

Florida Government Finance Officers Association



Challenges With Recently Issued Statements

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The views expressed in this presentation are those of Mr. Skelton and Ms. Parker.
Official positions of the GASB are reached only after extensive due process and deliberations.

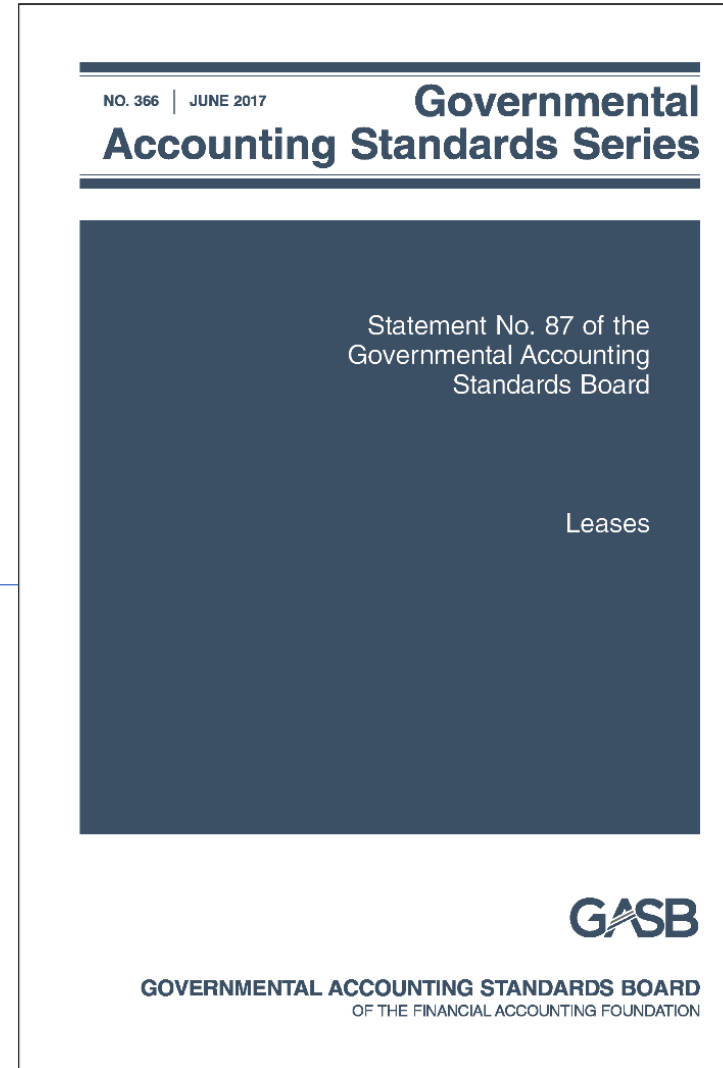
Materiality

Included in EVERY Statement:

The provisions of this Statement need not be applied to immaterial items.

Leases

Statement No. 87



Is this a short-term lease or SBITA?

- A short-term lease is a lease that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months or less, including any options to extend, regardless of their probability of being exercised.
 - 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 agreed to extend) are cancellable periods and should be excluded from the maximum possible term
 - A lease that had previously 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
- A short-term SBITA is defined the same way! Short-term lease implementation guidance can therefore be used for both!

Is this a short-term lease—2020 Implementation Guidance Update

4.9. Q—A government enters into a three-year lease contract. However, both the lessee and the lessor have a right to cancel at any time with 60 days' advance notice. For purposes of determining whether this lease is a short-term lease, what is the maximum possible term?

A—The maximum possible term is 60 days. Paragraph 16 of Statement 87 states, “for a lease that is cancelable by either the lessee or the lessor . . . the maximum possible term is the noncancelable period, including any notice periods.” In this example, there is no noncancellable period other than the notice period. Therefore, the maximum possible term is only the notice period of 60 days, and the lease is a short-term lease.

