

OHIO AUDITOR OF STATE KEITH FABER



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TO: All Public Offices
Independent Public Accountants

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SUBJECT: GASB 96, *Subscription-Based Information Technology Arrangements (SBITAs)*

Background Information

The Governmental Accounting Standards Board (GASB) issued GASB Statement No. 96, *Subscription-Based Information Technology Arrangements*, in May 2020. This statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for governments. GASB 96 defines a SBITA; establishes that a government generally should recognize a right-to-use subscription asset—an intangible asset—and a corresponding subscription liability; provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and requires note disclosures regarding a SBITA. (GASB 96 Summary) GASB 96 and subsequent amendments and guidance are codified in GASB Codification S80.

The requirements of this statement apply to all Ohio state and local governments that prepare financial statements following generally accepted accounting principles (GAAP). Applicability to Non-GAAP entities is addressed later in this bulletin.

Effective Date

The requirements of GASB 96 are effective for fiscal years beginning after June 15, 2022, and all reporting periods thereafter. Therefore, governments in Ohio are required to implement GASB 96 beginning with fiscal years ended June 30, 2023, and ending December 31, 2023.

Additional Guidance

GASB has also issued Implementation Guide No. 2023-1, Implementation Guidance Update--2023 which contains questions 4.7 to 4.9 to clarify the provisions of GASB 96. These questions are being incorporated into the Comprehensive Implementation Guide, Chapter Z as they become effective. Many of the concepts found in GASB 96 are similar to those found in GASB 87, *Leases*; therefore, the corresponding GASB 87 implementation guidance can also be referenced.

In addition, in April 2022, GASB issued Statement No. 99, *Omnibus 2022*, which includes additional provisions related to SBITAs. The provisions in this statement applicable to SBITAs are effective for fiscal years beginning after June 15, 2022, unless implemented earlier.

The guidance contained within this Bulletin contains only a portion of the above guidance and the basic requirements of GASB 96. Readers of this Bulletin are strongly encouraged to review GASB 96 and the aforementioned implementation guidance in full given the complexity of the statement.

GASB 96 Definition of a SBITA

Under GASB 96, a SBITA is defined as 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. (GASB 96 ¶ 6) The components of this definition are particularly important in determining whether a contract is considered a SBITA under these provisions. A contract must meet this definition in its entirety in order to qualify for reporting as a SBITA.

Contract

SBITAs include contracts that, although not explicitly identified as SBITAs, meet the definition of a SBITA. The definition excludes contracts that solely provide IT support services but includes contracts that contain *both* a right-to-use IT asset component and an IT support services component. (GASB 96 ¶ 8)

Conveys Control of the Right to Use

To determine whether a contract conveys control of the right to use the underlying IT assets, a government should assess whether it has both of the following:

- The right to obtain the present service capacity from use of the underlying IT asset as specified in the contract
- The right to determine the nature and manner of use of the underlying IT asset as specified in the contract.

(GASB 96 ¶ 7)

Exchange or Exchange-Like Transactions

In order to meet the definition of a SBITA under GASB 96, the substance of the transaction must be an exchange or exchange-like transaction. An exchange and exchange like transaction represents a transaction in which each party gives up essentially equal value. (GASB 33 ¶ 1)

Exclusions

The requirements of GASB 96 do not apply to the following:

- 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 Statement No. 87, *Leases*, in which the software component is insignificant when compared to the cost of the underlying tangible capital asset (for example, 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 definition of a public-private and public-public partnership in paragraph 5 of Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*
- Licensing arrangements that provide a perpetual license to governments to use a vendor’s computer software, which are subject to Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, as amended.

(GASB 96 ¶ 4)

Subscription Term

The subscription term is the period during which a government has a noncancelable right to use an underlying asset (referred to as the noncancelable period), plus the following periods, if applicable, based on all relevant factors and reasonable certainty:

Period covered by option of:	Option to:	Reasonably certain:
Government	Extend the SBITA	Lessee will exercise the option
Government	Terminate the SBITA	Lessee will NOT exercise the option
SBITA Vendor	Extend the SBITA	Lessor will exercise the option
SBITA Vendor	Terminate the SBITA	Lessor will NOT exercise the option

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 cancelable periods and are excluded from the subscription term. For example, a rolling month-to-month SBITA, or a SBITA that continues into a holdover period until a new SBITA contract is entered into, would not be enforceable if both the government and the SBITA vendor have an option to terminate and, therefore, either could cancel the SBITA at any time. (GASB 96 ¶ 9) GASB 99 ¶ 23 further explains that an option to terminate is an unconditional right that exists within the SBITA contract and clarifies that a provision that gives a party to the SBITA the right to terminate the SBITA contract only in certain circumstances (for example, a default on payments) should not be considered an option to terminate for the purposes of determining the SBITA term.

