August 19, 2019

Mr. David Bean, Director of Research and Technical Activities  
Project Number 38  
Governmental Accounting Standards Board  
401 Merritt 7, P.O. Box 5116  
Norwalk, CT 06856-5116

Submitted via email to director@gasb.org

Dear Mr. Bean:

Thank you for the opportunity to provide these comments regarding the proposed statement of the Governmental Accounting Standards Board (GASB, the Board), Subscription-Based Information Technology Arrangements (ED, the ED). The Board is to be commended for taking this step toward establishing guidance relating to subscription-based information arrangements (SBITA/SBITAs) and to eliminate diversity in practice relating to such arrangements. I appreciate this opportunity to respond and my comments reflect my views as a former government finance officer and a current academician responsible for teaching undergraduate and graduate level courses in governmental accounting and auditing.

Although a bit unwieldy, I commend, and agree with, the Board for using the term “subscription-based information technology arrangements” over the more commonly used phrase “cloud computing” as SBITAs can be more comprehensive than hosting services typically associated with “cloud computing”. I also commend, and agree with, the Board for aligning the proposed requirements for SBITAs with those in GASB Statement No. 87, Leases. In addition, I commend, and agree with, the Board proposing requirements for SBITA software assets similar to the requirements in GASB Statement No. 51, Accounting and Financial Reporting for Intangibles. Incorporating current guidance into the proposed guidance for SBITAs should minimize the “learning curve” for state and local governments and their auditors.

However, I strongly believe the proposed statement is excessively complex and it will not eliminate diversity in practice. My reasons for this are outlined below.

Excessive Complexity Concerns

Other than delineating “…hardware, software, or a combination of both…” the definition of a SBITA in the ED is virtually the same as the definition of a lease in Statement No. 87. Additionally, the accounting for SBITAs proposed in the ED is almost the same as for leases in Statement No. 87. It seems reasonable to assume a government would be able to bifurcate a SBITA between the hardware and software components without undue burden. As such, I believe Statement No. 87 should be amended to specifically include the hardware component of a SBITA¹. Under this approach, the definition of a SBITA in the ED would need to be modified to only include the “…right to use another party’s software”. A bifurcation approach to SBITAs would avoid unnecessary complexities in accounting and would better report the underlying substance of a government’s right to use another party’s hardware.

I understand amending Statement No. 87 to include intangibles such as software could be problematic; however, I encourage the Board to consider this in lieu of the accounting proposed in the ED. The

¹ If such an approach were taken, I would recommend a later effective date for applying the requirements of Statement No. 87 to hardware included in a SBITA.
accounting proposed in the ED as applied to the software component of a SBITA is still excessively complex especially in light of the similarities in the definitions of a SBITA and a lease and the accounting therefore. Alternatively, the Board might consider an approach similar to the one taken by the Financial Accounting Standards Board (FASB) in Accounting Standards Update (ASU) 2015-05, *Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement*. This ASU was part of the FASB’s Simplification Project the major impetus for which was user feedback about the complexity of financial reporting for certain transactions, including intangibles. Many analysts use financial statements of governmental and nongovernmental entities. I believe it would be less confusing, and might provide this user group more useful information for their decision making, if the accounting for the software component of a SBITA by governments was consistent with Statement No. 87 or with the accounting utilized by nongovernmental entities.

As proposed in the ED, I believe the requirement to report a “subscription asset” (par. 57 (b)) and a “subscription liability” (par. 57 (e)) separate from other capital assets and long-term debt provides no significant benefit to the users of government financial statements. The substance of the SBITA is the government has the right to use a capital asset for which it has incurred related long-term debt. In addition, I do not believe the amounts required to be disclosed in par. 57 (c) and (d) provide useful information (nor likely material information) for decision making nor does this information provided useful evidence of accountability. The disclosures in par. 57 (f), if material, would likely be discussed in the Management’s Discussion and Analysis in the next year’s facts and circumstances section. As such, also requiring this information in the notes would be redundant. If this requirement is carried forward to the final standard, it should clarify it relates only to material commitments related to material SBITAs. The level of detail delineated in par. 57 provides little benefit for the effort required to separately report SBITAs from other capital assets and long-term debt.

