

The Most Critical Challenges in Governmental Accounting Today

CGA4/23/V1

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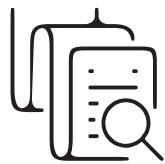
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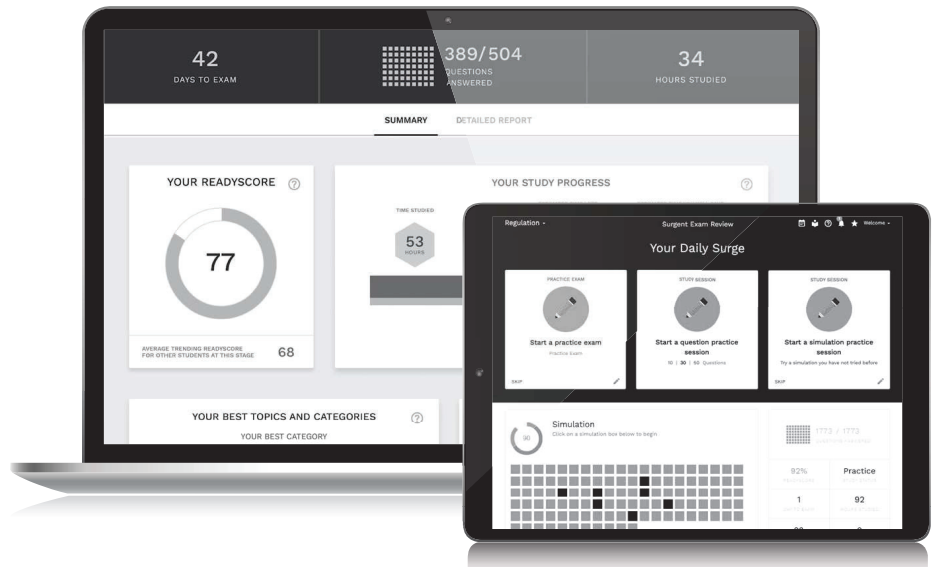
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Table of Contents

| | |
|--|----------|
| GASB No. 87: Glancing Back and Looking Forward..... | 1 |
| GASB No. 96 and SBITAs | 2 |
| Other GASB Developments | 3 |
| Latest Developments..... | 4 |

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Revised March 2023

GASB No. 87: Glancing Back and Looking Forward

| | |
|---|-----------|
| <i>Learning objectives</i> | 1 |
| <i>I. Glancing back</i> | 1 |
| A. A tale of two cities | 1 |
| <i>II. Looking forward (although perhaps not forward to it!)</i> | 7 |
| A. Exercise 1-3 | 7 |
| B. Remeasurements | 7 |
| C. Lease modifications and terminations | 9 |
| <i>III. Suggested solutions to exercises</i> | 10 |
| A. Suggested solution to Exercise 1-1 | 10 |
| B. Suggested solution to Exercise 1-2 | 10 |
| C. Suggested solution to Exercise 1-3 | 11 |
| D. Suggested solution to Exercise 1-4 | 11 |

GASB No. 87: Glancing Back and Looking Forward

Learning objectives



In this chapter, we will review aspects of how GASB No. 87 impacted governmental reporting and also examine issues to watch out for in year two of implementation.

I. Glancing back

For governments, 2022 was the year of the lease. The implementation of GASB No. 87 ushered in a new single reporting model for lease accounting based on the foundational principle that leases are financings of the right to use an asset. This new single reporting model came at a cost in terms of the time spent on: (1) locating and analyzing leasing arrangements; (2) calculating lease terms; (3) determining the lease payments to be included in lease liabilities; (4) developing incremental borrowing rates; (5) calculating lease liabilities/lease assets and related interest expense/amortization expense; (6) considering the existence of lessor lease receivables; and (7) developing disclosures. While many/most may question whether the cost incurred in implementing the new standard was worth the “benefit,” we likely can agree that GASB No. 87 has impacted financial reporting.

A. A tale of two cities

To look at how GASB No. 87 changed financial reporting, we reviewed two cities’ audited financial statements and aspects of how GASB No. 87 impacted their reporting. The following table contains information about the two cities we selected.

| A Tale of Two Cities | | |
|--|-----------------------|------------------|
| | Carrollton, TX | Plano, TX |
| Population | 135,110 | 291,200 |
| Fiscal year end selected | 9/30/2022 | 9/30/2022 |
| Were comparative f/s prepared in the year GASB No. 87 was implemented? | No | No |
| Government-wide f/s lessee lease liabilities at 9/30/22 | \$4,839,656 | \$5,056,040 |
| % of lease liabilities to total liabilities on 9/30/22 government-wide f/s | 1.7% | 0.6% |
| Government-wide f/s lessee lease assets (net) at 9/30/22 | \$4,775,503 | \$5,015,505 |
| % of lease assets (net) to total assets on 9/30/22 government-wide f/s | 0.5% | 0.2% |

| A Tale of Two Cities | | |
|--|--|---|
| | Carrollton, TX | Plano, TX |
| Types of assets leased as lessee | Police equipment, building lease, digital space, and advertising billboard space | Buildings and equipment |
| Lease assets amortization period | 2-10 years | Equipment 3-10 years Buildings 3-100 years |
| Government-wide f/s lessor lease receivable at 9/30/22 | \$186,194 | \$12,217,666 |
| % of lessor lease receivable to total assets on 9/30/22 government-wide f/s | 0.0% | 0.5% |
| Government-wide f/s lessor lease deferred inflows of resources at 9/30/22 | \$186,194 | \$12,148,404 |
| Types of assets leased as lessor | Live-work spaces, land, and building space | Land and cell sites |

1. GASB No. 87 and lessee disclosures

A somewhat mysterious and likely less emphasized aspect of implementing GASB No. 87 was the lessee disclosure requirements. As a reminder, the chart below summarizes the lessee disclosure requirements contained in GASB No. 87.

| GASB No. 87's lessee disclosure requirements | |
|--|--|
| A lessee will disclose the following about its lease activities (which may be grouped for purposes of disclosure), other than short-term leases: | |
| 🔍 | A general description of its leasing arrangements, including: (1) the basis, terms, and conditions on which variable payments not included in the measurement of the lease liability are determined and (2) the existence, terms, and conditions of residual value guarantees provided by the lessee not included in the measurement of the lease liability; |
| 🔍 | The total amount of lease assets, and the related accumulated amortization, disclosed separately from other capital assets; |
| 🔍 | The amount of lease assets by major classes of underlying assets, disclosed separately from other capital assets; |
| 🔍 | The amount of outflows of resources recognized in the reporting period for variable payments not previously included in the measurement of the lease liability; |
| 🔍 | The amount of outflows of resources recognized in the reporting period for other payments, such as residual value guarantees or termination penalties, not previously included in the measurement of the lease liability; |
| 🔍 | Principal and interest requirements to maturity, presented separately, for the lease liability for each of the five subsequent fiscal years and in five-year increments thereafter; |
| 🔍 | Commitments under leases before the commencement of the lease term; and |
| 🔍 | The components of any loss associated with an impairment. |

2. Selected lessee disclosures from Carrollton's financial statements

In this section, we will review selected excerpts from Carrollton's financial statements related to its **lessee disclosures**. (Note. The City of Plano also did an excellent job of its disclosures; however, we are presenting Carrollton's as they are less complex). The first excerpt primarily provides a general description of Carrollton's lessee leasing arrangements.

Selected excerpts from Carrollton's lessee disclosures

(15) LEASES

Effective October 1, 2021, the City implemented GASB Statement No. 87, *Leases*, which required the recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. The adoption of GASB No. 87 had no historical impact on the City's net position and no restatement of net position was made.

Lessee -

The City recognizes a lease liability and an intangible right-to-use lease asset (lease asset) in the government-wide funds financial statements.

At implementation of GASB Statement No. 87 and the commencement of leases beginning after October 1, 2021, the City initially measured the lease liability at the present value of payments expected to be made during the remaining lease term. Subsequently, the lease liability is reduced by the principal portion of lease payments made. The lease right-to-use asset was initially measured as the initial amount of the lease liability, adjusted for lease payments made at or before the lease commencement date, plus certain initial direct costs. Subsequently, the lease right-to use asset is amortized on a straight-line basis over its useful life.

Key estimates and judgments related to leases include how the City determines (1) the discount rate it uses to discount the expected lease payments to present value, (2) lease term and (3) lease payments.

The City uses the interest rate charged by the lessor as the discount rate. When the interest rate charged by the lessor is not provided, the City generally uses its estimated incremental borrowing rate as the discount rate for leases. The lease term includes the noncancellable period of the lease. Lease payments included in the measurement of the lease liability are composed of fixed payments and purchase option price that the City is reasonably certain to exercise.

The City monitors changes in circumstances that would require a re-measurement of its lease and will remeasure the lease asset and liability if certain changes occur that are expected to significantly affect the amount of the lease liability.

Leased assets are reported on the government-wide Statement of Net Position and lease liabilities are reported with noncurrent liabilities on the Statement of Net Position.

The second excerpt (see following page) provides the total amount of lease assets, and the related accumulated amortization, disclosed separately from other capital assets.

Selected excerpts from Carrollton's lessee disclosures

Leased asset activity for the year-ended September 30, 2022, was as follows:

| | Balance | | | | Balance |
|---|---------------------|---------------------|---------------------|--|---------------------|
| | Restated | Additions/ | Retirements/ | | Balance |
| | October 1 | Completions | Adjustments | | September 30 |
| Governmental Activities | | | | | |
| Leased assets | \$ 5,032,736 | \$ 434,154 | \$ - | | \$ 5,466,890 |
| <i>Total leased assets being amortized</i> | <u>5,032,736</u> | <u>434,154</u> | <u>-</u> | | <u>5,466,890</u> |
| Less accumulated amortization for: | | | | | |
| Leased assets | - | (691,387) | - | | (691,387) |
| <i>Total accumulated amortization</i> | <u>-</u> | <u>(691,387)</u> | <u>-</u> | | <u>(691,387)</u> |
| <i>Total leased assets being amortized, net</i> | <u>\$ 5,032,736</u> | <u>\$ (257,233)</u> | <u>\$ -</u> | | <u>\$ 4,775,503</u> |

The third excerpt provides the principal and interest requirements to maturity, presented separately, for the lease liability for each of the five subsequent fiscal years and in five-year increments thereafter.

Selected excerpts from Carrollton's lessee disclosures

2. Lease payable





Prior to beginning of the current fiscal year, the City entered into a ten-year lease agreement as lessee for the acquisition and use of police equipment and building lease for space. During the fiscal year the City, entered into two additional leases as the lessee for digital space and advertising billboard space. At the beginning of the fiscal year the initial lease liability was recorded in the amount of \$5,062,183. As of September 30, 2022, the value of the lease liability was \$4,839,656.