Is this a short-term lease—2020 Implementation Guidance Update

4.10. Q—A governmental housing authority enters into a 12-month residential lease contract that states the lessee may renew. If the lessee decides to renew, the housing authority and the lessee will enter into a separate lease contract at a later date for the subsequent 12-month period. Is the existing 12-month residential lease contract a short-term lease under Statement 87?

A—Yes. Paragraph 16 of Statement 87 provides that a short-term lease has a maximum possible term *under the contract* of 12 months or less, including any options to extend. Although the lease contract states that the lessee may renew, the lessee does not have a unilateral right to extend the existing contract because the housing authority and the lessee would enter into a new contract for the subsequent 12 months. Therefore, the maximum possible term under the existing contract is 12 months, and the lease is a short-term lease.

Is this a short-term lease—2020 Implementation Guidance Update

4.11. Q—A city leases boat slips in its marina to boat owners. Each lease is for 12 months and does not contain an option to extend. A certain boat owner has signed a new lease every year for the past 20 years, and the city expects her to continue to do so. Is this a short-term lease?

A—Yes. Whether a lease is a short-term lease depends on the terms of the contract. The history of new leases being signed every year and the likelihood of a new lease being signed next year are not relevant for making the determination of whether a lease is a short-term lease.

Is this a short-term lease—2023 Implementation Guidance Update

4.1. Q—A lease contract states that it will remain in effect for three years unless terminated before then. The contract allows the lessee to terminate the lease for any reason with 60 days' notice. The contract allows the lessor to terminate the lease with 60 days' notice only if the lessee defaults on payments. Is this a short-term lease?

A—No. The lessee has an unconditional right to terminate and, therefore, has an option to terminate. The lessor does not have an unconditional right to terminate because the lessor is allowed to terminate the lease only on the condition that the lessee defaults on payments and, therefore, does not have an option to terminate. Accordingly, there are no periods for which both the lessee and the lessor have an option to terminate and, therefore, no cancellable periods to exclude from the maximum possible term, which is three years.

Is this a short-term lease—2023 Implementation Guidance Update

4.2. Q—A lease has a noncancellable period of 36 months, and the lessee has an option to extend the lease for an additional 12 months. At the commencement of the lease, it is not reasonably certain that the lessee will exercise that option. At the end of the noncancellable period, the lessee exercises the option to extend the lease. Does exercising the option to extend result in a change to the maximum possible term?

A—No. In accordance with paragraph 16 of Statement No. 87, *Leases*, the maximum possible term at the commencement of the lease includes all options to extend, regardless of their probability of being exercised. At the commencement of the lease, the maximum possible term is 48 months, whereas the lease term is 36 months. When the lessee exercises the option to extend, the lease term is reassessed to be 12 months. However, the maximum possible term remains 48 months when the option is exercised.

Is this a short-term lease—2023 Implementation Guidance Update

4.3. Q—In what circumstances does a lease modification (as described in paragraph 71 of Statement 87) result in a short-term lease?

A—There are two circumstances in which a lease modification results in a short-term lease:

- a. If the lease was a short-term lease before the modification and the maximum possible term after the modification to extend the lease (reassessed from inception as described in paragraph 12 of Statement No. 99, *Omnibus 2022*) is 12 months or less, then the lease remains a short-term lease.
- b. Regardless of whether the lease was a short-term lease before the modification, if the modification meets the criteria in paragraph 72 of Statement 87 to be accounted for as a separate lease and the maximum possible term of that separate lease is 12 months or less, then the modification results in a separate short-term lease.

How do I report prepaid rent?

- There is no such thing as prepaid rent once a lease commences.
- An exchange transaction takes place at the commencement of the lease and payments made after that are financing a transaction that has already taken place
- Lease payments made before the commencement of the lease are reported as a prepayment, which then becomes part of the lease asset at commencement
- Lease payments made after the commencement of the lease (even if in advance of their due date per the contract) first reduce any accrued interest and then reduce the lease liability

How do I report prepaid rent—2020 Implementation Guidance Update

4.16. Q—A governmental lessor receives payments related to a building lease during a construction period before the lessee gains access to the building. How are those payments reported by the lessor?