Provisions that allow for termination of a SBITA due to the following are not considered termination options (GASB 96 ¶ 9):

- Payment of all sums due, or
- Default on payment.

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. This type of clause should affect the subscription term only if it is reasonably certain that the clause will be exercised. (GASB 96 ¶ 10)

Short-Term SBITAs

A short-term SBITA, 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. A government should recognize short-term subscription payments as outflows of resources (for example, expense) based on the payment provisions of the SBITA contract. (GASB 96 ¶¶ 13-14)

GASB 99 ¶ 24 provides the following clarifications regarding short-term SBITAs:

- A SBITA should be reassessed from the inception of the SBITA contract if the SBITA was previously determined to be short-term but has been modified to extend the initial maximum possible term under the SBITA contract. After this reassessment, if the maximum possible SBITA term is greater than 12 months, the SBITA should no longer be considered short-term.
- If a SBITA is reclassified from a short-term SBITA (see previous bullet point), the SBITA term should be assessed beginning at the date of modification for purposes of measuring the subscription liability.

SBITA Accounting – Government

A government should recognize a subscription liability and a subscription asset at the commencement of the subscription term, which is when the subscription asset is placed into service. The subscription liability should initially be measured at the present value of subscription payments expected to be made during the subscription term. The subscription asset should be

measured as the sum of the initial subscription liability amount, plus payments made to the SBITA vendor before commencement of the subscription term and capitalizable implementation costs, less any incentives received from the SBITA vendor at or before the commencement of the subscription term. (GASB 96 Summary)

A government should reduce the subscription liability as payments are made and recognize an outflow of resources (for example, expense) for interest on the liability. The government should amortize the subscription asset in a systematic and rational manner over the shorter of the subscription term or the useful life of the underlying IT asset. The notes to financial statements should include descriptive information about its SBITAs other than short-term SBITAs, such as the amount of the subscription asset, accumulated amortization, other payments not included in the measurement of a subscription liability, principal and interest requirements for the subscription liability, and other essential information. Additional details on disclosure requirements are included later in the bulletin. (GASB 96 Summary)

Government Accounting	
Initial Measurement	Subsequent Measurement
<p>Subscription Liability The measurement of the subscription liability should include the following if required by a SBITA:</p> <ul style="list-style-type: none"> • Fixed payments • Variable payments that depend on an index or a rate • 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 termination the SBITA or (2) a fiscal funding or cancellation clause • Any subscription contract incentives receivable from the SBITA vendor (refer to GASB 96 ¶¶ 42-43) • Any other payments that are reasonably certain of being required based on an assessment of all relevant factors <p>(GASB 96 ¶16)</p> <p>The future subscription payments should be discounted using the interest rate the SBITA vendor charges the government, which may be the interest rate implicit in the SBITA. If the interest rate cannot be readily determined by the government, the government's</p>	<p>For subsequent financial reporting periods, the government should calculate the amortization of the discount on the subscription liability and report that amount as an outflow of resources (for example, interest expense) for those periods. Any subscription payments made should be allocated first to the accrued interest liability and then to the subscription liability. (GASB 96 ¶ 19) In other words the ending subscription liability for the period will represent the beginning subscription liability less the principal portion of payments made. Interest expense for the reporting period will represent the interest portion of subscription payments made plus accrued interest at the end of the period less accrued interest at the beginning of the period.</p> <p>A subscription asset should 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 should be reported as an outflow or resources (for example, amortization expense), which may be combined with depreciation expense related to other capital assets for financial reporting purposes. (GASB 96¶ 27)</p>

<p>estimated incremental borrowing rate (an estimate of the interest rate that would be charged for borrowing the subscription payment amounts during the subscription term) should be used. (GASB 96 ¶ 18)</p> <p>Government Subscription Asset A government should initially measure the subscription asset as the sum of the following:</p> <ul style="list-style-type: none"> • The amount of the initial measurement of the subscription liability (see above) • Payments associated with the SBITA contract made to the SBITA vendor at the commencement of the subscription, if applicable • Capitalizable initial implementation costs as described in GASB 96¶29b <p>(GASB 96 ¶ 25)</p>	<p>If a subscription asset is impaired (refer to GASB 42), the amount reported for the subscription asset should be reduced first for any change in the corresponding subscription liability. Any remaining asset should be recognized as an impairment (GASB 96 ¶ 41)</p> <p>Therefore, the ending subscription asset should be equal to the beginning subscription asset less any amortization expense that is recognized during the period less an impairment loss recognized during the period (if any).</p>
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Initial Implementation Costs