The future principal and interest lease payments as of September 30, 2022, were as follows:

| Maturity Analysis | Principal | Interest | Total |
|--------------------------|---------------------|-------------------|---------------------|
| 10/01/2022 - 09/30/2023 | \$ 768,173 | \$ 35,184 | \$ 803,357 |
| 10/01/2023 - 09/30/2024 | 730,374 | 28,929 | 759,303 |
| 10/01/2024 - 09/30/2025 | 697,032 | 23,062 | 720,094 |
| 10/01/2025 - 09/30/2026 | 672,898 | 16,256 | 689,154 |
| 10/01/2026 - 09/30/2027 | 574,385 | 11,401 | 585,786 |
| 10/01/2027 - 09/30/2032 | 1,396,795 | 15,773 | 1,412,568 |
| 10/01/2032 - 09/30/2037 | - | - | - |
| Total | <u>\$ 4,839,657</u> | <u>\$ 130,605</u> | <u>\$ 4,970,262</u> |
| Lease Liability | <u>\$ 4,839,657</u> | | |

3. GASB No. 87 and lessor disclosures

Having looked at disclosures from the lessee perspective, let's move to the lessor side of the equation. As a reminder, the chart below summarizes the lessor disclosure requirements contained in GASB No. 87.

| GASB No. 87's lessor disclosure requirements | |
|---|---|
| A lessor will disclose the following about its lease activities (which may be grouped for purposes of disclosure), other than short-term leases and certain regulated leases: | |
|  | A general description of its leasing arrangements, including the basis, terms, and conditions on which any variable payments not included in the measurement of the lease receivable are determined; |
|  | The total amount of inflows of resources (e.g., lease revenue, interest revenue, and any other lease-related inflows) recognized in the reporting period from leases, if that amount cannot be determined based on the amounts displayed on the face of the financial statements; |
|  | The amount of inflows of resources recognized in the reporting period for variable and other payments not previously included in the measurement of the lease receivable, including inflows of resources related to residual value guarantees and termination penalties; and |
|  | The existence, terms, and conditions of options by the lessee to terminate the lease or abate payments if the lessor government has issued debt for which the principal and interest payments are secured by the lease payments. |

4. Selected lessor disclosures from Carrollton's financial statements

In this section, we will look at selected excerpts from Carrollton's financial statements related to its **lessor disclosures**. (Note. Once again, the City of Plano also did an excellent job of its disclosures; however, we are presenting Carrollton's as they are less complex). The first excerpt primarily provides a general description of Carrollton's lessor leasing arrangements.

| Selected excerpts from Carrollton's lessor disclosures |
|---|
| <p><u>Lessor</u> –</p> <p>The City recognizes a lease receivable and deferred inflow of resources in the government-wide and governmental funds financial statements.</p> <p>At implementation of GASB Statement No. 87 and the commencement of leases beginning after October 1, 2021, the City initially measured the lease receivable at the present value of payments expected to be received during the lease term. Subsequently, the lease receivable is reduced by the principal portion of lease payments received. The deferred inflow of resources is initially measured as the initial amount of the lease receivable, adjusted for lease payments received at or before the lease commencement date. Subsequently, the deferred inflow of resources is recognized as revenue over the life of the lease term. Key estimates and judgments include how the City determines (1) the discount rate it uses to discount the expected lease receipts to present value, (2) lease term and (3) lease receipts. The City uses the lessee's rate or the rate disclosed in the agreement. If the rate is not readily available, the City uses its estimated incremental borrowing rate as the discount rate. The lease term includes the non-cancellable period of the lease. Lease receipts included in the measurement of the lease receivable is composed of fixed payments from the lessee.</p> <p>The City monitors changes in circumstances that would require a re-measurement of its lease, and will remeasure the lease receivable and deferred inflows of resources if certain changes occur that are expected to significantly affect the amount of the lease receivable.</p> |

The second excerpt primarily provides the total amount of inflows of resources (e.g., lease revenue, interest revenue, and any other lease-related inflows) recognized in the reporting period.

Selected excerpts from Carrollton's lessor disclosures

1. Lease receivable

At the start of current fiscal year, the City was leasing live-work spaces, land and building space. These leases all had varying terms between two and three years. The City recognized \$370,439 in lease and interest revenue during the current fiscal year related to these leases. As of September 30, 2022, the City's receivable for lease payments was \$186,194. Also, the City has a deferred inflow of resources associated with this lease that will be recognized as revenue over the lease term. As of September 30, 2022, the balance of the deferred inflow of resources was \$186,194.

5. Exercise 1-1

Please answer the following question.

Government A says that it uses the cash basis for its financial statements and therefore does not need to disclose anything related to leases. **Do you agree or disagree?**

6. Exercise 1-2

Please answer the following question.

Government B says that it does not have any leases. **Should this be disclosed in the financial statements?**

II. Looking forward (although perhaps not forward to it!)

There are some accounting standards which are difficult to apply in the first year but really not much of an issue in subsequent years. GASB No. 87 does not exactly fit into that category. Due to GASB No. 87, each year governments will have to watch out for things like: (1) new leasing agreements being entered into; (2) the disclosure of variable lease payments that were not included in the measurement of the lease liability; (3) the annual updating of the lease asset and liability schedules; (4) lease options being exercised/not exercised contrary to initial expectations that require remeasurements; and (5) leases being modified or terminated.

A. Exercise 1-3

Please answer the following question.

How should a government treat a lease where the lease payments are based on the Consumer Price Index (CPI) each year and the CPI rate increases from one year to the next?

B. Remeasurements

As we learned during the implementation of GASB No. 87, multiple assumptions/assessments were made in calculating the lease amounts reported. We also know that we are not always going to be perfect in all of our assumptions/assessments. GASB No. 87 specifies several conditions under which the lease payment amounts likely have changed because of changes to the estimates used in determining the liability. For example, paragraph 15 of GASB No. 87 discusses the need to reassess the lease term if: (1) the lessee or lessor elects to **exercise an option** or **not to exercise an option** contrary to the initial determination of the lease term; or (2) an event specified in the lease contract that requires an extension or termination of the lease takes place.






A helpful Q&A related to lease term reassessment

The GASB Implementation Guide No. 2020-1 question 4.8 provides the following Q&A related to lease term reassessment:

Q—A county leases a piece of equipment. The noncancellable period is five years, and the county has an option to extend for another two years. The county initially determines that it is not reasonably certain that it will exercise the option to extend and, therefore, assesses the lease term to be five years. In year three, the county determines that it has become reasonably certain that it will exercise the option to extend but does not plan to make the election (by notifying the lessor) until year five. Should the county reassess the lease term in year three?

A—No. Paragraph 15 of Statement 87 provides that the lease term should be reassessed if the lessee elects to exercise an option that previously was not reasonably certain of being exercised. Therefore, the county should not reassess the lease term until it exercises the option to extend by notifying the lessor—in this case, in year five—even if it becomes reasonably certain of doing so in year three.

In addition to changes in the lease term, there can be additional changes that require remeasurements. As discussed in the following, under GASB No. 87, a lessee remeasures the lease liability and a lessor remeasures the lease receivable if certain conditions are met.

| When do we have to remeasure? | |
|---|---|
| Under GASB No. 87, a lessee remeasures the lease liability if one or more of the following changes have occurred and the changes individually or in aggregate are expected to significantly affect the amount of the lease liability since the previous measurement: | |
|  | There is a change in the lease term; |
|  | An assessment of all relevant factors indicates that the likelihood of a residual value guarantee being paid or a purchase option being exercised has changed from reasonably certain to not reasonably certain, or vice versa; |
|  | A change in the estimated amounts for payments already included in the measurement of the lease liability, except for those variable payments that depend on an index or rate; |
|  | A change in the interest rate the lessor charges the lessee, if used as the initial discount rate; or |
|  | A contingency upon which some or all of the variable payments that will be made over the remainder of the lease term are based is resolved such that those payments now meet the criteria for measuring the lease liability. |
| Note. Lessors are essentially required to remeasure the lease receivable if the first, fourth, or fifth items above occur. | |

When the above conditions are met, lessees follow the remeasurement guidance in paragraphs 25-29 of GASB No. 87 and lessors follow the remeasurement guidance in paragraphs 49-52. When a lessee remeasures a lease liability, the lease asset generally will be adjusted by the same amount (GASB No. 87 paragraph 33). When a lessor remeasures the lease receivable, the deferred inflow of resources generally will be adjusted by the same amount (GASB No. 87 paragraph 54).

1. Exercise 1-4

Please indicate whether the following statement is true or false.

| | | True or False |
|----------|---|---------------|
| 1 | A lease liability should not be remeasured, nor should the discount rate be reassessed, solely for a change in the lessee's incremental borrowing rate. | |

C. Lease modifications and terminations

We just discussed certain conditions that may trigger the need to remeasure a lease under GASB No. 87 (e.g., a lessee elects to exercise an existing option contrary to the initial determination of the lease term). Another complication in lease accounting occurs when a **lease contract is actually modified or terminated** during the lease term. Examples of modifications or terminations include: (1) the parties agree to extend or reduce a lease when there is no option to extend or reduce; (2) payment amounts are revised; (3) another underlying asset is added or an asset is removed; or (4) the parties simply agree to terminate a lease prior to its scheduled end date when such a provision was not included in the contract. Governments affected by lease modifications and terminations will look to paragraphs 71-79 of GASB No. 87. (**Note.** This amendment guidance is distinct from the lease remeasurement guidance we discussed.)

III. Suggested solutions to exercises

This section contains the suggested solutions to the exercises presented in the chapter.

A. Suggested solution to Exercise 1-1

Government A says that it uses the cash basis for its financial statements and therefore does not need to disclose anything related to leases. **Do you agree or disagree?**

The author tends to disagree in terms of not disclosing anything. Special-purpose framework questions are always tough to answer as many folks seem to have different thoughts but there is by definition no standard setter to set rules per se. The first thing to tackle here is whether Government A is truly cash basis **or** (more likely) modified cash basis (i.e., recording certain amounts of assets and liabilities). If they are modified cash we need to look at the level of modifications. **If an entity is on the modified cash basis and reporting capital assets and debt in the financial statements**, then reporting and disclosing leases consistent with how capital assets and debt are being handled would seem to be the best approach. **If an entity is on the modified cash basis and not reporting capital assets or debt in the financial statements**, perhaps the issue could be handled by a disclosure regarding what is and is not being included in the financial statements and notes.

Note. Paragraph .A26 of AU-C 800 discusses that when the special purpose financial statements contain items that are the same as, or similar to, those in financial statements prepared in accordance with GAAP, informative disclosures similar to those required by GAAP are necessary to achieve fair presentation. For example, financial statements prepared on a tax basis or on a modified cash basis of accounting usually reflect depreciation, long-term debt, and owners' equity. Thus, the informative disclosures for depreciation, long-term debt, and owners' equity in such financial statements would be comparable to those in financial statements prepared in accordance with GAAP.

B. Suggested solution to Exercise 1-2

Government B says that it does not have any leases. **Should this be disclosed in the financial statements?**

This is also an area where preparers have different thoughts. GAAP typically tells us what is required to be disclosed when the transaction/condition is applicable. When something is not disclosed, the user can infer that it either was not applicable or not material to the entity. Having said that, the author believes that there is nothing wrong in explaining the absence of certain information (because it was not applicable or not material at the particular entity) if users typically expect to see it and might be confused by its absence.

C. Suggested solution to Exercise 1-3

How should a government treat a lease where the lease payments are based on the Consumer Price Index (CPI) each year and the CPI rate increases from one year to the next?

The increase in rent is treated as an outflow (expense) of the period. The GASB Implementation Guide No. 2019-03, *Leases*, provides a helpful illustration of this as shown below (see final sentence):

Example 1—Variable Payments That Depend on an Index

Facts and Assumptions

A school district enters into a lease contract for a building for five years. Lease payments are due at the beginning of each year. The payment for each year is 100 times the Consumer Price Index (CPI) as of December 31 of the prior year. The lease commences on January 1, 20X1. The CPI as of December 31, 20X0, was 251.

Accounting and Financial Reporting

The first payment, due January 1, 20X1, will be \$25,100 (100 times the CPI of 251). In accordance with paragraph 21b of Statement 87, the variable payments initially should be measured using the CPI as of the commencement of the lease term. Therefore, the initial measurement of the lease liability will be the present value of \$125,500 (\$25,100 per year, multiplied by 5 years).

If the CPI at December 31, 20X1, increases to 253, the school district's payment on January 1, 20X2, will be \$25,300. The additional \$200 will be recognized as an outflow of the period.

D. Suggested solution to Exercise 1-4

| | | True or False |
|---|---|---------------|
| 1 | A lease liability should not be remeasured, nor should the discount rate be reassessed, solely for a change in the lessee's incremental borrowing rate. | True. |

GASB No. 96 and SBITAs

| | |
|---|-----------|
| Learning objective | 1 |
| I. GASB No. 96 | 1 |
| A. Exercise 2-1 | 1 |
| B. The big picture view of SBITA accounting under GASB No. 96 | 1 |
| C. Exercise 2-2 | 2 |
| II. Concepts that must be understood upfront | 2 |
| A. The definition of a <i>SBITA</i> | 2 |
| B. The meaning of <i>reasonably certain</i> | 5 |
| C. The calculation of the <i>subscription term</i> | 5 |
| D. The definition of a <i>short-term SBITA</i> | 7 |
| E. Contracts with multiple components | 8 |
| F. Materiality | 8 |
| III. SBITA recognition, measurement, and disclosure | 9 |
| A. An overview of SBITA accounting | 9 |
| B. Calculating the subscription liability | 9 |
| C. Accounting for the subscription liability over the subscription term | 11 |
| D. Calculating the subscription asset | 11 |
| E. Accounting for the subscription asset over the subscription term | 13 |
| F. The current financial resources measurement focus financial statements | 13 |
| G. SBITA disclosure requirements | 14 |
| IV. Effective date and transition | 15 |
| A. Exercise 2-13 | 16 |
| V. A few parting thoughts about implementation | 16 |
| VI. Suggested solutions to exercises | 17 |
| A. Suggested solution to Exercise 2-1 | 17 |
| B. Suggested solution to Exercise 2-2 | 17 |
| C. Suggested solution to Exercise 2-3 | 18 |
| D. Suggested solution to Exercise 2-4 | 18 |
| E. Suggested solution to Exercise 2-5 | 19 |
| F. Suggested solution to Exercise 2-6 | 19 |
| G. Suggested solution to Exercise 2-7 | 19 |
| H. Suggested solution to Exercise 2-8 | 20 |
| I. Suggested solution to Exercise 2-9 | 20 |
| J. Suggested solution to Exercise 2-10 | 21 |
| K. Suggested solution to Exercise 2-11 | 21 |
| L. Suggested solution to Exercise 2-12 | 21 |
| M. Suggested solution to Exercise 2-13 | 21 |

GASB No. 96 and SBITAs

Learning objective



Upon completing this chapter, you will be able to prepare for and implement GASB No. 96 on subscription-based information technology arrangements (SBITAs).