A—The lessor should recognize a liability at the time the payments are received from the lessee. At the commencement of the lease term, the liability should be reduced, and the payments should be included in the initial measurement of the deferred inflow of resources to the extent that they relate to future periods in accordance with paragraph 53b of Statement 87.

If a lease/SBITA is modified and the lease/subscription liability and asset are increased, is anything recognized in governmental funds?

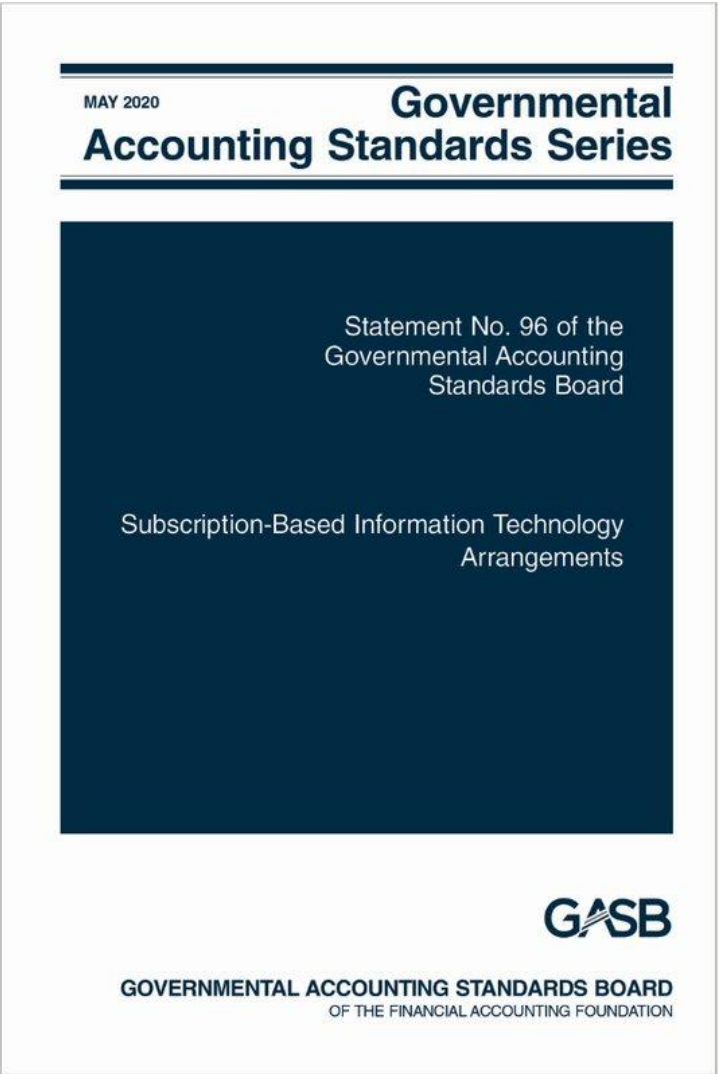
- There is no authoritative guidance on this
- Approach taken when developing the standard was to carryforward existing guidance for capital leases in governmental funds and to not develop further guidance – Financial Reporting Model Improvements (FRM) project was developing concepts for governmental funds
 - Governmental funds were removed from the FRM project
 - Advice – be consistent for all leases/SBITAs

How do I account for leasehold improvements?

- **It depends** on who is paying for them, who owns them, and whether they are part of the lease exchange transaction
- Very facts and circumstances based:
 - Sometimes leasehold improvements are done by the tenant for the landlord as part of the consideration for the lease. ("We'll charge less rent in cash if you do these improvements.")
 - The improvements then are considered lease payments (lease payments don't have to be cash).
 - But other times they're not part of the lease transaction and then general capital asset guidance applies.
 - If the tenant pays for them and owns them, they're the tenant's assets.
 - If the landlord pays for them and tenant owns them, it might be a lease incentive.

Subscription-Based Information Technology Arrangements

Statement No. 96



Scope and Applicability

A subscription-based information technology arrangement (SBITA) “is 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.”

