Note 18. Contingencies

Financial Treatment of Loss Contingencies

Loss contingencies are existing conditions, situations, or set of circumstances involving uncertainty as to possible loss to an entity. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. The reporting of loss contingencies depends on the likelihood that a future event or events will confirm the loss or impairment of an asset or the incurrence of a liability. Terms used to assess the range for the likelihood of loss are probable, reasonably possible, and remote. Loss contingencies that are assessed as probable and measurable are accrued in the financial statements. Loss contingencies that are assessed to be at least reasonably possible are disclosed in this note and loss contingencies that are assessed as remote are not reported in the financial statements, nor disclosed in the notes. The following table provides criteria for how federal agencies are to account for loss contingencies, based on the likelihood of the loss and measurability.[3]

Likelihood of future outflow or other sacrifice of resources	Loss amount can be reasonably measured	Loss range can be reasonably measured	Loss amount or range cannot be reasonably measured
Probable Future confirming event(s) are more likely to occur than not.[4]	Accrue the liability. Report on Balance Sheet and Statement of Net Cost.	Accrue liability of the best estimate or (if there is no best estimate) minimum amount in loss range, and disclose nature of contingency and range of estimated liability.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Reasonably possible Possibility of future confirming event(s) occurring is more than remote and less than likely.	Disclose nature of contingency and estimated loss amount.	Disclose nature of contingency and estimated loss range.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Remote Possibility of future event(s) occurring is slight.	No disclosure.	No disclosure.	No disclosure.

[3] In addition, a third condition must be met to be a loss contingency: a past event or an exchange transaction must occur.
[4] For loss contingencies related to litigation, probable is defined as the future confirming event or events are more likely than not to occur, with the exception of pending or threatened litigation and unasserted claims. For the pending or threatened litigation and unasserted claims, the future confirming event or events are likely to occur.

The Government is subject to loss contingencies that include insurance and litigation cases. These loss contingencies arise in the normal course of operations and their ultimate disposition is unknown. Based on information currently available, however, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the financial statements, except for the insurance and litigation described in the following section, which could have a material adverse effect on the financial statements.

Insurance Contingencies

At the time an insurance policy is issued, a contingency arises. The contingency is the risk of loss assumed by the insurer, that is, the risk of loss from events that may occur during the term of the policy. The Government has insurance contingencies that are reasonably possible in the amount of $253.1 billion as of September 30, 2017, and $243.8 billion as of September 30, 2016. The major programs are identified below:

- PBGC reported $252.2 billion and $242.8 billion as of September 30, 2017, and 2016, respectively, for the estimated aggregate unfunded vested benefits exposure to the PBGC for private-sector single-employer and multiemployer defined benefit pension plans that are classified as a reasonably possible exposure to loss. This increase is primarily due to the decrease in the interest factors used for valuing liabilities for the single-employer program, while the multiemployer program experienced a decrease in liability due to the removal of certain plans that are no longer classified as reasonably possible. Please refer to the PBGC financial statements for further details.
- FDIC reported $0.6 billion and $0.7 billion as of September 30, 2017, and 2016, respectively, for identified additional risk in the financial services industry that could result in additional loss to the Deposit Insurance Fund (DIF) should potentially vulnerable insured institutions ultimately fail. Actual losses, if any, will largely depend on future economic and market conditions.

Deposit Insurance

Deposit insurance covers all types of deposit accounts such as checking, Negotiable Order of Withdrawal and savings accounts, money market deposit accounts, and certificates of deposit received at an insured bank, savings association, or credit union. The insurance covers the balance of each depositor's account and shares, dollar-for-dollar, up to the insurance limit, including principal and any accrued interest through the date of the insured financial institution's closing. As a result, the Government has the following exposure from federally-insured financial institutions:

- FDIC has estimated insured deposits of $7,092.0 billion as of September 30, 2017, and $6,822.9 billion as of September 30, 2016, for the DIF.
- National Credit Union Administration (NCUA) has estimated insured shares of $1,080.9 billion as of September 30, 2017, and $1,015.9 billion as of September 30, 2016, for the National Credit Union Share Insurance Fund.