I. GASB No. 96

In May 2020, the GASB issued GASB No. 96, *Subscription-Based Information Technology Arrangements*. GASB No. 96 provides requirements related to subscription-based information technology arrangements (**SBITAs**). In the past decade, SBITAs have become increasingly prevalent as governments and vendors continue to migrate away from traditional information technology (IT) arrangements based on a purchasing/perpetual licensing model and move to a **subscription model**. Prior to GASB No. 96, there was no accounting or reporting guidance specifically for SBITAs as: (1) GASB No. 51 and prior Implementation Guides addressed only certain aspects of accounting for **purchased** computer software; and (2) GASB No. 87 excluded SBITAs. GASB No. 96 is effective for fiscal years beginning after June 15, 2022, and there are special transitional implementation provisions that we will discuss later. The requirements in GASB No. 96 track closely to the requirements found in GASB No. 87, but the guidance is tailored to issues surrounding SBITAs (e.g., how a government that enters into a software subscription agreement should account for related implementation costs).

A. Exercise 2-1

Please indicate whether the following statement is true or false.

| | | True or False |
|---|--|---------------|
| 1 | Government A enters into an arrangement with a vendor which conveys control of the right to use the vendor's IT assets. Under the arrangement, Government A has remote access to software applications and cloud data storage. This would likely be a SBITA. | |

B. The big picture view of SBITA accounting under GASB No. 96

The following chart provides a big picture view of SBITA accounting under GASB No. 96.

| The big picture view of SBITA accounting under GASB No. 96 | |
|--|--|
| | Under GASB No. 96, a government generally will recognize an intangible right-to-use subscription asset and a corresponding subscription liability . A government will recognize the subscription liability at the commencement of the subscription term (i.e., when the subscription asset is placed into service). The subscription liability will be initially measured at the present value of expected subscription payments over the subscription term. |

C. Exercise 2-2

Please indicate whether the following statement is true or false.


| | | True or False |
|---|---|---------------|
| 1 | GASB No. 87 provides guidance for lessees and lessors. GASB No. 96 does the same thing for SBITAs (i.e., it provides guidance for government end users and governments that provide the right to use their IT assets to other entities through SBITAs). | |

II. Concepts that must be understood upfront

GASB No. 96 is a comprehensive standard (approximately 70 pages). The good news is that much of the guidance in GASB No. 96 parallels guidance which governments had to learn and apply in implementing GASB No. 87. In this section, we are going to explore the following concepts that must be understood upfront to implement the standard: [1] the definition of a **SBITA**; [2] the meaning of **reasonably certain**; [3] the calculation of the **subscription term**; [4] the definition of a **short-term SBITA**; [5] contracts with multiple components; and [6] materiality.

A. The definition of a SBITA

A fundamental aspect of applying GASB No. 96 is understanding the definition of a SBITA. GASB No. 96 is a very substance over form standard. For example, a contract may be called a “lease,” but the underlying asset is primarily IT software. While that contract may not use the term “subscription”, it would be accounted for as a SBITA if it meets the definition.

| | |
|---|---|
|  | <p style="text-align: center;">GASB No. 96 defines a SBITA as being...</p> <p>A contract that conveys control of the right to use another party’s (a SBITA vendor’s) IT software, alone or in combination with tangible capital assets (the underlying IT assets), as specified in the contract for a period of time in an exchange or exchange-like transaction.</p> |
|---|---|

Based on the above, each SBITA has three elements which can be remembered by the acronym **CPE** (i.e., **conveyance** of control, for a **period** of time, in an **exchange** or exchange-like transaction).

1. Conveys control of the right to use

For a contract to meet the definition of a SBITA, the contract needs to **convey control of the right to use** another party’s (a SBITA vendor’s) IT software, alone or in combination with tangible capital assets (the underlying IT assets), as specified in the contract for a period of time in an exchange or exchange-like transaction. To determine whether a contract **conveys control of the right to use** the underlying IT assets, a government will assess whether it has **both**: (1) the right to obtain the present service capacity from use of the underlying IT assets as specified in the contract; **and** (2) the right to determine the nature and manner of use of the underlying IT assets as specified in the contract.

2. Exercise 2-3

Please answer the following questions.

Is this a SBITA? – Part 1

Government B enters into a 24-month agreement with Router-Router to provide 24/7 off-site live troubleshooting of basic IT problems and periodic training for Government B's employees. **This is probably a SBITA?**

Is this a SBITA? – Part 2

Andy Auditor is meeting with Stuart (the client's IT Director). Stuart shows Andy an agreement entitled "Infrastructure as a Service." **This is probably a SBITA?**

3. For a period of time

For a contract to meet the definition of a SBITA, the contract needs to convey control of the right to use another party's (a SBITA vendor's) IT software, alone or in combination with tangible capital assets (the underlying IT assets), as specified in the contract for a **period of time** in an exchange or exchange-like transaction. We will soon see that licensing arrangements that provide a **perpetual license** to governments to use a vendor's computer software are not subject to GASB No. 96 (i.e., if something is perpetual in nature, there is not a period of time but rather it is forever).

4. Exercise 2-4


Please answer the following question related to whether a contract is for a period of time.

Is this for a period of time?

Anne Auditor is meeting with Sue (a client's IT Director). Sue shows Anne an agreement entitled "Software Subscription". The agreement calls for three annual payments of \$10,000 and in return the client is granted a perpetual license for the right to use a leasing software package. **Is this likely a SBITA?**





5. An exchange or exchange-like transaction

For a contract to meet the definition of a SBITA, the contract needs to convey control of the right to use another party's (a SBITA vendor's) IT software, alone or in combination with tangible capital assets (the underlying IT assets), as specified in the contract for a period of time in an **exchange or exchange-like transaction**.

| | |
|---|---|
|  | <p>For a contract to meet the definition of a SBITA, it needs to be an exchange or exchange-like transaction</p> |
| | <p>Typically, there are few issues that arise in determining whether a SBITA contract is an exchange or exchange-like transaction (as most are exchange or exchange-like transactions). However, hypothetically, if a government obtained the right to use a SBITA asset, which had a market value of \$100,000 per year, for \$1 per year such a contract would not meet the GASB No. 96 definition of a SBITA. The substance of that type of arrangement would represent a nonexchange transaction addressed in GASB No. 33, <i>Accounting and Financial Reporting for Nonexchange Transactions</i>.</p> |

6. Items specifically excluded from GASB No. 96

GASB No. 96 specifically excludes certain contracts from its scope as discussed in the following chart.

| GASB No. 96 does not apply to: | |
|---|--|
|  | Contracts that convey control of the right to use another party's combination of IT software and tangible capital assets that meets the definition of a lease in GASB No. 87 in which the software component is insignificant when compared to the cost of the underlying tangible capital asset (e.g., a computer with operating software or a smart copier that is connected to an IT system). |
|  | Governments that provide the right to use their IT software and associated tangible capital assets to other entities through SBITAs. |
|  | Contracts that meet the GASB No. 94 definition of a PPP. |
|  | Licensing arrangements that provide a perpetual license to governments to use a vendor's computer software, which are subject to GASB No. 51, <i>Accounting and Financial Reporting for Intangible Assets</i> , as amended. |

7. Exercise 2-5

Please answer the following question.

| |
|--|
| <p>Where things can get fuzzy</p> <p>We just saw that GASB No. 96 does not apply to contracts that convey control of the right to use another party's combination of IT software and tangible capital assets that meets the definition of a lease in GASB No. 87 in which the software component is insignificant when compared to the cost of the underlying tangible capital asset (e.g., a computer with operating software or a smart copier that is connected to an IT system). If an agreement has both a software component and a tangible asset (e.g., hardware) component, how do we know whether to apply GASB No. 87 or GASB No. 96?</p> |
|--|

B. The meaning of *reasonably certain*

GASB No. 87 introduced the term **reasonably certain** into the GASB literature. Reasonably certain is used as the threshold for several decision points in applying GASB No. 87. The Basis for Conclusions to GASB No. 87 states that “the Board believes that the term **reasonably certain**, although also requiring the use of professional judgment, **is a higher threshold and is less speculative than probable.**” Thus, the GASB intends for this threshold to be rather high and certainly higher than just likely to occur. In practice, the course author has observed that many interpret this threshold to be in the 90% certainty range. Reasonably certain is also used throughout GASB No. 96 for several decision points relating to: (1) subscription term options; (2) fiscal funding clauses; and (3) the inclusion of certain payments in the subscription liability.

1. Exercise 2-6

Please answer the following question related to the reasonably certain threshold.

Reasonably certain

We just saw that **reasonably certain** is used throughout GASB No. 96 for several decision points relating to: (1) subscription term options; (2) fiscal funding clauses; and (3) the inclusion of certain payments in the subscription liability. We also saw that reasonably certain is a rather high threshold. Les C. Quandary is reviewing several SBITA contracts and determining whether options to extend or terminate should be included in the subscription term. **What are some factors Les will consider in determining whether the reasonably certain threshold has been met?**

C. The calculation of the *subscription term*

In implementing GASB No. 87, we saw the importance of properly calculating the **lease term**. In implementing GASB No. 96, the calculation of the **subscription term** is equally important. Fortunately, the concepts applied in calculating the term period are the same for both standards (i.e., we can leverage our leasing knowledge in implementing GASB No. 96). In general, the determination of the subscription term starts with the **non-cancellable period** since it is the period for which the government and SBITA vendor are legally obligated without the possibility of cancellation. Contracts may include options to extend or terminate the contract at or after a certain point in time. The subscription term will include certain **optional periods** based on the likelihood of those options being exercised. The goal of this approach is that the subscription term should reflect how long the SBITA is expected to be in effect. The following chart describes the GASB No. 96 subscription term calculation.

GASB No. 96 describes the *subscription term* as being...

The period during which a government has a noncancellable right to use the underlying IT assets (i.e., the **noncancellable period**), **plus** the following **optional periods**, if applicable:

- 1 Periods covered by a **government's option** to extend the SBITA if it is **reasonably certain**, based on all relevant factors, that the government **will exercise** that option;
- 2 Periods covered by a **government's option** to terminate the SBITA if it is **reasonably certain**, based on all relevant factors, that the government **will not exercise** that option;
- 3 Periods covered by a **SBITA vendor's option** to extend the SBITA if it is **reasonably certain**, based on all relevant factors, that the SBITA vendor **will exercise** that option; and
- 4 Periods covered by a **SBITA vendor's option** to terminate the SBITA if it is **reasonably certain**, based on all relevant factors, that the SBITA vendor **will not exercise** that option.


1. Exercise 2-7

Please indicate whether the following statements are true or false.

| | | True or False |
|----------|--|---------------|
| 1 | Periods for which both the government and the SBITA vendor have an option to terminate the SBITA without permission from the other party (or if both parties have to agree to extend) are cancellable periods and are excluded from the subscription term . | |
| 2 | Provisions that allow for the termination of a SBITA due to a violation of SBITA terms and conditions, such as a default on payments, are not considered options to terminate the SBITA. | |


2. Fiscal funding or cancellation clauses

Many governmental contracts include fiscal funding or cancellation clauses. Laws or regulations often require inclusion of a fiscal funding or cancellation clause, but the government, acting in good faith when it enters into an agreement, does not intend or expect to exercise that clause. GASB No. 96 provides guidance related to when fiscal funding or cancellation clauses should be factored into the subscription term calculation.

| | |
|---|--|
|  | <p>Should fiscal funding or cancellation clauses be factored into the subscription term?</p> <p>A fiscal funding or cancellation clause allows a government to cancel a SBITA, typically on an annual basis, if the government does not appropriate funds for the subscription payments. That type of clause should affect the subscription term only if it is reasonably certain that the clause will be exercised (i.e., funds will not be appropriated).</p> |
|---|--|

3. Reassessing the subscription term after the initial determination


As discussed in the following chart, after the initial subscription term is determined, the subscription term will be updated if the government or SBITA vendor elects to exercise an option or not to exercise an option **contrary** to the initial determination of the subscription term.

| | |
|---|---|
|  | <p style="text-align: center;">When should the subscription term be reassessed?</p> <p>Under GASB No. 96, a government will reassess the subscription term only if one or more of the following occur: (1) the government or SBITA vendor elects to exercise an option even though it was previously determined that it was reasonably certain that the government or SBITA vendor would not exercise that option; (2) the government or SBITA vendor elects not to exercise an option even though it was previously determined that it was reasonably certain that the government or SBITA vendor would exercise that option; or (3) an event specified in the SBITA contract that requires an extension or termination of the SBITA takes place.</p> |
|---|---|

Comparable to GASB No. 87's leasing guidance, we should also note that paragraphs 52 to 57 of GASB No. 96 provide guidance for when SBITAs are amended while the contract is in effect (e.g., SBITA modifications or SBITA terminations). That guidance is distinct from the remeasurement guidance in the prior chart.


