decrease) is also reflected in Note 16—Other Liabilities and the Reconciliation of Net Operating Cost and Budget Deficit. Refer to the individual notes for more information.

Also, in fiscal year 2019 errors were noted in the presentation of Note 19—Commitments for operating leases and other commitments that required correction of balances reported in fiscal year 2018. The corrections resulted in the restatement of prior year amounts for DOT's other commitments ($6.4 billion increase) and VA's operating leases ($3.9 billion increase). Refer to Note 19—Commitments for more information.

In addition, in fiscal year 2019 Smithsonian Institution had a 2018 restatement between the Balance Sheet lines Note 9—Other Assets and Note 7—Debt and Equity Securities of $1.9 billion. The $1.9 billion is also reflected on the Debt and equity securities and Other assets lines on the Reconciliations of Net Operating Cost and Budget Deficit. Also, Note 4—Loans Receivable and Loan Guarantee Liabilities, Net 2018 subsidy expense/(income), principal amounts of loans under guarantee, and principal amounts guaranteed by the U.S. have been restated to provide consistency among credit reform entities. In addition, Note 18—Contingencies restated the 2018 estimated range of loss for reasonably possible contingencies for DOE. Refer to the notes for more information.

V. Fiduciary Activities

Fiduciary activities are the collection or receipt, as well as the management, protection, accounting, investment and disposition by the government of cash or other assets in which non-federal individuals or entities have an ownership interest that the government must uphold. Fiduciary cash and other fiduciary assets are not assets of the government and are not recognized on the Balance Sheet. See Note 21—Fiduciary Activities, for further information.

W. Use of Estimates

The government has made certain estimates and assumptions relating to the reporting of assets, liabilities, revenues, expenses, and the disclosure of contingent liabilities to prepare these financial statements. There are a large number of factors that affect these assumptions and estimates, which are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. As such, actual results will differ from these estimates and such differences may be material.

Significant transactions subject to estimates are included in the balance of loans and credit program receivables, federal employee and veteran benefits payable, credit reform subsidy costs, investments in GSEs, and other non-federal securities and related impairment, tax receivables, loan guarantees, depreciation, imputed costs, other actuarial liabilities, cost and earned revenue allocations, as well as contingencies and any related recognized liabilities.

The government recognizes the sensitivity of credit reform modeling to slight changes in some model assumptions and uses regular review of model factors, statistical modeling, and annual reestimates to reflect the most accurate cost of the credit programs to the U.S. government. *Federal Credit Reform Act of 1990* loan receivables and loan guarantees are disclosed in Note 4—Loans Receivable and Loan Guarantee Liabilities, Net.

The forecasted future cash flows used to determine credit reform amounts are sensitive to slight changes in model assumptions, such as general economic conditions, specific stock price volatility of the entities in which the government has an equity interest, estimates of expected default, and prepayment rates. Therefore, forecasts of future financial results have inherent uncertainty.

The annual valuation performed as of September 30 on the senior preferred stock and warrants comprising the Investments in GSEs line item on the Balance Sheets incorporates various forecasts, projections, and cash flow analyses to develop an estimate of the asset's fair value. The value of the senior preferred stock is estimated by first estimating the fair value of the total equity of each GSE (which, in addition to the senior preferred stock, is comprised of other equity instruments including common stock, common stock warrants, and junior preferred stock). The fair value of the total equity is based on a discounted cash flow valuation methodology, whereby the primary input is the present value of the projected quarterly cash flows to equity holders. The fair value of the GSEs' other equity instruments are then deducted from its total equity, with the remainder representing the fair value of the senior preferred stock. The primary input into the warrants valuation is the market value of the shares of common stock of the GSEs which, along with the junior preferred stock, are traded on the OTC Bulletin Board. Treasury evaluates the need for adjusting the OTC market-based valuation of the warrants for the effects, if any, of significant events occurring after the close of the market but before the end of the measurement date. Treasury records any changes in valuation, including impairment, on the Statement of Net Cost and the Balance Sheet. Since the valuation is an annual process, Treasury deems changes in valuation of the senior preferred stock and warrants as usual and recurring.

