

John Williams'  
**Shadow Government Statistics**  
*Analysis Behind and Beyond Government Economic Reporting*

**SPECIAL COMMENTARY NUMBER 340**  
**2010 Financial Statements of the U.S. Government**

**December 22, 2010**

---

**Actual 2010 Annual GAAP Deficit in \$5 Trillion Range**

**"Uncertain" Impact of Health Care Law Roils the Accounting**

**No U.S. Guarantee behind Fannie Mae and Freddie Mac?**

---

*PLEASE NOTE: This Commentary is a brief summary of the numbers from the government's 2010 GAAP accounting released yesterday afternoon (December 21st). Further analysis will be prepared, either as a standalone Commentary, or as part of the pending update to the Hyperinflation Special Report. The next regular Commentary will be tomorrow, Thursday, December 23rd, following release of the November New Orders for Durable Goods, along with assessments of the November housing and home sales numbers, and the third-estimate of third-quarter GDP.*

*-- Best wishes to all for a most joyous holiday season! -- John Williams*

**2010 GAAP Accounting Shows Ongoing Unsustainable and Uncontainable Annual Federal Deficits.** Against an official quasi-cash-basis reporting of a \$1.294 trillion 2010 federal budget deficit, which narrowed from a \$1.417 trillion shortfall in 2009, the [\*2010 Financial Report of the United States Government\*](#) showed a GAAP-based 2010 deficit of \$2.080 trillion, which widened from \$1.254 trillion in 2009.

The latter set of numbers reflects GAAP accounting (generally accepted accounting principles), which, at present, excludes the level of and annual changes in the net present value of unfunded liabilities for Social Security and Medicare in balance sheet and income-statement accounting. Those numbers, however, are footnoted and discussed in the financial statements.

Broader GAAP-based federal deficits, including the Social Security and Medicare unfunded liabilities, have been in the \$4 trillion to \$5 trillion range in 2008 and 2009, and 2010's deficit again likely was near \$5 trillion, remaining both uncontainable and unsustainable. The federal government cannot cover such an annual shortfall by raising taxes, as there are not enough untaxed wages and salaries or corporate profits to do so. On the spending side, all government spending, except Social Security and Medicare could be cut, but the broad GAAP results still would be in deficit. As demonstrated by recent Administration and Congressional reaction to the deficit cutting measures put forth by the deficit commission, there is no political will to slash Social Security and Medicare severely. The implications from this are discussed in the [Hyperinflation Report](#). Although that report will be updated in the next month, the underlying fundamentals there have not changed.

***The Problems in Accounting for Healthcare.*** The estimate of a broader GAAP-based deficit at \$5 trillion is mine. At issue with the published report, consistent year-to-year accounting was not shown, with a large, one-time reduction in reported 2010 Medicare liabilities based on overly optimistic assumptions of the impact from recently enacted healthcare legislation. Referred to in the statements as the Affordable Care Act (ACA), the broad GAAP-based results from the ACA accounting show an annual surplus of \$7.0 trillion in 2010, but again, that is not in terms of consistent reporting. Looking at what the annual change would have been in Medicare liabilities, consistently viewed either on the 2009 base versus a 2010 number on the 2009 basis, or the 2009 number on the 2010 basis versus the 2010 base, should result in net deterioration on a relative year-to-year basis.

Separately, the one-time ACA-based reduction in the net present value of unfunded social insurance liabilities (closed group), from \$52.1 trillion in 2009, to \$43.1 trillion in 2010, all was due to the Medicare restatement; Social Security liabilities actually rose.

The new health-care enhanced Medicare results used in the statements were prepared under the auspices of the Administration, but the GAO -- the U.S. government's auditor and the auditor of the GAAP-based financials -- did not fully buy into the happy numbers.