D. The definition of a *short-term SBITA*

In an effort to reduce application costs, GASB No. 87 provides an exception to the recognition, measurement, and disclosure requirements for short-term leases. Fortunately, GASB No. 96 contains comparable guidance. The following chart discusses the formal GASB No. 96 definition of a short-term SBITA.

| | |
|---|--|
|  | <p style="text-align: center;">GASB No. 96 defines a <i>short-term SBITA</i> as being...</p> <p>A SBITA that, at the commencement of the subscription term, has a maximum possible term under the SBITA contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised. Periods for which both the government and the SBITA vendor have an option to terminate the SBITA without permission from the other party (or if both parties have to agree to extend) are cancellable periods and should be excluded from the maximum possible term. For a SBITA that has cancellable periods, such as a rolling month-to-month SBITA or a year-to-year SBITA, the maximum possible term of that SBITA is the noncancellable period, including any notice periods.</p> |
|---|--|

1. The benefit to SBITAs meeting the short-term SBITA exception

The benefit to SBITAs meeting the short-term SBITA exception will be more fully appreciated by the end of this chapter. However, it centers on easier accounting as illustrated in the following chart.

| | |
|---|---|
|  | Accounting for short-term SBITAs under GASB No. 96 |
| | For short-term SBITAs, governments will not recognize subscription liabilities or subscription assets. Instead, governments will recognize short-term subscription payments as outflows of resources (e.g., expense) based on the payment provisions of the SBITA contract. A government will recognize an asset if subscription payments are made in advance or a liability if subscription payments are to be made subsequent to the reporting period. A government will not recognize an outflow of resources for the period for which the SBITA vendor grants the right to use the underlying IT assets to the government free of charge (e.g., one or more months free). |

2. Exercise 2-8

Please indicate whether the following statements are true or false.

| | | True or False |
|----------|---|---------------|
| 1 | Maximum possible term assumes that all options to extend would be exercised and inherently would exclude all options to terminate. | |
| 2 | The short-term SBITA exception in GASB No. 96 may potentially come into play more frequently than the short-term lease exception does in GASB No. 87. | |

E. Contracts with multiple components

Consistent to the approach taken in GASB No. 87 with leases, if a SBITA contract contains multiple components, a government should account for each component as a separate SBITA or non-subscription component (e.g., maintenance services for the IT assets) and allocate the contract price to the different components. However, if it is not practicable to determine a best estimate for price allocation for some or all components in the contract, a government should account for those components as a single SBITA. Paragraphs 44 to 49 of GASB No. 96 provide detailed guidance on contracts with multiple components and paragraphs 50 and 51 provide detailed guidance on contract combinations.

F. Materiality

GASB No. 96 carries the typical GASB disclaimer that “the provisions of this Statement need not be applied to immaterial items.” While some may have wished that GASB No. 96 contain stated exceptions for “small ticket” SBITAs or SBITAs with a minimum number of users, the GASB did not feel that was an appropriate area to wade into. In looking at GASB No. 96 and materiality, governments will need to work through comparable issues to what they worked through in implementing GASB No. 87.

III. SBITA recognition, measurement, and disclosure

Conceptually, in a SBITA transaction, a government receives the legal right to use an underlying SBITA asset (e.g., access to a vendors' IT software and associated tangible capital assets) at the commencement of the subscription term. In exchange, the government promises to make payments over time for the right to use that underlying asset. Thus, the government has **financed** the acquisition of that legal right.

A. An overview of SBITA accounting

The SBITA recognition, measurement, and disclosure concepts found in GASB No. 96 are based on the concepts the GASB developed in GASB No. 87. In general, a government will recognize a **subscription liability** and a **subscription asset** (i.e., an intangible right-to-use asset) at the commencement of the subscription term, **unless** the SBITA is a short-term SBITA or a perpetual license. However, there are some nuance differences from GASB No. 87 due to the type of asset involved (e.g., additional guidance related to implementation costs). Sometimes, it's nice to know the destination before beginning the journey. The following chart provides an overview of where we are going in terms of accounting for SBITAs under GASB No. 96 that we will expand upon in the rest of the chapter.







| Overview of SBITA accounting | | |
|------------------------------|--|--|
| | Asset | Liability |
| Initial reporting | Intangible right-to-use subscription asset = subscription liability + prepayments + qualifying implementation costs | Subscription liability = PV of expected SBITA payments to be made over the subscription term |
| Subsequent reporting | Amortize the subscription asset into amortization expense over the shorter of the useful life of the IT asset or the subscription term | Reduce the subscription liability by the principal portion of SBITA payments. Recognize interest expense for the amortization of the discount on the subscription liability. |

B. Calculating the subscription liability

In applying GASB No. 96, we always start by calculating the subscription liability first (as the calculation of the subscription asset is dependent upon the liability calculation). Conceptually, the government's initial **subscription liability** will be measured at **the present value of subscription payments expected to be made during the subscription term**. However, since there are several different types of payments that may be required under a SBITA contract, the calculation of the subscription liability can become somewhat complex depending upon the terms of the contract.

Calculating the initial subscription liability

A government initially will measure the **subscription liability** at the **present value of subscription payments expected to be made during the subscription term**. Measurement of the subscription liability **will include the following**, if required by a SBITA:

| | |
|---|---|
|  | Fixed payments; |
|  | Variable payments that depend on an index or a rate (such as the Consumer Price Index or a market interest rate), measured using the index or rate as of the commencement of the subscription term; |
|  | Variable payments that are fixed in substance; |
|  | Payments for penalties for terminating the SBITA [if the subscription term reflects the government exercising: (1) an option to terminate the SBITA; or (2) a fiscal funding or cancellation clause]; |
|  | Any subscription contract incentives receivable from the SBITA vendor (if applicable, see paragraphs 42 and 43 of GASB No. 96); and |
|  | Any other payments to the SBITA vendor associated with the SBITA contract that are reasonably certain of being required based on an assessment of all relevant factors |

1. Exercise 2-9

Please indicate whether the following statements are true or false.


| | | True or False |
|----------|--|---------------|
| 1 | The payments considered in calculating the subscription liability under GASB No. 96 are identical to those found in GASB No. 87 related to the lease liability. | |
| 2 | Government X enters into a SBITA requiring annual payments of \$40,000 for three years. If in any given year, Government X has over 50 user seats utilizing the SBITA, an additional annual charge of \$750 is imposed per user seat. Only the three annual payments of \$40,000 should be included in the subscription liability. | |

2. Determining the discount rate

Since a government initially will measure the subscription liability at the **present value** of subscription payments expected to be made during the subscription term, a discount rate will be needed. Under GASB No. 96, the future subscription payments are required to be discounted using the interest rate the SBITA vendor charges the government, which may be the interest rate implicit in the SBITA. However, if the interest rate cannot be readily determined by the government, the government's estimated incremental borrowing rate (an estimate of the interest rate that would be charged for borrowing the subscription payment amounts during the subscription term) will be used. (**Note.** In practice, most governments will use their estimated incremental borrowing rate as they have done with GASB No. 87).

C. Accounting for the subscription liability over the subscription term

True to the concept that a SBITA is a financing, GASB No. 96 requires that a government recognize **interest expense** related to the amortization of the discount on the subscription liability.

| | |
|---|---|
|  | <p>In subsequent financial reporting periods...</p> <p>A government will calculate the amortization of the discount on the subscription liability and report that amount as an outflow of resources (e.g., interest expense) for those periods. Any subscription payments made will be allocated first to the accrued interest liability and then to the subscription liability.</p> |
|---|---|

Paragraphs 20-24 of GASB No. 96 discuss several conditions (e.g., a change in the subscription term) that require the subscription liability to be remeasured at subsequent reporting dates if the changes are expected to significantly affect the amount of the subscription liability. Those paragraphs also discuss certain circumstances that trigger reassessment of the discount rate used to measure the subscription liability. We should also note that paragraphs 52-57 discuss modifications and terminations of SBITAs while the contract is in effect.




1. Exercise 2-10

Please indicate whether the following statement is true or false.

| | | True or False |
|----------|--|---------------|
| 1 | A subscription liability is not required to be remeasured, nor is the discount rate required to be reassessed, solely for a change in a government's incremental borrowing rate. | |

D. Calculating the subscription asset

After calculating the subscription liability, a government will be in position to calculate the subscription asset. Conceptually, the initial **subscription asset** will be measured at **the amount of the initial subscription liability, plus payments made to the SBITA vendor before commencement of the subscription term, and certain implementation costs.**

| | |
|---|---|
| <p>Calculating the initial subscription asset</p> <p>A government initially will measure the subscription asset as the sum of the following, less any SBITA vendor incentives (if applicable, see paragraphs 42 and 43 of GASB No. 96) received from the SBITA vendor at the commencement of the subscription term:</p> | |
|  | The amount of the initial measurement of the subscription liability ; |
|  | Payments associated with the SBITA contract made to the SBITA vendor at the commencement of the subscription term, if applicable; and |
|  | Capitalizable initial implementation costs |

Payments before the commencement of the subscription term associated with the SBITA contract made to the SBITA vendor, as well as payments made for the capitalizable initial implementation costs before the commencement of the subscription term, should be reported as a prepayment (an asset). A prepayment to a SBITA vendor should be reduced by any incentives received from the same SBITA vendor before the commencement of the subscription term, if a right of offset exists. That prepayment should be reclassified as an addition to the initial measurement of the subscription asset at the commencement of the subscription term. If the SBITA vendor incentives are greater than the SBITA vendor prepayments made to the same vendor, the difference should be reported as a liability until the commencement of the subscription term, at which time that amount should reduce the initial measurement of the subscription asset.

1. Exercise 2-11

Please indicate whether the following statement is true or false.

| | | True or False |
|----------|--|---------------|
| 1 | City X enters into a three-year SBITA contract. City X provides payment in full at the commencement of the subscription term. City X will need to recognize interest expense during the term of the agreement. | |

2. Outlays other than subscription payments, including implementation costs

Paragraphs 29-40 of GASB No. 96 provide detailed guidance/criteria related to SBITA related outlays **other than subscription payments**, including implementation costs. The treatment for these outlays may vary depending upon whether the costs are incurred during: (1) the **preliminary project stage**; (2) the **initial implementation stage**; or (3) the **operation and additional implementation stage**. Capitalizable implementation costs (capitalized as part of the subscription asset) generally will be found during the **initial implementation stage**. The following chart discusses the three different stages of costs and the types of activities found in each stage.

| Outlays other than subscription payments | | |
|---|--|---|
| Activities associated with a SBITA (other than subscription payments) should be grouped into the following stages: | | |
| Preliminary project stage | Initial implementation stage | Operation and additional implementation stage |
| Activities in this stage include: (1) the conceptual formulation and evaluation of alternatives; (2) the determination of the existence of needed technology; and (3) the final selection of alternatives for the SBITA | Activities in this stage include: [1] ancillary charges related to designing the chosen path (e.g., configuration, coding, testing) and installation associated with the government’s access to the underlying IT assets; and [2] other ancillary charges necessary to place the subscription asset into service. Note. The initial implementation stage for the SBITA is completed when the subscription asset is placed into service. | Activities in this stage include: [1] maintenance, troubleshooting, and other activities associated with the government’s ongoing access to the underlying IT assets; and [2] additional implementation activities (e.g., those related to additional modules that occur after the subscription asset is placed into service) |

Note. Under Paragraph 31 of GASB No. 96, data conversion is considered an activity of the initial implementation stage **only** when necessary to place the subscription asset into service. Otherwise, data conversion is considered an activity of the operation and additional implementation stage.

Outlays other than subscription payments

Outlays related to the implementation of a SBITA may overlap or occur in multiple cycles and are recognized based on the **nature** and **timing** of the outlay (activity).