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

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

Scope and Applicability

- Statement 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 Statement 87, in which the software component is insignificant compared to the cost of the underlying tangible capital asset
 - 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 P3 in Statement 94
 - Licensing arrangements that provide a perpetual license to governments to use a vendor's computer software, which are subject to Statement 51

Is this a perpetual license—2023 Implementation Guidance Update

4.7. Q—Is a licensing agreement for a vendor’s computer software that automatically renews until cancelled a licensing agreement that provides a perpetual license?

A—No. A provision under which a licensing agreement automatically renews until cancelled is an option to terminate the agreement at each renewal date. An agreement that includes an option to terminate is not a purchase, whereas a perpetual license is a purchase in which a government is granted a permanent right to use the vendor’s computer software. Therefore, a licensing agreement for a vendor’s computer software that automatically renews until cancelled does not provide a perpetual license.

Combination of Software and Hardware—2023 Implementation Guidance Update

4.8. Q—For purposes of determining the applicability of Statement 96, do Software as a Service, Platform as a Service, and Infrastructure as a Service contain a combination of IT software and tangible capital assets?

A—Yes. Software as a Service, Platform as a Service, and Infrastructure as a Service are three common deployment models of cloud computing arrangements. Notwithstanding the labels of those arrangements, each deployment model contains IT software used in combination with tangible capital assets. To further assess the applicability of Statement 96, the substance of the arrangement should be evaluated in accordance with all aspects of paragraph 6 of that Statement to determine whether the arrangement meets the definition of a subscription-based information technology arrangement (SBITA).

Relationship between Leases and SBITAs

- All SBITAs meet definition of lease
- Depends on what the underlying asset is:
 - Tangible capital assets alone – Statement 87
 - IT software alone – Statement 96
 - IT software in combination with tangible capital assets:
 - Software component is insignificant compared to cost of underlying tangible capital asset – Statement 87
 - Otherwise – Statement 96

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GFOA's Award Program

Leases & SBITAs

Review Comments Provided—Leases & SBITAs



- New leases and SBITAs result are noncash financing activities that should be included in the schedule of noncash investing and financing activities that accompanies the Statement of Cash Flows for proprietary funds
- Total direct debt displayed in the debt capacity schedules in the statistical section should include all long-term debt instruments, including lease and subscription liabilities
- The calculation of net investment in capital assets should include the long-term debt related the acquisition, construction, development, and improvement of capital assets, *including lease and subscription liabilities*
- If a lease results in a lessee recognizing a lease asset, or a SBITA results in a subscription asset, the cash flows (including the interest portion) of payments should be *included in the capital and related financing activity* on the statement of cash flows
- In governmental funds – New leases and SBITAs should result in other financing sources and capital expenditures equal to the lease liability that would be reported on a full accrual, economic resources MFBA

Review Comments Provided—Leases & SBITAs (cont.)



- Capital asset roll-forward note disclosure
 - Should clearly include lease assets and SBITA assets
 - Should disclose the amount of lease assets and their related accumulated amortization by major classes of underlying assets, separately from other capital assets
 - Should disclose subscription assets and their related accumulated amortization in their own classification of capital assets
 - Should clearly display lease and subscription assets as sub-classification of capital assets and include them in the reported total capital assets
 - Reiterated and built-on by GASB 104 requirements

Review Comments Provided—Leases & SBITAs (cont.)



- Government *lessees* and governments in SBITAs often
 - Fail to provide a schedule of future principal and interest requirements to maturity, or more broadly,
 - Fail to provide all required information in note disclosures
- Government *lessors* often
 - Fail to provide the required note disclosures specific to regulated leases, where applicable, or more broadly,
 - Fail to provide all required information in note disclosures

Review Comments Provided—Leases



- Lessees should disclose the amount of lease assets by major classes of underlying assets, separately from other (owned) capital assets in the capital asset roll-forward note disclosure (reiterated in GASB 104).
- No more capital leases – just “leases”
 - Misnamed leases may really be financed purchases, which are not leases
- Intangible right-to-use assets are properly referred to as “lease assets” *not* “leased assets”
 - Other names, such as “intangible rights to use leased assets,” are also appropriate

Review Comments Provided—Leases (cont.)