Per the covering letter of Robert F. Dacey, Chief Accountant, U.S. Government Accountability Office, the GAO would not express an opinion on the financial statements (see pages 221-233 of the statements). Specifically, consider the following excerpts from pages 226 and 227:

"DISCLAIMER OF OPINION ON THE STATEMENT OF SOCIAL INSURANCE FOR 2010 AND UNQUALIFIED OPINIONS FOR 2009, 2008, AND 2007

"Because of significant uncertainties (discussed in Note 26 to the consolidated financial statements), primarily related to the achievement of projected reductions in Medicare cost growth reflected in the 2010 Statement of Social Insurance, we were unable to obtain sufficient evidence to support the amounts presented in the 2010 Statement of Social Insurance. Consequently, we are unable to, and we do not, express an opinion on the 2010 Statement of Social Insurance. The Statement of Social Insurance presents the actuarial present value of the federal government's estimated future revenue to be received

from or on behalf of participants and estimated future expenditures to be paid to or on behalf of participants, based on benefit formulas in current law and using a projection period sufficient to illustrate the long-term sustainability of the social insurance programs. ..."

"As a result, readers are cautioned that amounts reported in the 2010 Statement of Social Insurance and related Notes may not fairly present, in all material respects, the financial condition of the federal government's social insurance programs, in conformity with GAAP. The uncertainties related to the 2010 Statement of Social Insurance also affect the projected Medicare and Medicaid costs reported in the Fiscal Projections for the U.S. government, which is presented in Supplemental Information and is summarized in Management's Discussion and Analysis and other accompanying information."

***What's An Extra \$12.4 Trillion or So?*** The GAO went so far as to run an "Illustrative Alternative Scenario" (page 130) to the government's happy Medicare adjustments, with the net effect of showing a net present value of unfunded Medicare liabilities (open group) \$12.4 trillion higher than that used in the formal accounting. The alternative assumptions appear more realistic than the politicized data used in getting ACA enacted.

Unfortunately, under present accounting conditions there simply is no way of coming up with meaningful hard numbers, in terms of total government obligations.

**SGS Alternative Fiscal Deficit and Debt Table.** Given the unusual accounting uncertainty, I have prepared two versions of the 2010 data in the table that follows. The "Official 2010" line represents the numbers as published in the financial statements. The "Alternative 2010" line represents the official data with an added \$12.4 trillion in the net present value of Medicare unfunded liabilities in 2010, as modeled by the GAO. I'm using the latter version as a placeholder for what eventually should be more accurate accounting.

For 2010, gross federal debt was 94% of GDP, and total federal obligations were 443% (official) or 529% (alternative) of GDP, depending on the number used. The difference, though, is not material, as either ratio leaves the U.S. government insolvent over the long haul.

Further from the 2010 statements, per the GAO, the federal government still does not guarantee the securities issued by Freddie Mac and Fannie Mae. Accordingly, the financials of those entities are not consolidated into the federal government's numbers. The money put into those entities by the government, however, is counted as an expense. If the debt of Freddie Mac and Fannie Mae were consolidated into the U.S. government's statements, such would add almost 50 percentage points to the debt-to-GDP ratios mentioned in the preceding paragraph.

## U.S. Government - Alternative Fiscal Deficit and Debt

### Reported by U.S. Treasury

Sources: U.S. Treasury, Shadow Government Statistics.

Fiscal Year <sup>(1)</sup>	Formal Cash-Based Deficit (\$Billions)	GAAP Ex-SS Etc. Deficit (\$Billions)	GAAP With SS Etc. Deficit (\$Trillions)	GAAP Federal Negative Net Worth (\$Trillions)	Gross Federal Debt (\$Trillions)	Total <sup>(2)</sup> Federal Obligations (GAAP) (\$Trillions)
<i>Alternative</i>						
2010	\$1,294.1	\$2,080.3	\$5.3 <sup>(3)</sup>	\$68.9 <sup>(3)</sup>	\$13.6	\$76.3 <sup>(3)</sup>
<i>Official</i>						
2010	\$1,294.1	\$2,080.3	(\$7.0) <sup>(3)</sup>	\$56.5 <sup>(3)</sup>	\$13.6	\$64.0 <sup>(3)</sup>
2009 <sup>(4)</sup>	1,417.1	1,253.7	4.3	63.6	11.9	70.5
2008	454.8	1,009.1	5.1	59.3	10.0	65.6
2007	162.8	275.5	1.2 <sup>(5)</sup>	54.3	9.0	59.8
2006	248.2	449.5	4.6	53.1	8.5	58.2
2005	318.5	760.2	3.5	48.5	7.9	53.3
2004	412.3	615.6	11.0 <sup>(6)</sup>	45.0	7.4	49.5
2003	374.8	667.6	3.0	34.0	6.8	39.1
2002	157.8	364.5	1.5	31.0	6.2	35.4