Preliminary project stage

Outlays expensed as incurred

Initial implementation stage

Outlays generally **capitalized as part of the subscription asset**

Outlays expensed as incurred if no subscription asset is recognized (e.g., a short-term SBITA)


Operation and additional implementation stage

Outlays expensed as incurred (unless they meet the specific capitalization criteria in GASB No. 96 paragraph 40)

Note. GASB No. 96 paragraph 39 specifies that **training costs should be expensed as incurred, regardless of the stage in which they are incurred**

E. Accounting for the subscription asset over the subscription term

Under GASB No. 96, a government will recognize **amortization expense** related to the subscription asset, representing the decrease in the useful life of the SBITA asset over the subscription term.

| | |
|---|---|
|  | In subsequent financial reporting periods... |
| | A subscription asset will be amortized in a systematic and rational manner over the shorter of the subscription term or the useful life of the underlying IT assets. The amortization of the subscription asset will be reported as an outflow of resources (e.g., amortization expense), which may be combined with depreciation expense related to other capital assets for financial reporting purposes. Amortization will begin at the commencement of the subscription term. |








A subscription asset generally will be adjusted by the same amount as the corresponding subscription liability when that liability is remeasured based on paragraphs 20-24 of GASB No. 96. However, if that change reduces the carrying value of the subscription asset to zero, any remaining amount will be reported in the resource flows statement (e.g., a gain).

F. The current financial resources measurement focus financial statements

Consistent with the approach taken with leases under GASB No. 87, GASB No. 96 discusses that if a SBITA is expected to be paid from general government resources, the SBITA will be accounted for and reported on a basis consistent with governmental fund accounting principles. An expenditure and other financing source will be reported in the period the subscription asset is initially recognized. The expenditure and other financing source will be measured as provided in paragraphs 16-18 of GASB No. 96. Subsequent governmental fund subscription payments will be accounted for consistent with principles for debt service payments on long-term debt.

G. SBITA disclosure requirements

As we alluded to earlier, GASB No. 96 requires notes to financial statements related to a government's SBITA arrangements. Overall, the required disclosures are comparable to the disclosures required by GASB No. 87. However, in a few aspects the disclosures are easier. For example: [1] governments do not have required disclosures related to residual value guarantees or purchase options because they are not relevant to SBITAs; and [2] for disclosure purposes, SBITAs may be grouped (i.e., rather than being broken down into major classes of underlying assets as is required for leases).

| GASB No. 96's SBITA disclosure requirements | |
|--|--|
| A government will disclose in notes to financial statements the following information about its SBITAs (which may be grouped for purposes of disclosure) other than short-term SBITAs: | |
|  | A general description of its SBITAs, including the basis, terms, and conditions on which variable payments not included in the measurement of the subscription liability are determined; |
|  | The total amount of subscription assets, and the related accumulated amortization, disclosed separately from other capital assets; |
|  | The amount of outflows of resources recognized in the reporting period for variable payments not previously included in the measurement of the subscription liability; |
|  | The amount of outflows of resources recognized in the reporting period for other payments, such as termination penalties, not previously included in the measurement of the subscription liability |
|  | Principal and interest requirements to maturity, presented separately, for the subscription liability for each of the five subsequent fiscal years and in five-year increments thereafter |
|  | Commitments under SBITAs before the commencement of the subscription term; and |
|  | The components of any loss associated with an impairment. |

Note. For disclosure purposes, subscription liabilities are not considered debt that is subject to the disclosure requirements in GASB No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*.

1. Exercise 2-12

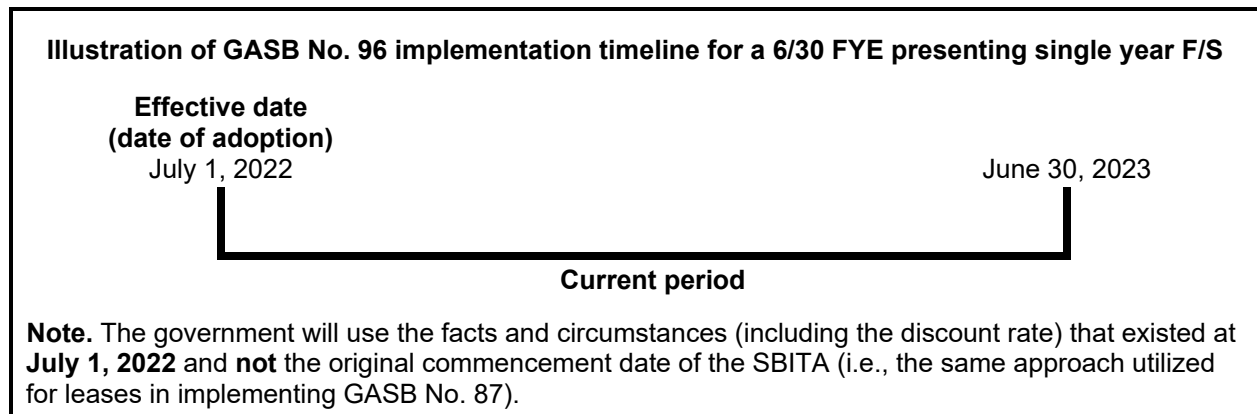
Please indicate whether the following statements are true or false.

| | | True or False |
|----------|--|---------------|
| 1 | GASB No. 96 provides some good illustrations of the SBITA note disclosures. | |
| 2 | The GASB No. 96 SBITA disclosures are required to be presented after the lease disclosures in the notes to the financial statements. | |

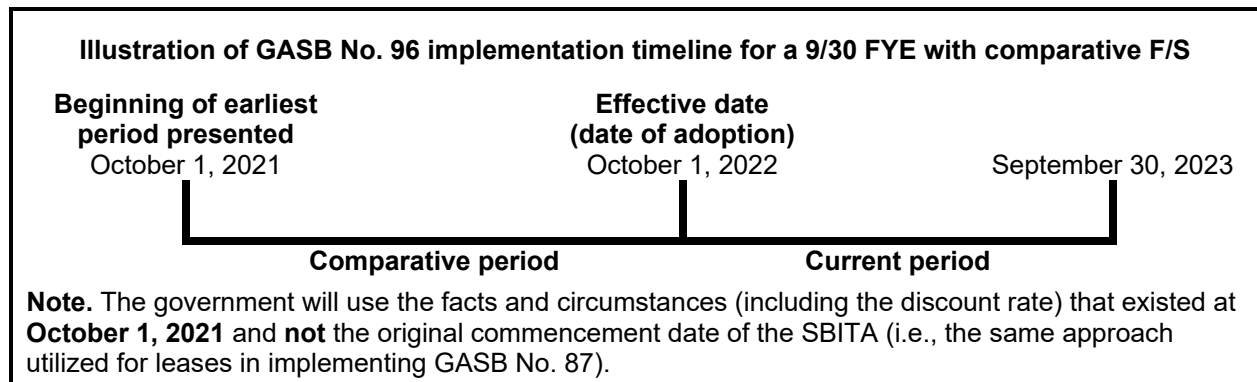
IV. Effective date and transition

The requirements of GASB No. 96 are effective for **fiscal years beginning after June 15, 2022**. Changes adopted to conform to the provisions of GASB No. 96 will be applied retroactively by restating financial statements, **if practicable**, for all prior fiscal years presented. If restatement for prior fiscal years **is not practicable**, the cumulative effect, if any, of applying GASB No. 96 will be reported as a restatement of beginning net position (or fund balance or fund net position, as applicable) for the earliest fiscal year restated. In the first fiscal year that GASB No. 96 is applied, the notes to financial statements will disclose the nature of the restatement and its effect. Also, the reason for not restating prior fiscal years presented will be disclosed.

SBITAs will be recognized and measured using the facts and circumstances **that existed at the beginning of the fiscal year in which GASB No. 96 is implemented**. If applied to earlier fiscal years, SBITAs will be recognized and measured using the facts and circumstances that existed at the beginning of the earliest fiscal year restated. Governments are permitted, **but are not required**, to include in the measurement of the subscription asset capitalizable outlays associated with the initial implementation stage and the operation and additional implementation stage incurred prior to the implementation of GASB No. 96. The following illustration shows the implementation timeline for a 6/30 fiscal year-end government presenting single year financial statements.



The following illustration shows the implementation timeline for a 9/30 fiscal year-end government presenting comparative financial statements.



A. Exercise 2-13

Please indicate whether the following statement is true or false.

| | | True or False |
|----------|---|---------------|
| 1 | The subscription liability should be measured using the remaining subscription term and discount rate as of the beginning of the fiscal year of implementation or the beginning of the earliest fiscal year restated. The subscription asset should be measured based on the subscription liability at that date. | |

V. A few parting thoughts about implementation

Without question, for many governments the implementation of GASB No. 87 was a significant challenge. As we have seen, the GASB No. 96 requirements are extremely similar to those found in GASB No. 87. Hopefully, the experience of persevering GASB No. 87 will help in implementing GASB No. 96. The following chart contains factors that might make the implementation of GASB No. 96 easier (+’s) **or** more difficult (-’s) than the implementation of GASB No. 87.

| Factors that may make the implementation of GASB No. 96 easier/more difficult than GASB No. 87 | |
|--|--|
| +’s | -’s |
| The requirements are very similar to GASB No. 87 (i.e., we have more knowledge going into the process) | The nature of the asset involved and the technical complexity of understanding it |
| SBITA agreements tend to be more centrally located within the government (i.e., reducing the time spent searching for agreements as we did with leases) | We may encounter more agreements that have a material service component that needs to be broken out compared to leases |
| SBITA agreements tend to be of shorter duration than many leases (i.e., perhaps more short-term SBITAs than leases or shorter subscription terms than leases) | Many governments issued single year f/s in implementing GASB No. 87 (as they did not want to restate the prior year). They may want to do comparative for GASB No. 96 (as they may perceive it to be a lesser “lift” than GASB No. 87) requiring additional work to restate the comparative year |
| Typically, fewer overall number of agreements to work through than leases | |

VI. Suggested solutions to exercises

This section contains the suggested solutions to the exercises presented in the chapter.

A. Suggested solution to Exercise 2-1

| | | True or False |
|----------|--|---|
| 1 | Government A enters into an arrangement with a vendor which conveys control of the right to use the vendor’s IT assets. Under the arrangement, Government A has remote access to software applications and cloud data storage. This would likely be a SBITA. | True , assuming the agreement was not a perpetual license. |

B. Suggested solution to Exercise 2-2

| | | True or False |
|----------|---|--|
| 1 | GASB No. 87 provides guidance for lessees and lessors. GASB No. 96 does the same thing for SBITAs (i.e., it provides guidance for government end users and governments that provide the right to use their IT assets to other entities through SBITAs). | False . GASB No. 96 applies to government end users but does not apply to governments that provide the right to use their IT assets to other entities through SBITAs. The GASB essentially felt that governments acting as vendors is not a prevalent enough practice at this point in time to warrant inclusion in GASB No. 96. |

C. Suggested solution to Exercise 2-3

Is this a SBITA? – Part 1

Government B enters into a 24-month agreement with Router-Router to provide 24/7 off-site live troubleshooting of basic IT problems and periodic training for Government B's employees. **This is probably a SBITA?**

No. The definition of a SBITA excludes contracts that solely provide IT support services. However, if the contract had contained both a right-to-use IT asset component and an IT support services component, the right-to-use IT asset component would be subject to GASB No. 96.

Is this a SBITA? – Part 2

Andy Auditor is meeting with Stuart (the client's IT Director). Stuart shows Andy an agreement entitled "Infrastructure as a Service." **This is probably a SBITA?**

Yes. One example of a typical SBITA is a cloud computing arrangement. Paragraph B14 of GASB No. 96 contains a good discussion of cloud computing arrangements. The three most common deployment models for cloud computing are Software as a Service (**SaaS**), Platform as a Service (**PaaS**), and Infrastructure as a Service (**IaaS**). All three models involve a SBITA vendor providing the customer with the right to use the SBITA vendor's IT resources, including its software application and cloud infrastructure (including network, servers, operating systems, storage, and other tools). **SaaS** provides a customer with the ability to use a SBITA vendor's applications (software) through a cloud infrastructure. **PaaS** allows a customer to use a SBITA vendor's tools or coding language (software) to create applications that will run on the SBITA vendor's cloud infrastructure. **IaaS** allows a customer to remotely access the SBITA vendor's network, server, and other fundamental computing tools to process, store, and operate the customer's data. Although those cloud computing deployment models are referred to by many as "as a Service," the economic substance of those arrangements is, in fact, the right to use vendors' IT assets. The reference to "services" in those models highlights the fundamental difference between the subscription models and the traditional purchasing and perpetual licensing models.