While not within the scope of this project, I believe, in the future or as part of the Disclosure Framework project, the Board should consider one capital asset note. This note would include all capital asset transactions whether the underlying assets were acquired through purchase, financing, lease, or SBITA. I believe the same disclosure compression should be considered for long-term debt as well. In doing this, it a user would be able to find all the information about capital assets and long-term debt in one location in the notes. As such, it might be easier to assess the investment a government has made in its capital assets as well as how leveraged a government may be whether due to funds for capital assets or other public purposes.

**Diversity in Practice Concerns**

While I (still) don’t agree with the Board’s definition of an asset, as defined in Concepts Statement No. 4, *Elements of Financial Statements*, I do agree certain SBITAs, as defined in the ED, may meet this definition of an asset. However, other SBITAs may not meet the definition of an asset due to the control requirement. In some SBITAs, the government does not “control” the underlying hardware and/or software other than to make a decision to procure the use of such through a SBITA. A SBITA for software, for example, may automatically include updates to the software and the government has no control over the content of the update nor are they able to opt out of such updates. Similarly, a government may not control hardware capacity provided under a cloud-based SBITA hosting arrangement because the level of capacity is at the discretion of the SBITA provider and not the government. The ED does not appear to define nor address how a government would account for SBITAs

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2 The discussion in par. B16 assumes the government has the discretion to decide when, and to what extent a vendor’s hardware or software will be used. Some SBITAs include a restriction on this discretion in certain circumstances which are typically enumerated in the contract. For example, the vendor may restrict a government’s use of cloud hosting services during peak usage times or during a natural disaster.
not meeting the definition of a SBITA. I believe diversity in practice might be mitigated if the final standard defines these types of SBITAs and/or clarifies the accounting for SBITAs not meeting the definition of an asset.

Generally, I believe the proposed requirements will create confusion among financial statement users because of the similarities between accounting for and reporting SBITAs and leases. In addition, the proposed accounting for SBITAs represents another difference between accounting standards utilized by governmental and nongovernmental entities. I believe the financial statement user community routinely compares government capital assets and related debt to private sector counterparts and vice versa. The substance of a lease is the same regardless of the form of the lease or the type of lessee and the same is true for SBITAs and cloud-computing arrangements. It seems the accounting and reporting of these arrangements should be consistent between governmental and nongovernmental entities. Minimizing the differences between accounting for SBITAs by governmental and cloud computing arrangements by nongovernmental entities would provide more useful information for decision making by the creditor/analyst stakeholder group.

Proposed Effective Date

The proposed effective date is extremely aggressive. Governments have dealt with the retrospective implementation of a number of complex standards (pensions, other post-employment benefits, and fiduciary activities) over the last several years. Currently governments are preparing to retrospectively implement the requirements of Statement No. 87 which is likely to require a significant commitment of capital and human resources for many governments. The accounting and financial reporting changes relating to SBITAs are also likely to require significant time to implement properly and still issue financial statements on a timely basis. As such, I think the proposed effective date should be no earlier than for fiscal years beginning after June 15, 2022.

Alternatively, if the final standard does not change significantly from the ED, the Board could consider requiring prospective application rather than retrospective application of the final standard. The term for a number of SBITAs is relatively short compared to other long-term debt agreements thus providing little benefit for the cost involved in providing retrospective information. Another alternative might be to allow either a retrospective or prospective application, at the choice of the government, of the final standard which is similar to what was allowed under ASU 2015-05. Either of these alternatives would appear to provide a tremendous amount of relief to state and local governments and their auditors.

Concluding Remarks

Overall, I am confused as to why this ED was issued as a stand-alone standard when it proposes accounting and reporting requirements which are basically the same as those for leases in Statement No. 87. It appears a significant amount of staff and Board time was spent on the project when amending Statement No. 87 would have been a more efficient method of providing guidance to account for and report SBITAs.

As always, thank you for the opportunity to respond to this due process document. Should you have any questions regarding the above, please contact me at (321) 277-1536 or lkmdennis@gmail.com.

Sincerely,

Lynda M. Dennis, CPA, CGFO, PhD