As mentioned above, a subscription asset should include capitalizable initial implementation costs. Activities associated with a SBITA, other than making subscription payments, should be grouped into the following three stages, and their costs should be accounted for accordingly:

- Preliminary Project Stage, including activities such as evaluating alternatives, determining needed technology, and selecting a SBITA vendor. Outlays in this stage should be expensed as incurred.
- Initial Implementation Stage, including all ancillary charges necessary to place the subscription asset into service. Outlays in this stage generally should be capitalized as an addition to the subscription asset.
- Operation and Additional Implementation Stage, including activities such as subsequent implementation activities, maintenance, and other activities for a government’s ongoing operations related to a SBITA. Outlays in this stage should be expensed as incurred unless they meet specific capitalization criteria.

In classifying certain outlays into the appropriate stage, the nature of the activity should be the determining factor. Training costs should be expensed as incurred, regardless of the stage in which they are incurred. See GASB 96 ¶¶ 29-40 for additional information. (GASB 96 Summary)

Expense Recognition

GASB 96 requires that a government recognize interest expense related to the amortization of the discount on the subscription liability. A government also should recognize amortization expense related to the subscription asset, representing the decrease in the useful life of the right to use the underlying IT asset over the subscription term. The amortization of the subscription asset should

be calculated in a systematic and rational manner. This is consistent with depreciation and amortization of other capital assets. The interest expense and amortization expense are reported in the resource flows statements with other interest and depreciation or amortization expense amounts. (GASB 96 ¶ 19 and ¶ 27)

Governmental Funds

An expenditure and other financing source should be recognized in the period the subscription asset is initially recognized. Subsequent payments should be accounted for consistent with principles for debt service payments on long-term debt. (GASB 96 ¶ 59)

Notes to the Financial Statements

GASB 96 ¶ 60 identifies the following disclosures about SBITAs, 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.
- The components of any loss associated with an impairment (the impairment loss and any related change in the subscription liability, as discussed in GASB 96 ¶ 41).

SBITA Accounting – Transition

SBITAs should be recognized and measured using the facts and circumstances that existed at the beginning of the period of implementation. (GASB 96 ¶64) For example, a school district implementing GASB 96 for fiscal year 2023 should recognize and measure any SBITAs which existed prior to the fiscal year using the facts and circumstances that existed as of July 1, 2022.

SBITA Accounting – Other

GASB 96 contains additional information to the above topics that are not covered within this Bulletin, including, but not limited to:

- Incentives Provided by a SBITA Vendor
- Contracts with Multiple Components
- Contract Combinations

- SBITA Modifications and Terminations

For specific guidance related to these topics please refer to GASB 96 or GASB Codification S80.

Applicability to Non-GAAP Entities

GASB 96 requires the recognition of certain subscription liabilities for contracts that meet the GASB 96 definition of a SBITA.

These subscription liabilities will not be recognized on regulatory statements or on OCBOA cash basis (unmodified); therefore, regulatory and OCBOA cash basis (unmodified) filers will only need to incorporate changes to their Notes to the Basic Financial Statements. When preparing the Notes to the Basic Financial Statements, for both regulatory and OCBOA cash basis (unmodified), the following note disclosures should be made:

- the summary of significant accounting policies should describe the accounting treatment for SBITAs

For OCBOA modified cash basis, modifications for subscription liabilities should only be made when the transaction follows a cash transaction, there is substantial support in GAAP or other accounting literature, and the modification is logical. Since not all OCBOA modified cash basis preparers will elect to make this modification for subscription liabilities, note disclosures should be made as follows:

- If a local government is electing to make a modification for GASB 96 because the GASB 96 SBITA follows a cash transaction, the corresponding disclosure requirements from GASB 96 should be made.
- If an OCBOA modified cash basis preparer is electing not to make the GASB 96 modifications, the OCBOA cash basis (unmodified) disclosures identified above should be made.

Additional Resources Available on the Auditor of State's Website

The Auditor of State's Office has a Frequently Asked Questions (FAQ) document available related to the implementation of GASB 96 on our website at:

<https://ohioauditor.gov/references/gasbfaqs.html>

This document contains frequently asked questions related to the implementation of GASB 96 and will be updated as additional information becomes available.

Questions

If you have any questions regarding the information presented in this Bulletin, please contact Local Government Services at (800) 345-2519 or ContactLGS@ohioauditor.gov.

A handwritten signature in black ink that reads "Keith Faber". The signature is written in a cursive, flowing style.

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