(1) Fiscal year ended September 30th; the numbers are subject to rounding differences. (2) Includes gross federal debt, not just "public" debt. While the non-public debt is debt the government owes to itself for Social Security, etc., the obligations there are counted as "funded" and as such are part of total government obligations. (3) The official reporting includes a large, one-time reduction in the estimated net present value of unfunded Medicare liabilities, due to generally favorable underlying assumptions tied to the passage of healthcare legislation. With consistent accounting, SGS estimates the GAAP shortfall with Social Security and Medicare for 2010 to be roughly \$5 trillion. The *Alternative* numbers here are being used as a placeholder until better accounting estimates are available, and reflect results using the "illustrative alternative scenario" on Medicare costs shown on page 130 of the 2010 report. (4) The 2009 data predate December 2009 guarantees of Fannie Mae and Freddie Mac and do not reflect PBGC or FDIC liabilities. Please note that mid-year accounting redefinitions for TARP knocked off roughly \$500 billion from the reported formal cash-based estimate and contributed to a TARP "profit" in the GAAP numbers. (5) On a consistent reporting basis, net of one-time changes in actuarial assumptions and accounting, SGS estimates that the GAAP-based deficit for 2007 topped \$4 trillion, with negative net worth of \$57.1 trillion and total obligations of \$59.8. So as to maintain consistency with the official GAAP statements, the "official" numbers are shown. (6) SGS estimates \$3.4 trillion, excluding one-time unfunded setup costs of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (enacted December 2003). Again, in order to maintain consistency with the official GAAP statements, the "official" numbers are shown in the table for 2004. The 2010 GAAP statements were released on December 21, 2010:

<http://fms.treas.gov/fr/index.html>.

### Sources for SGS Table Data

***Fiscal Year (Column 1)*** -- All numbers are for the indicated fiscal year (ended September 30th), in either billions or trillions of dollars as shown.

***Formal Cash-Based Deficit (Column 2)*** -- headline deficit number from page xi of the 2010 report, "Nation by the Numbers Table," hereinafter referred to as NBN, line: "Unified Budget Deficit."

***GAAP ex-SS Etc. Deficit (Column 3)*** -- euphemistically referred to as "Net Operating Cost" in NBN. It excludes social insurance unfunded liabilities.

***GAAP with SS Etc. Deficit (Column 4)*** -- previous number (2) plus year-to-year change in the net present value of social insurance unfunded liabilities, which comes from NBN (page xi) line "Closed Group" under "Statement of Social Insurance," 2010 minus 2009 (for the 2010 number). The "Closed Group" is used here as it has been the preferred measure used in earlier government statements.

The *Alternative* accounting adds in the differential to the NBN line "Closed Group" and the \$12.4 trillion additional net present value of excess expenditures over income for Medicare shown in the "Illustrative Alternative Scenario," shown on page 130.

***GAAP Federal Negative Net Worth (Column 5)*** -- "Total net position" from NBN (page xi), plus the 2010 "Closed Group" total net present value unfunded liabilities of social insurance from NBN. The *Alternative* is adjusted for the alternative Medicare example.

***Gross Federal Debt (Column 6)*** -- from "Note 14. Federal Debt ..." pages 88 to 90 of the 2010 report. Total held by public (p. 88) plus Total intragovernmental (p. 90).

***Total Federal Obligations (Column 7)*** -- Total liabilities from the NBN (page xi) line in the 2010 report, plus the 2010 "Closed Group" total net present value unfunded liabilities of social insurance from NBN, plus total intragovernmental debt from (p. 90) of the 2010 report.

The *Alternative* accounting adds in the NBN line "Closed Group" adjusted for the \$12.4 trillion additional net present value of excess expenditures over income for Medicare shown in the "Illustrative Alternative Scenario," shown on page 130.