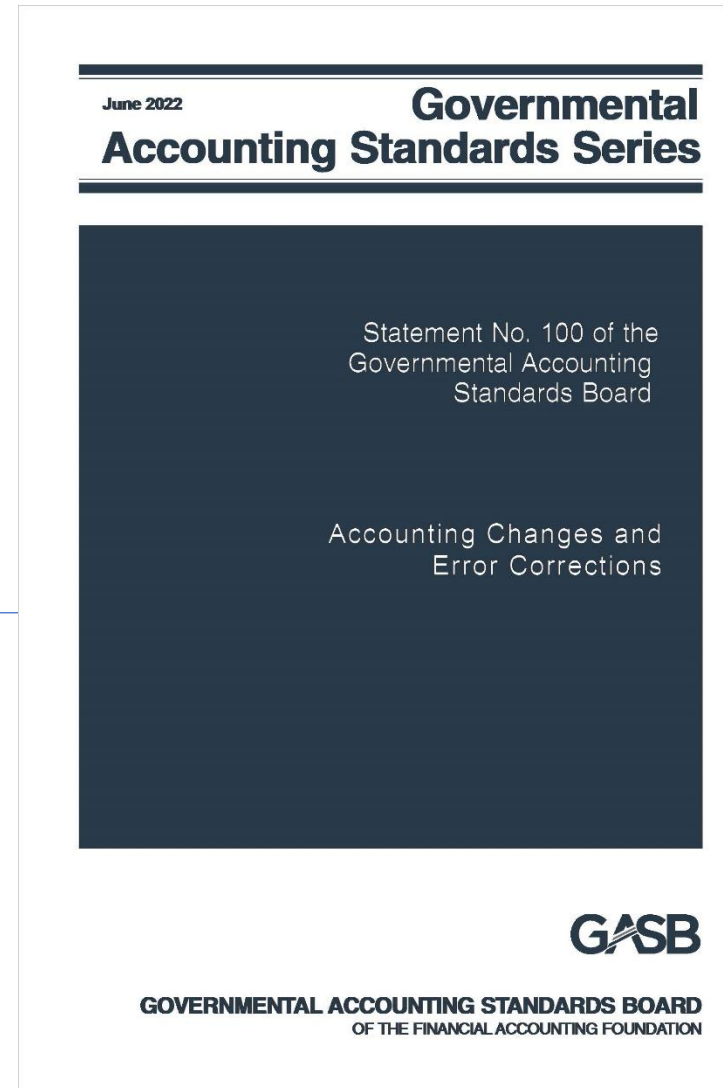


Note: there are fewer comments given to lessors because there are fewer government lessors than lessees

- Lessors should recognize lease receivables and deferred inflows of resources upon inception – *both in governmental funds* and in all financial statements prepared using economic resources/full accrual MFBA

Accounting Changes and Error Corrections

Statement No. 100



Change in Accounting Principle

- A change in accounting principle **results from either:**
 - A **change** from one generally accepted accounting principle to another that is justified on the basis that the newly adopted accounting principle is preferable
 - Preferability based on the qualitative characteristics of financial reporting
 - Implementation of new pronouncements.

Is this a change in accounting principle—2025 Implementation Guidance Update

4.11. Q—Is a change in a government’s capitalization threshold a change in accounting principle as defined in Statement 100?

A—No. A capitalization threshold is the application of materiality to a specific asset class, not an accounting principle. Therefore, the requirements of Statement 100 for a change in accounting principle, including the requirement to restate beginning balances, as appropriate, do not apply to that change.

Change to or within the Financial Reporting Entity

- A change to or within the financial reporting entity results from:
 - Addition/removal of a fund that results from movement of continuing operations within the primary government, including its blended component units
 - A change in the fund presentation as major or nonmajor
 - Addition/removal of a component unit (except for acquisitions, mergers, and transfers of operations, and Statement 90 component units)
 - Change in presentation (blended or discrete) of a component unit.