In the above, we worded the **question** "This is **probably** a SBITA" instead of "This is **definitely** a SBITA." The usage of "probably" instead of "definitely" was intentional as GASB No. 96 is a very substance over form standard and each arrangement must be reviewed individually. Governments will need to exercise professional judgment in looking at the definition of a SBITA and the elements included in that definition (i.e., **conveyance** of control, for a **period** of time, in an **exchange** or exchange-like transaction).

D. Suggested solution to Exercise 2-4

Is this for a period of time?

Anne Auditor is meeting with Sue (a client's IT Director). Sue shows Anne an agreement entitled "Software Subscription". The agreement calls for three annual payments of \$10,000 and in return the client is granted a perpetual license for the right to use a leasing software package. **Is this likely a SBITA?**

No. Some arrangements may be labeled by vendors as subscriptions because they involve an installment plan, but those arrangements do not, in fact, meet the definition of a SBITA if they grant a perpetual license for the right to use software indefinitely rather than for a finite period of time. This client would look to GASB No. 51, *Accounting and Financial Reporting for Intangible Assets*, for guidance.

E. Suggested solution to Exercise 2-5

Where things can get fuzzy

We just saw that GASB No. 96 **does not apply** to contracts that convey control of the right to use another party's combination of IT software and tangible capital assets that meets the definition of a lease in GASB No. 87 in which the software component is insignificant when compared to the cost of the underlying tangible capital asset (e.g., a computer with operating software or a smart copier that is connected to an IT system). **If an agreement has both a software component and a tangible asset (e.g., hardware) component, how do we know whether to apply GASB No. 87 or GASB No. 96?**

One way to think through this is: (1) if a contract is software alone you follow GASB No. 96; (2) if a contract has a **significant software component** compared to the hardware component you follow GASB No. 96; and (3) if a contract has an **insignificant software component** compared to the hardware component you follow GASB No. 87.

F. Suggested solution to Exercise 2-6

Reasonably certain

We just saw that **reasonably certain** is used throughout GASB No. 96 for several decision points relating to: (1) subscription term options; (2) fiscal funding clauses; and (3) the inclusion of certain payments in the subscription liability. We also saw that reasonably certain is a rather high threshold. Les C. Quandary is reviewing several SBITA contracts and determining whether options to extend or terminate should be included in the subscription term. **What are some factors Les will consider in determining whether the reasonably certain threshold has been met?**

Les will holistically consider factors such as: [1] the presence of a significant economic incentive (e.g., a contract contains a provision for an optional additional period that is favorable compared to current market rates); [2] a potential change in technological development that significantly affects the technology used by the underlying IT assets; [3] a potential significant change in the government's demand for the SBITA vendor's IT assets; [4] the presence of a significant economic disincentive (e.g., costs associated with terminating a SBITA and signing/implementing a new SBITA); [5] the government's history of exercising options to extend or terminate; and [6] the degree to which the underlying IT assets in the SBITA are essential to the provision of government services.

G. Suggested solution to Exercise 2-7

| | | True or False |
|----------|--|---|
| 1 | Periods for which both the government and the SBITA vendor have an option to terminate the SBITA without permission from the other party (or if both parties have to agree to extend) are cancellable periods and are excluded from the subscription term . | True. Paragraph 9 of GASB No. 96 specifies this and it is the same concept applied in GASB No. 87. |
| 2 | Provisions that allow for the termination of a SBITA due to a violation of SBITA terms and conditions, such as a default on payments, are not considered options to terminate the SBITA. | True. |

H. Suggested solution to Exercise 2-8

| | | True or False |
|----------|---|---|
| 1 | Maximum possible term assumes that all options to extend would be exercised and inherently would exclude all options to terminate. | True. Equally true is that cancellable periods would be excluded from the maximum possible term. |
| 2 | The short-term SBITA exception in GASB No. 96 may potentially come into play more frequently than the short-term lease exception does in GASB No. 87. | Likely true. Due to the inherent nature of technology, SBITA assets tend to have a shorter life than fixed assets which likely translates to shorter agreements. The GASB's pre-agenda research for GASB No. 96 indicated that the length of a SBITA term may vary from several months to 10 years but generally is from 1 to 5 years. |

I. Suggested solution to Exercise 2-9

| | | True or False |
|----------|--|--|
| 1 | The payments considered in calculating the subscription liability under GASB No. 96 are identical to those found in GASB No. 87 related to the lease liability. | Close to true but false. In calculating the lease liability under GASB No. 87 the lessee includes reasonably certain residual value guarantees and purchase options. Paragraph B29 of GASB No. 96 states that "SBITAs do not include provisions for residual value guarantees or purchase options and, consequently, such features are not included in the measurement of a subscription liability." |
| 2 | Government X enters into a SBITA requiring annual payments of \$40,000 for three years. If in any given year, Government X has over 50 user seats utilizing the SBITA, an additional annual charge of \$750 is imposed per user seat. Only the three annual payments of \$40,000 should be included in the subscription liability. | True. The three annual payments of \$40,000 should be included in the subscription liability as they are fixed/fixed in substance. Under GASB No. 96, variable payments based on future performance of a government, usage of the underlying IT assets, or number of user seats, will not be included in the measurement of the subscription liability. Rather, those variable payments will be recognized as expense in the period in which the obligation for those payments is incurred. |

J. Suggested solution to Exercise 2-10

| | | True or False |
|----------|--|--|
| 1 | A subscription liability is not required to be remeasured, nor is the discount rate required to be reassessed, solely for a change in a government's incremental borrowing rate. | True. The GASB specified this in paragraph 23 of GASB No. 96. |

K. Suggested solution to Exercise 2-11

| | | True or False |
|----------|--|--|
| 1 | City X enters into a three-year SBITA contract. City X provides payment in full at the commencement of the subscription term. City X will need to recognize interest expense during the term of the agreement. | False. Because City X provides payment in full at the commencement of the subscription, there is no subscription liability on which to base interest expense. In accordance with GASB No. 96 paragraph 25, City X would measure the subscription asset at the amount of the subscription payment made at the commencement of the subscription term. |

Note. The course author analogized the above to SBITAs from a lease question (4.9) in GASB Implementation Guide No. 2021-1.

L. Suggested solution to Exercise 2-12

| | | True or False |
|----------|--|---|
| 1 | GASB No. 96 provides some good illustrations of the SBITA note disclosures. | Unfortunately false. However, governments now have at least a general template per se having implemented GASB No. 87. |
| 2 | The GASB No. 96 SBITA disclosures are required to be presented after the lease disclosures in the notes to the financial statements. | False. The GASB has previously refrained from providing authoritative guidance on the placement of information within notes to financial statements and this is true for SBITAs as well. Paragraph B62 of GASB No. 96 discusses that the location of SBITA information, whether presented with lease disclosures, capital asset disclosures, or separately, should be left to professional judgment. |

M. Suggested solution to Exercise 2-13


| | | True or False |
|----------|---|---------------|
| 1 | The subscription liability should be measured using the remaining subscription term and discount rate as of the beginning of the fiscal year of implementation or the beginning of the earliest fiscal year restated. The subscription asset should be measured based on the subscription liability at that date. | True |

Other GASB Developments

| | |
|--|----|
| <i>Learning objectives</i> | 1 |
| <i>I. That's not all folks!</i> | 1 |
| <i>II. GASB No. 94</i> | 2 |
| A. What is GASB No. 94 addressing and why was it issued? | 2 |
| B. Understanding the terminology is critical to applying GASB No. 94 | 2 |
| C. Where to go for guidance | 5 |
| D. The PPP term under GASB No. 94 | 5 |
| E. Transferor accounting for PPPs under GASB No. 94 | 6 |
| F. Operator accounting for PPPs under GASB No. 94 | 7 |
| G. Additional PPP guidance contained in GASB No. 94 | 8 |
| H. Putting it all together | 8 |
| I. APA guidance contained in GASB No. 94 | 9 |
| <i>III. GASB No. 99</i> | 10 |
| A. Clarifications to GASB Nos. 87, 94 and 96 | 10 |
| B. Clarifications to other standards | 11 |
| <i>IV. GASB Nos. 100 and 101</i> | 11 |
| A. GASB No. 100 | 12 |
| B. GASB No. 101 | 12 |
| <i>V. Suggested solutions to exercises</i> | 13 |
| A. Suggested solution to Exercise 3-1 | 13 |
| B. Suggested solution to Exercise 3-2 | 14 |
| C. Suggested solution to Exercise 3-3 | 15 |
| D. Suggested solution to Exercise 3-4 | 15 |





Other GASB Developments

Learning objectives

| | |
|---|--|
|  | <p>Upon completing this chapter, you will have an understanding of additional GASB standards that governments are presently implementing and an overview of future developments.</p> |
|---|--|

I. That's not all folks!

Thus far, we have discussed the past and present impact of GASB No. 87 on governments. We also discussed the implementation of GASB No. 96 which governments will be applying throughout 2023. One might think that based on those developments alone, the GASB might pause and be content in terms of change in the short term. However, if one were to make that presumption, they would unfortunately be incorrect. The following chart lists the additional GASB developments that we will be discussing in this chapter and a flavor for what each development addresses.


| Additional GASB developments affecting governments in the near future | |
|---|--|
|  | <p>GASB No. 94, <i>Public-Private and Public-Public Partnerships and Availability Payment Arrangements</i> – Like GASB No. 96, governments will be applying GASB No. 94 during 2023. While GASB No. 94 will not apply to as many governments as GASB No. 96 does, it will definitely pose a challenge for certain governments and can be a difficult standard to work through.</p> |
|  | <p>GASB No. 99, <i>Omnibus 2022</i> – In recent years, the GASB has developed a bad habit of issuing omnibus statements (e.g., GASB Nos. 92 and 85) to address aspects of previously issued standards. In some cases, the omnibus statements are making meaningful changes to standards. However, in other cases, the changes seem to be more just clarifications or rewordings of concepts that are already being applied in practice. This makes the omnibus statements difficult to parse through and apply.</p> |
|  | <p>GASB No. 100, <i>Accounting Changes and Error Corrections – an amendment of GASB Statement No. 62</i> – GASB No. 100 almost feels more like a concepts statement than an accounting statement. Governments will essentially be applying GASB No. 100 in their 2024 year end statements.</p> |
|  | <p>GASB No. 101, <i>Compensated Absences</i> – GASB No. 101 updates the recognition and measurement guidance for all types of compensated absences under a unified model in large part in reaction to the paid-time-off (PTO) model that packages vacation and sick leave. Calendar year-end governments will be applying GASB No. 101 in 2024 and other governments will be applying it in 2025.</p> |

II. GASB No. 94

In March 2020, GASB No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, was issued to address public-private and public-public partnership arrangements (PPPs) and availability payment arrangements (APAs). [Note. In a bit of bad timing, throughout GASB No. 94, public-private and public-public partnership arrangements are referred to as “PPPs”; however, we are not talking about the SBA’s Paycheck Protection Program, which has dominated our vernacular since 2020.] GASB No. 94 supersedes GASB No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, and amends several standards. GASB No. 94 is effective for fiscal years beginning after June 15, 2022. Retroactive restatement is required, if practicable, for all prior fiscal years presented. When applying the standard, PPPs will be recognized and measured using the facts and circumstances that exist at the beginning of the period of implementation (or if applicable to earlier periods, the beginning of the earliest period restated).

A. What is GASB No. 94 addressing and why was it issued?

In recent decades, some governments have become more creative in terms of how they construct, maintain, and operate costly public projects.





| | |
|---|--|
|  | <p style="text-align: center;">Addressing a wide variety of collaborative arrangements</p> <p>GASB No. 94 addresses a wide variety of collaborative arrangements between a government and another party that can be used to finance, build, and operate projects that are normally capital in nature, with the overall objective of providing services to a government’s constituents. Examples of possible PPP arrangements could involve assets such as toll roads, bridges, parking lots, transportation terminals, public transit, hospitals, college dormitories, sports facilities, jails, wastewater treatment, and etc.</p> |
|---|--|

While guidance for the above types of collaborative arrangements previously existed under GASB No. 60, and in some cases GASB No. 87, the GASB believed that certain arrangements did not clearly fit into either GASB No. 60 or GASB No. 87, and that more all-encompassing guidance was needed (i.e., GASB No. 94). The GASB also believed that the GASB No. 60 model needed to be updated to better align with GASB No. 87 and that the changes warranted a new standard (i.e., GASB No. 94) rather than simply trying to amend GASB No. 60.