Legal Contingencies

Legal contingencies as of September 30, 2017, and 2016, are summarized in the table below:

	2017			2016		
		Estimated Range of Loss for Certain Cases [2]			Estimated Range of Loss for Certain Cases [2]	
(In billions of dollars)	Accrued Liabilities [1]	Lower End	Upper End	Accrued Liabilities [1]	Lower End	Upper End
Legal contingencies:						
Probable	7.4	6.8	8.6	7.2	7.2	7.9
Reasonably possible............	-	3.1	12.6	-	9.2	16.3

[1] Accrued liabilities are recorded and presented in the related line items of the Balance Sheet.

[2] Does not reflect the total range of loss; many cases assessed as reasonably possible of an unfavorable outcome did not include estimated losses that could be determined.

The Government is party to various administrative claims and legal actions brought against it, some of which may ultimately result in settlements or decisions against the Government.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the Government and the loss amounts are reasonably measurable. The estimated liabilities for "probable" cases against the government are $7.4 billion and $7.2 billion as of September 30, 2017, and 2016, respectively, and are included in "Other Liabilities" on the Balance Sheet. For example, the U.S. Supreme Court decision in *Salazar v. Ramah Navajo Chapter*, dated June 18, 2012, is likely to result in additional claims against the Indian Health Service (IHS), which is a component within HHS. As a result of this decision, many tribes have filed claims. Some claims have been settled and others have been asserted but not yet settled.

There are also administrative claims and legal actions pending where adverse decisions are considered by management and legal counsel as "reasonably possible" with an estimate of potential loss or a range of potential loss. The estimated potential losses reported for such claims and actions range from $3.1 billion to $12.6 billion as of September 30, 2017, and from $9.2 billion to $16.3 billion as of September 30, 2016. For example, the Department of the Treasury's *American Recovery and Reinvestment Tax Act of 2009 (ARRA) Related Cases* are a number of cases that were filed in the U.S. Court of Federal Claims alleging that the U.S. government violated statutory and regulatory mandates to make proper payments to plaintiffs under ARRA, Section 1603, for having placed certain energy properties into service. The Department has determined there is a reasonably possible likelihood of unfavorable outcomes in some of the cases.

Numerous litigation cases are pending where the outcome is uncertain or it is reasonably possible that a loss has been incurred and where estimates cannot be made. There are other litigation cases where the plaintiffs have not made claims for specific dollar amounts, but the settlement may be significant. The ultimate resolution of these legal actions for which the potential loss could not be determined may materially affect the U.S. government's financial position or operating results. An example of a specific case is summarized below:

- In the case, *Starr International Co., Inc. v. United States*, the plaintiff, an American International Group, Inc. (AIG) shareholder that brought suit on behalf of two classes of shareholders, alleges that the U.S. government violated the Fifth Amendment to the United States Constitution by illegally exacting or taking property without just compensation. One class, the Credit Agreement Class, claimed that the Fifth Amendment was violated when a majority share of AIG's equity and voting rights was conveyed in connection with an $85 billion loan to AIG during the 2008 financial crisis. Starr also asserted a Fifth Amendment violation on behalf of the second class, the Reverse Stock Split Shareholder Class, alleging that a June 2009 reverse split of AIG's common stock constituted a taking of the common stockholders' asserted right to a shareholder vote on whether to approve a reverse split of AIG's common stock. The U.S. Court of Federal Claims held that the Credit Agreement Shareholder Class prevails on liability, but recovers no damages, and that the Reverse Stock Split Shareholder class does not prevail on liability or damages. On appeal, the U.S. Court of Appeals for the Federal Circuit overturned the lower court's finding with respect to the Credit Agreement Shareholder Class and held that the plaintiff did not have standing to bring the illegal exaction claim, since equity-acquisition claims belong exclusively to AIG and not to its shareholders. (AIG's board of directors declined to pursue any claims against the Government in a unanimous vote in January 2013.) The Federal Circuit also affirmed the trial court's ruling on the reverse stock split claim. On October 6, 2017, the plaintiff petitioned the Supreme Court for a writ of certiorari. The Government is unable to determine the likelihood of an unfavorable outcome or make an estimate of potential loss at this time.

Environmental and Disposal Contingencies

Environmental and disposal contingencies as of September 30, 2017, and 2016, are summarized in the table below:

(In billions of dollars)	2017			2016		
		Estimated Range of Loss for Certain Cases [2]			Estimated Range of Loss for Certain Cases [2]	
	Accrued Liabilities [1]	Lower End	Upper End	Accrued Liabilities [1]	Lower End	Upper End
Environmental and disposal contingencies:						
Probable	28.4	27.7	29.5	25.9	25.8	25.9
Reasonably possible............	-	0.7	1.5	-	0.7	1.8

[1] Accrued liabilities are recorded and presented in the related line items of the Balance Sheet.