Is this a change to or within the financial reporting entity—2023 Implementation Guidance Update

4.10. Q—Upon completion of a capital project during the year, a government closes out a major capital projects fund and moves remaining resources to the general fund. Does this circumstance constitute a change to or within the financial reporting entity?

A—No. Even though the capital projects fund will no longer be included in the government’s financial reports in future periods (that is, the fund will be removed for financial reporting purposes), it does not constitute a change to or within the financial reporting entity in accordance with paragraph 9a of Statement 100 because, in this case, the removal of the fund does not result from a movement of continuing operations. Instead, that movement of remaining resources to the general fund should be reported as interfund activity in accordance with paragraph 112 of Statement 34, as amended.

Display in the financial statements—2025 Implementation Guidance Update

4.12. Q—Can an individual adjustment to or restatement of beginning net position, fund balance, or fund net position be displayed separately from the remaining aggregate of adjustments to or restatements of those beginning balances?

A—No. Paragraph 31 of Statement 100 requires display of the aggregate of all adjustments and restatements. Accordingly, unless each accounting change and each error correction is separately displayed in the financial statements in accordance with the exception permitted by paragraph 32 of Statement 100 (in addition to the aggregate amount as required by paragraph 31), a single line item presenting the sum of all adjustments to and restatements of beginning balances for each reporting unit should be displayed.

What about what some call a ghost column—2025 Implementation Guidance Update

4.13. Q—How should a change in a fund’s presentation from major to nonmajor be displayed in the financial statements?

A—Paragraph 31 of Statement 100 requires that the aggregate adjustments to and restatements of beginning net position, fund balance, or fund net position, as applicable, be displayed separately by reporting unit. As a result, a column should continue to be presented in the statement of revenues, expenditures, and changes in fund balances or the statement of revenues, expenses, and changes in fund net position, as applicable, that displays (a) the fund’s beginning balance as previously reported in the major column and (b) the adjustment to that balance, even though that column does not present activity for the reporting period. Correspondingly, in the statement of revenues, expenditures, and changes in fund balances or the statement of revenues, expenses, and changes in fund net position, as applicable, the column that presents nonmajor funds in the aggregate also should display the adjustment to its beginning balance.

What about what some call a ghost column—2025 Implementation Guidance Update

4.14. Q—Would the answer to Question 4.13 be different if the major fund no longer exists as a result of the movement of continuing operations, for example, a major enterprise fund will be reported as part of the general fund (instead of as a result of a change in fund presentation as described in Question 4.13)?

A—No. Consistent with the answer in Question 4.13, in the example in this question, a column should continue to be presented in the statement of revenues, expenses, and changes in fund net position that displays (a) the enterprise fund’s beginning balance as previously reported in the major column and (b) the adjustment to that balance, even though that column does not present activity for the reporting period. Correspondingly, in the statement of revenues, expenditures, and changes in fund balances, the column that presents the general fund also should display the adjustment to its beginning balance.

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GFOA's Award Program Accounting Changes and Error Corrections

Review Comments Provided—Restatements



- The terms “adjustments” and “restatements” have replaced the term “prior period adjustments,” which should no longer be used
 - On financial statements
 - In note disclosures
 - In required supplementary information (MD&A, notes to other RSI)
 - In other supplementary information (letter of transmittal, statistical section)

Review Comments Provided—Display Requirements



Governments should present the following for each affected reporting unit on a position statement

1. The applicable beginning positions (net position, fund balance, fund net position) as previously reported and
2. Either (a) a single line item presenting the aggregate of all adjustments to and/or restatements of applicable beginning positions*, or (b) individual line items for each accounting change and error correction individually.

*If aggregated, a table must be included in note disclosures providing details (later slide)

Review Comments Provided—Display Requirements (cont.)