B. Understanding the terminology is critical to applying GASB No. 94

The good news about GASB No. 94 is that many governments are not affected by it; the bad news is that some governments are. While GASB No. 94’s requirements are not overly complex (i.e., in many cases the concepts in GASB No. 94 are comparable to GASB No. 87’s leasing guidance and/or the prior guidance in GASB No. 60), there is good amount of terminology which must be understood upfront to apply the standard. **The terminology in GASB No. 94 is critical as it drives the accounting and reporting path one takes in the standard.**

As discussed in the following chart, there are four definitions that are critical to applying GASB No. 94.

| Four definitions that are critical to applying GASB No. 94 | |
|---|---|
|  | GASB No. 87 defines a lease as being a contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction . |
|  | GASB No. 94 defines a PPP as being an arrangement in which a government (the transferor) contracts with an operator to provide public services by conveying control of the right to operate or use a nonfinancial asset, such as infrastructure or other capital asset (the underlying PPP asset), for a period of time in an exchange or exchange-like transaction . |
|  | <p>GASB No. 94 defines a service concession arrangement (SCA) as being a PPP arrangement between a transferor and an operator in which all of the following criteria are met:</p> <p style="margin-left: 40px;">The transferor conveys to the operator the right and related obligation to provide public services through the use and operation of an underlying PPP asset in exchange for significant consideration, such as an up-front payment, installment payments, a new facility, or improvements to an existing facility;</p> <p>a</p> <p style="margin-left: 40px;">b The operator collects and is compensated by fees from third parties;</p> <p style="margin-left: 40px;">The transferor determines or has the ability to modify or approve which services the</p> <p>c operator is required to provide, to whom the operator is required to provide the services, and the prices or rates that can be charged for the services; and</p> <p>d The transferor is entitled to significant residual interest in the service utility of the underlying PPP asset at the end of the arrangement.</p> |
|  | GASB No. 94 defines an APA as being an arrangement in which a government compensates an operator for activities that may include designing, constructing, financing, maintaining, or operating an underlying nonfinancial asset for a period of time in an exchange or exchange-like transaction. The payments by the government are based entirely on the asset's availability for use rather than on tolls, fees, or similar revenues or other measures of demand. |

Once again, the above terminology is critical as it drives the accounting and reporting path one takes in applying GASB No. 94.

1. Exercise 3-1

Please answer the following true or false questions.

| | | True or False |
|----------|---|----------------------|
| 1 | The definition of a SCA under GASB No. 94 is conceptually consistent with the definition of a SCA found in GASB No. 60 which it is superseding. | |
| 2 | All SCAs are PPPs but not all PPPs are SCAs. | |




2. Exercise 3-2

The below chart describes several types of arrangements between a government and another party. Based on the limited facts provided, please indicate whether the arrangement most likely represents: (1) a GASB No. 87 lease; (2) a PPP which is a SCA; (3) a PPP which is not a SCA; (4) an APA; or (5) something else altogether.

| | Description of arrangement | Is the arrangement: (1) a GASB No. 87 lease; (2) a PPP which is a SCA; (3) a PPP which is not a SCA; (4) an APA; or (5) something else altogether |
|----------|---|--|
| 1 | State A enters into an arrangement with the Boring Transit Authority (BTA) in which BTA has agreed to design and build a tunnel for State A and then operate the tunnel for 40 years. During the term of the arrangement, BTA is entitled to collect and retain tolls generated by the tunnel at the rates approved by State A. After 40 years, operation of the tunnel will be transferred to State A. | |
| 2 | School District B enters into an arrangement with Youth Sports Association (YSA) in which YSA is allowed to use School District B's sports facilities for four months a year for 10 years in exchange for consideration. | |
| 3 | City C enters into an arrangement with Park It Inc. (PII) to design, build, and finance the construction of a downtown parking garage. PII will collect all parking fees for 20 years and remit them to City C. City C will remit to PII \$4.5 million at the start of the project, \$4.5 million on the date the garage is placed into service, and \$250,000 annually for each of the 20 years that PII will operate the garage as compensation for designing, building, and financing the garage. City C also will remit \$50,000 per month during the 20 years to compensate PII for collecting the parking fees. | |
| 4 | Community College D enters into an arrangement with Bartwells Building (BB) in which BB will build and own a college dormitory for 30 years. In exchange for transferring ownership of the dormitory at the end of the arrangement, BB is allowed to set the price charged to students during the arrangement and retain the proceeds. | |
| 5 | County E enters into an arrangement with Grease And Go (GAG) to provide routine maintenance on its vehicle fleet for the next 5 years. | |


C. Where to go for guidance

Now that we have reviewed the four definitions that are critical to applying GASB No. 94 and also worked through some examples of different types of arrangements and how we might classify them, it is important that we discuss where we go to find accounting and reporting guidance for the various types of arrangements.

| Where do we go for accounting and reporting guidance? | |
|---|---|
|  | For PPPs which are SCAs we look to GASB No. 94 |
|  | For PPPs which are not SCAs <u>and</u> meet the definition of a lease , we look to the GASB No. 87 leasing guidance if: (1) existing assets of the transferor are the only underlying PPP assets; and (2) improvements are not required to be made by the operator to those existing assets as part of the PPP arrangement. For all other PPPs which are not SCAs we look to GASB No. 94 |
|  | For APAs we look to GASB No. 94 |

D. The PPP term under GASB No. 94

In implementing GASB No. 87, governments observed the importance of properly determining the **lease term**. In implementing GASB No. 94, properly determining the **PPP term** is of equal importance. The good news is that GASB No. 94 leverages many of concepts used in determining the lease term under GASB No. 87 to how we determine the PPP term under GASB No. 94. Paragraphs 10 to 13 of GASB No. 94 provide detailed guidance on how the PPP term is calculated. The following chart summarizes this guidance.

| Determining the PPP term | |
|---|--|
|  | The PPP term is defined as the period during which an operator has a noncancellable right to use an underlying PPP asset, plus , if applicable, certain periods if it is reasonably certain , based on all relevant factors, that the transferor or the operator either will exercise an option to extend the PPP or will not exercise an option to terminate the PPP . |

Similar to GASB No. 87, periods for which both the operator and the transferor have an option to terminate the PPP without permission from the other party (or if both parties have to agree to extend) are cancellable periods and are excluded from the PPP term. Also similar to GASB No. 87, fiscal funding clauses will only come into play when it is reasonably certain that the clause will be exercised. In considering whether optional periods of time are included in the PPP term, the economics involved are the primary driver in the reasonably certain criteria. GASB No. 94's guidance regarding situations requiring a reassessment of the PPP term are similar to GASB No. 87's guidance regarding situations requiring reassessment of the lease term.

1. Exercise 3-3

Please answer the following true or false question.

| | | True or False |
|----------|---|---------------|
| 1 | GASB No. 94 contains provisions related to short-term PPPs that are comparable to GASB No. 87's guidance regarding short-term leases. | |

E. Transferor accounting for PPPs under GASB No. 94

GASB No. 94 is written in a manner which addresses the accounting and reporting of PPPs from both the **transferor** (e.g., the government entering into a tollway arrangement with a tollway authority) and **operator** (e.g., the tollway authority entering into the tollway arrangement with the government) perspectives. In this section, we will briefly summarize how transferors account for PPPs under GASB No. 94 (**Note.** Detailed guidance in this area is found in paragraphs 14 to 36 of GASB No. 94). The following chart overviews the transferor accounting for PPPs in the economic resources measurement focus financial statements.

| Summarized view of transferor accounting for PPPs under GASB No. 94 | | |
|---|---|--|
| <p>Is the PPP asset an existing asset of the transferor? If so...</p> <p>Continue to report the underlying PPP asset</p> | <p>Is the PPP asset a new asset purchased or constructed by the operator in a PPP which is a SCA? If so...</p> <p>Recognize the new asset at acquisition value (when the asset is placed in service)</p> | <p>Is the PPP asset a new asset purchased or constructed by the operator in a PPP which is not a SCA? If so...</p> <p>Recognize a receivable for the new asset (when the asset is placed in service) measured based on the operator's estimated carrying value of the underlying PPP asset as of the expected date of the transfer in ownership</p> |
| <p>Recognize a receivable at PV for installment payments (if any) to be received from the operator</p> | <p>Recognize a receivable at PV for installment payments (if any) to be received from the operator</p> | <p>Recognize a receivable at PV for installment payments (if any) to be received from the operator</p> |
| <p>Recognize a deferred inflow of resources for the consideration received or to be received by the transferor (Note. This will be amortized into revenue in a systematic and rational manner over the PPP term)</p> | <p>Recognize a deferred inflow of resources for the consideration received or to be received by the transferor (Note. This will be amortized into revenue in a systematic and rational manner over the PPP term)</p> | <p>Recognize a deferred inflow of resources for the consideration received or to be received by the transferor (Note. This will be amortized into revenue in a systematic and rational manner over the PPP term)</p> |

For financial statements prepared using the current financial resources measurement focus, a transferor will recognize a receivable for installment payments and a deferred inflow of resources to account for a PPP. Governmental fund revenue would be recognized in a systematic and rational manner over the PPP term.

1. Exercise 3-4

Please answer the following true or false question.

| | |
|--|----------------------|
| | True or False |
| 1 GASB No. 94 contains disclosure requirements related to PPPs. | |

F. Operator accounting for PPPs under GASB No. 94




Having looked at transferor accounting under GASB No. 94, let us now summarize how governmental operators account for PPPs under GASB No. 94 (**Note.** Detailed guidance in this area is found in paragraphs 37 to 59 of GASB No. 94). The following chart overviews the operator accounting for PPPs in the economic resources measurement focus financial statements.

| Summarized view of operator accounting for PPPs under GASB No. 94 | | |
|--|---|--|
| <p>Is the PPP asset an existing asset of the transferor? If so...</p> <p>Report an intangible right-to-use asset related to the underlying PPP asset based on the amount of consideration to be provided to the transferor, plus any payments made to the transferor at or before the commencement of the PPP term, and certain direct costs. The right-to-use asset will be amortized into expense in a systematic and rational manner.</p> <p>Recognize a liability at PV for installment payments (if any) expected to be paid</p> | <p>Is the PPP asset a new asset purchased or constructed by the operator in a PPP which is a SCA? If so...</p> <p>Report an intangible right-to-use asset related to the underlying PPP asset based on the amount of consideration to be provided to the transferor, plus any payments made to the transferor at or before the commencement of the PPP term, and certain direct costs (Note. This amount would include the cost of the purchased or constructed PPP asset). The right-to-use asset will be amortized into expense in a systematic and rational manner.</p> <p>Recognize a liability at PV for installment payments (if any) expected to be paid</p> | <p>Is the PPP asset a new asset purchased or constructed by the operator in a PPP which is not a SCA? If so...</p> <p>Recognize the underlying PPP asset (including depreciation/impairment over time) until ownership of the asset is transferred to the transferor</p> <p>Recognize a liability (when the asset is placed in service) based on the estimated carrying value of the underlying PPP asset as of the expected date of the transfer in ownership</p> <p>Recognize a liability at PV for installment payments (if any) expected to be paid</p> <p>Recognize a deferred outflow of resources for the estimated carrying value of the underlying PPP asset as of the expected date of the transfer in ownership (Note. This will be amortized into expense in a systematic and rational manner over the PPP term)</p> |

For financial statements prepared using the current financial resources measurement focus, an operator will recognize an expenditure and other financing source in the period the PPP is initially recognized. Subsequent governmental fund PPP payments will be accounted for consistent with the principles for debt service payments of long-term debt.


G. Additional PPP guidance contained in GASB No. 94

In addition to providing the accounting and reporting guidance for PPPs from both the transferor and operator perspectives, GASB No. 94 (paragraphs 60 to 75) provides guidance related to PPPs with multiple components, PPP arrangement modifications, and PPP arrangement terminations. The following chart summarizes aspects of this guidance.

| Summarized additional PPP guidance contained in GASB No. 94 | |
|---|---|
|  | Governments should account for PPP and non-PPP components of a PPP as separate contracts. If a PPP involves multiple underlying assets, a transferor and an operator in certain cases should account for each underlying PPP asset as a separate PPP. If determining the best estimate of the components is not practicable, multiple components in a PPP should be accounted for as a single PPP. |
|  | GASB No. 94 requires an amendment to a PPP to be considered a PPP modification, unless the operator's right to use the underlying PPP asset decreases, in which case it should be considered a partial or full PPP termination. |
|  | A PPP termination should be accounted for by a transferor by reducing, as applicable, any receivable for installment payments or any receivable related to the transfer of ownership of the underlying PPP asset and by reducing the related deferred inflow of resources. An operator should account for a termination by reducing the carrying value of the right-to-use asset and, as applicable, any liability for installment payments or liability to transfer ownership of the underlying PPP asset. A PPP modification that does not qualify as a separate PPP should be accounted for by remeasuring PPP assets and liabilities. |

H. Putting it all together

We have reviewed the PPP accounting from the transferor and operator perspectives under GASB No. 94. To help bring these concepts together, the following illustration reflects the treatment of a PPP (in this case a new PPP asset constructed by the operator in a PPP which is a SCA) from both perspectives.

| Background facts for illustration | |
|---|--|
|  | Government Transferor (GT) enters into a PPP arrangement with Government Operator (GO) in which GO has agreed to design and build a bridge for GT and then operate the bridge for 30 years. During the term of the arrangement, GO is entitled to collect and retain tolls generated by the bridge. The arrangement meets all criteria in GASB No. 94 to qualify as a SCA. The cost to GO to construct the bridge is \$180 million. The acquisition value of the bridge when it is placed into service at the end of the current year is \$210 million. GO is not a component unit in GT's financial reporting entity. |


The following chart highlights the accounting for GT and GO related to the PPP arrangement.