[2] Does not reflect the total range of loss; many cases assessed as reasonably possible of an unfavorable outcome did not include estimated losses that could be determined.

The Government is subject to loss contingencies for a variety of environmental cleanup costs for the storage and disposal of hazardous material as well as the operations and closures of facilities at which environmental contamination may be present.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the Government and the loss amounts are reasonably measurable. The estimated liabilities for these cases are $28.4 billion and $25.9 billion as of September 30, 2017, and 2016, respectively, and are included in "Other Liabilities" on the Balance Sheet.

In accordance with the *Nuclear Waste Policy Act of 1982* (NWPA), DOE entered into more than 68 standard contracts with utilities in return for payment of fees established by the NWPA into the Nuclear Waste Fund. DOE agreed to begin disposal of spent nuclear fuel (SNF) by January 31, 1998. Because DOE has no facility available to receive SNF under the NWPA, it has been unable to begin disposal of the utilities' SNF as required by the contracts. Therefore, DOE is subject to SNF litigation for damages suffered by all utilities as a result of the delay in beginning disposal of SNF and also damages for alleged exposure to radioactive and/or toxic substances. Significant claims for partial breach of contract and a large number of class action and/or multiple plaintiff tort suits have been filed with estimated liability amounts of $26.7 billion and $24.7 billion as of September 30, 2017, and 2016, respectively.

Other Contingencies

DOT, HHS, and Treasury reported the following other contingencies:

- The Federal Highway Administration (FHWA) preauthorizes states to establish construction budgets without having received appropriations from Congress for such projects. FHWA has authority to approve projects using advance construction under 23 U.S.C. 115(a). FHWA does not guarantee the ultimate funding to the states for these "advance construction" projects and does not obligate any funds for these projects. When funding becomes available to FHWA, the states can then apply for reimbursement of costs that they have incurred on such projects, at which time FHWA can accept or reject such requests. FHWA has pre-authorized $55.2 billion and $50.6 billion to the states to establish budgets for its construction projects for fiscal years ending September 30, 2017, and 2016, respectively. Congress has not provided appropriations for these projects and no liability is accrued in the DOT consolidated financial statements.

- Contingent liabilities have been accrued as a result of Medicaid audit and program disallowances that are currently being appealed by the states and for reimbursement of state plan amendments. The Medicaid amounts are $12.2 billion and $10.2 billion for fiscal years ending September 30, 2017, and 2016, respectively. In all cases, the funds have been returned to HHS. If the appeals are decided in favor of the states, HHS will be required to pay these amounts. In addition, certain amounts for payment have been deferred under the Medicaid program when there is reasonable doubt as to the legitimacy of expenditures claimed by a state. There are also outstanding reviews of the state expenditures in which a final determination has not been made.
- Through an annual process, Treasury assesses the need for an estimated contingent liability that reflects the forecasted equity deficits of the GSEs. Based on this assessment, no accrued contingent liability was recorded for fiscal years 2017 and 2016. However, the reduction in U.S. corporate tax rate resulting from the enactment of the *Tax Cuts and Jobs Act* on December 22, 2017, required that each of Fannie Mae and Freddie Mac record a reduction in the value of their deferred tax assets in the quarter in which the legislation was enacted, impacting potential future funding draws. The funding draws and the associated amounts are expected to be realized in March 2018. See Note 8—Investments in Government-Sponsored Enterprises for further information.

Treaties

The Government is a party to treaties and other international agreements. These treaties and other international agreements address various issues including, but not limited to, trade, commerce, security, and law enforcement that may involve financial obligations or give rise to possible exposure to losses. Treaties and other international agreements fall into three broad categories: (1) no commitment to spend money; (2) commitment to spend money; or (3) potential obligation to spend money. A review must be conducted of potential contingent liabilities arising from litigation related to treaties and other international agreements. This review, along with any resulting relevant information, is captured and reported in the annual legal representation letter process. Refer to the Legal Contingencies section of this note for further information. It has been confirmed that the relevant financial obligations are included in the applicable financial statements and notes for the commitment to spend money and the potential obligation to spend money categories. The final category of no commitment to spend money will continue to be analyzed to confirm that all material financial obligations or possible loss exposures are properly reported in the *Financial Report*.