Treasury performs annual calculations, as of September 30, to assess the need for recording an estimated liability in accordance with SFFAS No. 5, *Accounting for Liabilities of The Federal Government,* related to the government's funding commitment to the GSEs under the SPSPAs. Liability recognition is predicated on the probable future occurrence of an excess of liabilities and minimum capital reserve amounts, as defined, over the assets of either GSE at the end of any reporting quarter. The occurrence of future GSE deficits, which ultimately determines the liability to the GSEs, is most sensitive to future changes in the housing price index and, to a lesser extent, future changes in guarantee fees received by the GSEs on single family mortgages and interest rates. For more detailed information on investments in GSEs and the amended SPSPAs, see Note 8—Investments in Government-Sponsored Enterprises.

The government offers its employees' pension and other post-employment retirement benefits, as well as life and health insurance. OPM administers the largest civilian plan and DOD and VA administer the military plans. The benefits payable are generally recorded during the time employee services are rendered. The related liabilities for defined benefit pension plans, veterans' compensation and burial benefits, post-retirement health benefits, life insurance benefits, education benefits, and FECA benefits are recorded at estimated present value of future benefits, less any estimated present value of future normal cost contributions. See Note 12—Federal Employee and Veteran Benefits Payable for additional information.

X. Credit Risk

Credit risk is the potential, no matter how remote, for financial loss from a failure of a borrower or counterparty to perform in accordance with underlying contractual obligations. The government takes on credit risk when it makes direct loans or guarantees to non-federal entities, provides credits to foreign entities, or becomes exposed to institutions that engage in financial transactions with foreign countries.

The government also takes on credit risk related to committed, but undisbursed direct loans, funding commitments to GSEs, and other activities. Many of these programs were developed to provide credit where borrowers are not able to get access to credit with reasonable terms and conditions. These programs expose the government to potential costs and losses. The extent of the risk assumed is described in more detail in the notes to the financial statements, and where applicable, is factored into credit reform models and reflected in fair value measurements.

Y. Treaties and Other International Agreements

For financial reporting purposes, treaties and other international agreements may be understood as falling into three broad categories:

- No present or contingent obligation to provide goods, services, or financial support,
- Present obligation to provide goods, services, or financial support, or
- Contingent obligation to provide goods, services, or financial support.

The proper financial reporting of treaties and other international agreements depends on the probable future outflow or other sacrifice of resources as a result of entering into the agreement.

In many cases, treaties and other international agreements establish frameworks that govern cooperative activities with other countries but leave to the discretion of the parties whether to engage in any such activities. In other cases, the agreements may contemplate specific cooperative activities, but create no present or contingent obligations to engage in them. Cooperative activities relevant to these treaties and other international agreements fall under the first category, which does not result in the U.S. government incurring any financial liability. Since these treaties and other international agreements have no financial impact, they are not reported or disclosed in this *Financial Report*.

Some treaties and other international agreements fall under the second category, and involve a present obligation, and therefore result in liability recognition. Such present obligation may relate to the U.S. government providing financial and in-kind support, including assessed contributions, voluntary contributions, grants, and other assistance to international organizations in which it participates as a member. Examples of such agreements include those that establish international organizations under which the U.S. government undertakes obligations to pay assessed dues to the organization; grant agreements under which the U.S. government provides foreign assistance funds to other countries; and claims settlement agreements under which the U.S. government agrees to pay specific sums of money to settle claims. For further information related to treaties and other international agreements that fall under the second category, refer to Note 19—Commitments.

The last category encompasses those treaties or other international agreements which result in contingencies that may require recognition or disclosure in the financial statements. Such contingencies may stem from commitments in a treaty or other international agreement to provide goods, services, or financial support when a future event occurs, or from litigation, claims, or assessments forged by other parties to the agreement.

Z. Public-Private Partnerships

Federal P3s are risk-sharing arrangements or transactions with expected lives greater than five years between public and private sector entities. Such arrangements or transactions provide a service or an asset for government and/or general public use where in addition to the sharing of resources, each party shares in the risks and rewards of said arrangements or transactions. The P3s that are deemed material to the consolidated financial statements and have met the criteria of SFFAS No. 49, *Public Private Partnerships*, are disclosed. For more details on P3s, see Note 26—Public Private Partnerships.