Summary of GT's and GO's accounting for the PPP under GASB No. 94

| When: | The transferor's accounting: | The operator's accounting: |
|---|---|---|
| Accounting at the commencement of the PPP term and when the underlying PPP asset is placed into service | GT will recognize a \$210 million capital asset for the acquisition value of the bridge when it is placed into service and a \$210 million deferred inflow of resources | GO will recognize an intangible right-to-use asset in the amount of \$180 million (i.e., the cost to design and build the bridge) |
| Accounting in future years | GT will apply existing capital asset guidance, including depreciation, if applicable, to the bridge. If GT elects to use the straight-line method, it will recognize \$7 million (i.e., \$210 million divided by 30 years) in revenue and reduce the related deferred inflow of resources in the same amount each year of the arrangement | If GO elects to use the straight-line method of amortization, it will amortize the intangible asset and recognize expense in the amount of \$6 million each year (i.e., \$180 million divided by 30 years). GO will recognize revenue and expense on bridge operations based on applicable revenue and expense recognition guidance |

I. APA guidance contained in GASB No. 94

As we saw earlier, GASB No. 94 defines an **APA** as being an arrangement in which a government compensates an operator for activities that may include designing, constructing, financing, maintaining, or operating an underlying nonfinancial asset for a period of time in an exchange or exchange-like transaction. The payments by the government are based entirely on the asset's availability for use rather than on tolls, fees, or similar revenues or other measures of demand. The following chart summarizes the treatment of APAs under GASB No. 94 (**Note**. Detailed guidance in this area is found in paragraphs 76 to 83 of GASB No. 94).






| The treatment of APAs under GASB No. 94 | |
|---|--|
|  | <p>An APA that is related to designing, constructing, and financing a nonfinancial asset in which ownership of the asset transfers by the end of the contract will be accounted for by a government as a financed purchase of the underlying nonfinancial asset. GASB No. 94 requires a government that engaged in an APA that contains multiple components to recognize each component as a separate arrangement. An APA that is related to operating or maintaining a nonfinancial asset will be reported by a government as an outflow of resources in the period to which payments relate.</p> |

III. GASB No. 99

In April 2022, the GASB issued GASB No. 99, *Omnibus 2022*. In general, omnibus standards are designed to address aspects of previously issued standards and make sure that everyone is on the same page in applying a standard. For example, the Basis for Conclusions section of GASB No. 99 states that “The provisions in this Statement include several technical corrections that the Board believes will have little or no effect on the application of the underlying Statements that will be amended.”

A. Clarifications to GASB Nos. 87, 94 and 96








The amendments that GASB No. 99 makes to GASB Nos. 87, 94 and 96 are effective for fiscal years beginning after June 15, 2022. The following chart discusses the key GASB No. 99 clarifications to GASB No. 87.

| Key GASB No. 99 clarifications to GASB No. 87 | |
|---|---|
|  | An option to purchase the underlying asset should be considered an option to terminate that should be taken into account in the evaluation of the lease term. For example, a 5-year lease contains a lessee option to purchase the asset at the end of year 3. If the lessee is reasonably certain of exercising that option , we would look at this lease as having a 3-year lease term. |
|  | An option to terminate is an unconditional right that exists within the lease contract. A provision that gives a lessee or lessor the right to terminate the lease only in certain circumstances or upon the occurrence of certain events, such as the action or inaction of the other party to the lease contract, should not be considered an option to terminate the lease for purposes of determining the lease term. For example, provisions that allow for the termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease. |
|  | Periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party (or if both parties have to agree to extend) are cancellable periods and should be excluded from the maximum possible term . |
|  | Governments should not remeasure a lease liability or a lease asset solely for a change in an index or a rate used to determine variable payments, nor should the discount rate be reassessed solely for a change in the lessee’s incremental borrowing rate. |
|  | The GASB No. 99 Basis for Conclusions discusses that the GASB acknowledges that a government may circumvent the leasing provisions by entering into a new short-term lease rather than modifying an existing short-term lease. However, GASB No. 99 states that a lease that previously had been determined to be short-term and that has been modified to extend the initial maximum possible term under the lease contract should be reassessed from the inception of the lease. If the reassessed maximum possible term is greater than 12 months, the lease should no longer be considered a short-term lease. For a lease that is reclassified from a short-term lease, the lease term should be assessed beginning at the date of the modification for purposes of measuring the lease receivable or lease liability. |

Important Note. The above key clarifications to GASB No. 87 were generally also carried over into GASB Nos. 94 and 96 when relevant.

B. Clarifications to other standards

The following chart summarizes the clarifications GASB No. 99 made to other standards. In general, except for the clarifications to GASB Nos. 53 and 70 (which are effective for fiscal years beginning after June 15, 2023), these clarifications became effective upon the issuance of GASB No. 99.

| Clarifications GASB No. 99 made to other standards | |
|---|---|
|  | GASB No. 53, <i>Accounting and Financial Reporting for Derivative Instruments</i> – GASB No. 99 clarifies the treatment for a derivative that is neither an investment nor hedging derivative instrument. GASB No. 99 also provides an update for the treatment upon termination of hedge accounting. |
|  | GASB No. 70, <i>Accounting and Financial Reporting for Nonexchange Financial Guarantees</i> – GASB No. 99 establishes the recognition threshold for liabilities related to exchange and exchange-like financial guarantees is when a payment is more likely than not to occur. |
|  | GASB No. 93, <i>Replacement of Interbank Offered Rates</i> – GASB No. 99 provides guidance as to derivative instruments and the end of LIBOR as an appropriate benchmark. |
|  | GASB No. 33, <i>Accounting and Financial Reporting for Nonexchange Transactions</i> - GASB No. 99 clarifies that the accounting for Supplemental Nutrition Assistance Program transactions should follow the guidance in GASB No. 33 (i.e., the guidance on the recognition of assets for government-mandated or voluntary nonexchange transactions). |
|  | GASB No. 48, <i>Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues</i> – GASB No. 99 adds guidance to address the process of blending a component unit created to issue debt on behalf of a primary government when that component unit is required to be presented as a blended component unit. |
|  | GASB No. 62, <i>Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements</i> - GASB No. 99 makes a minor clarification to the disclosure requirements of nonmonetary transactions. |
|  | GASB No. 34 – <i>Basic Financial Statements</i> – GASB No. 99 attempts to reduce potential confusion regarding the applicability of requirements for government-wide financial statements to display information about the overall reporting government when a total column is not presented. |

IV. GASB Nos. 100 and 101

Having discussed GASB standards that governments are presently implementing (i.e., GASB Nos. 94, 96 and 99), we want to briefly give an overview of a couple of standards that governments will be applying in the next few years.

A. GASB No. 100

In June 2022, the GASB issued GASB No. 100, *Accounting Changes and Error Corrections - an Amendment of GASB Statement No. 62*. GASB No. 100 is effective for accounting changes and error corrections made in fiscal years beginning after June 15, 2023. GASB No. 100 defines four categories of changes/corrections and outlines the presentation, disclosure, and effects on RSI & SI for each category: [1] changes in accounting principles (retroactive restatement); [2] corrections of errors in previously issued financial statements (retroactive restatement); [3] changes in accounting estimates (prospectively recognizing the change in the current period); and [4] changes to or within the financial reporting entity (adjusting beginning balances of the current period).

B. GASB No. 101

In June 2022, the GASB issued GASB No. 101, *Compensated Absences*. GASB No. 101 is effective for fiscal years beginning after December 15, 2023. GASB No. 16 (the primary guidance we currently have for compensated absences) was issued in 1992 before the growing paid-time-off model (PTO) that packages vacation and sick leave became popular and the GASB believed there was some inconsistencies in how governments are accounting for PTO. GASB No. 101 aligns the recognition and measurement guidance for all types of compensated absences under a unified model that will result in governments recognizing a liability that more appropriately reflects when they incur an obligation for compensated absences. Under GASB No. 101, a liability will generally be recognized when the leave: (1) is attributable to services already rendered; (2) accumulates; and (3) is more likely than not to be used for time off or otherwise paid or settled.

V. Suggested solutions to exercises

This section contains the suggested solutions to the exercises presented in the chapter.

A. Suggested solution to Exercise 3-1

| | | True or False |
|----------|---|---|
| 1 | The definition of a SCA under GASB No. 94 is conceptually consistent with the definition of a SCA found in GASB No. 60 which it is superseding. | True. |
| 2 | All SCAs are PPPs but not all PPPs are SCAs. | True. As seen in the definition of a SCA, all SCAs are PPPs. However, there may also be PPPs which are not SCAs. For example, an arrangement where an operator constructs and owns a new capital asset to provide additional governmental services and in exchange for transferring ownership of the capital asset to the transferor at the end of the arrangement, the operator is allowed to set the price or rate that will be charged to users of the capital asset during the arrangement. |

B. Suggested solution to Exercise 3-2

| | Description of arrangement | Is the arrangement: (1) a GASB No. 87 lease; (2) a PPP which is a SCA; (3) a PPP which is not a SCA; (4) an APA; or (5) something else altogether |
|----------|--|---|
| 1 | <p>State A enters into an arrangement with the Boring Transit Authority (BTA) in which BTA has agreed to design and build a tunnel for State A and then operate the tunnel for 40 years.</p> <p>During the term of the arrangement, BTA is entitled to collect and retain tolls generated by the tunnel at the rates approved by State A. After 40 years, operation of the tunnel will be transferred to State A.</p> | PPP which is a SCA |
| 2 | <p>School District B enters into an arrangement with Youth Sports Association (YSA) in which YSA is allowed to use School District B's sports facilities for four months a year for 10 years in exchange for consideration.</p> | GASB No. 87 lease |
| 3 | <p>City C enters into an arrangement with Park It Inc. (PII) to design, build, and finance the construction of a downtown parking garage. PII will collect all parking fees for 20 years and remit them to City C. City C will remit to PII \$4.5 million at the start of the project, \$4.5 million on the date the garage is placed into service, and \$250,000 annually for each of the 20 years that PII will operate the garage as compensation for designing, building, and financing the garage. City C also will remit \$50,000 per month during the 20 years to compensate PII for collecting the parking fees.</p> | APA |
| 4 | <p>Community College D enters into an arrangement with Bartwells Building (BB) in which BB will build and own a college dormitory for 30 years. In exchange for transferring ownership of the dormitory at the end of the arrangement, BB is allowed to set the price charged to students during the arrangement and retain the proceeds.</p> | PPP which is not a SCA |
| 5 | <p>County E enters into an arrangement with Grease And Go (GAG) to provide routine maintenance on its vehicle fleet for the next 5 years.</p> | Something else altogether [i.e., it's an agreement for services and not: (1) a lease; (2) a PPP which is a SCA; (3) a PPP which is not a SCA; or (4) an APA] |

C. Suggested solution to Exercise 3-3

| | | True or False |
|---|---|--|
| 1 | GASB No. 94 contains provisions related to short-term PPPs that are comparable to GASB No. 87's guidance regarding short-term leases. | False. While the GASB decided that the guidance related to measuring the lease term should generally be applied to measuring the PPP term, the GASB believes that short-term arrangements do not occur in PPPs. |

D. Suggested solution to Exercise 3-4

| | | True or False |
|---|---|---|
| 1 | GASB No. 94 contains disclosure requirements related to PPPs. | True (the GASB loves disclosures). GASB No. 94 has disclosure requirements for both transferors and operators. However, they are not as bad as you might presume. One nice thing that GASB No. 94 does is provide illustrative disclosures (in its Appendix C) if the standard applies to you. |

Latest Developments

This chapter is reserved for additional materials to be added throughout the year as appropriate. As this course went to press there were no latest developments to include.