- Restatements and adjustments should be presented immediately following the beginning position balance as previously reported
- For changes in the reporting entity, governments often fail to include the appropriate additional reporting units (i.e., “ghost columns” for previously included reporting units) necessary to show the change on the face of financial statements
- GFOA requires similar displays of ghost columns in combining financial statements in ACFRs

Review Comments Provided—Disclosure Requirements



- When correcting errors, governments often fail to
 - Present all required information in notes
 - Make restatements for all prior periods in RSI – including MD&A – and SI when they make error corrections, or disclose that and why it is impracticable to do so

Review Comments Provided—Disclosure Requirements (cont.)

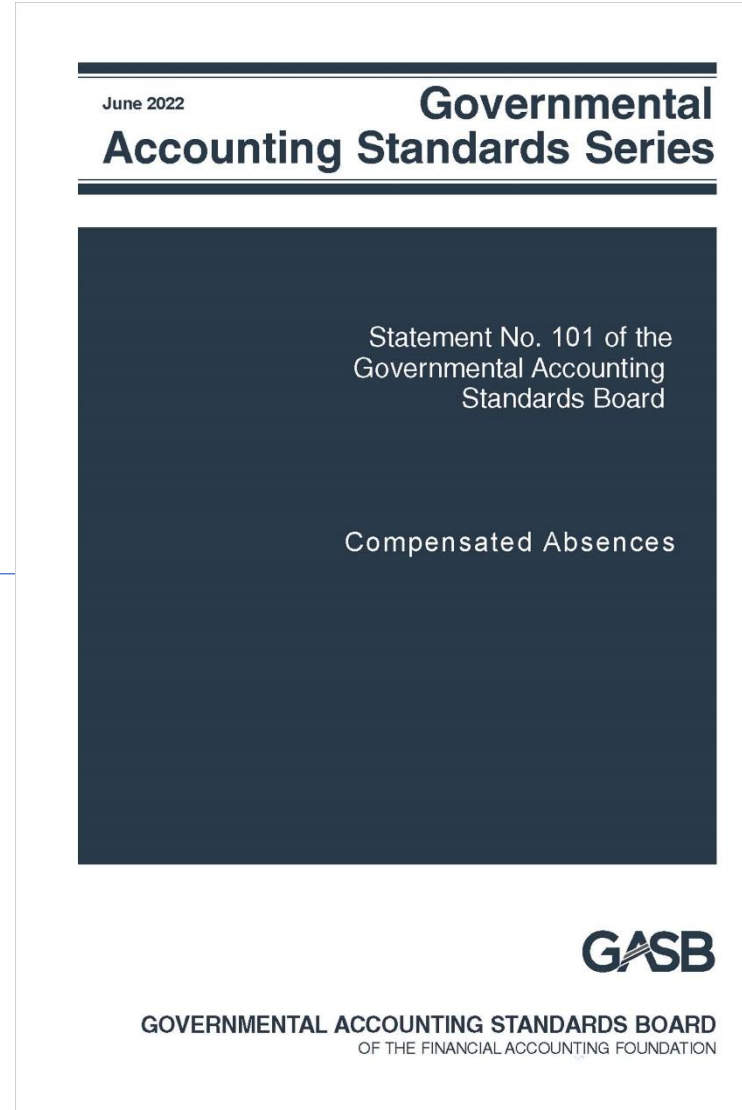


- When required,* governments often fail to include the tabular presentation of all adjustments and restatements to each affected reporting unit, beginning with the previously reported ending positions, detailing each individual accounting change or error correction, and ending with the restated beginning positions of each reporting unit.

*Unless each is shown individually on face of the position statement

Compensated Absences

Statement No. 101



Why do I have to recognize a liability for sick leave that doesn't get paid out when an employee leaves?

- Basis for Conclusions paragraphs B17 and B22 – sick leave should have the same recognition and measurement criteria as other types of leave
- Use of sick leave is conditional on a required event, employee becoming ill—one could assert that a government does not become obligated to pay for the leave until the required event occurs
- Board position is that a government becomes obligated to pay an employee for sick leave when the **employee earns the time off** and the sick leave is made available to the employee, if it is **more likely than not that the benefit will be used**
 - It is a present obligation of the government for a benefit for past service—paid leave in the future
 - It's about recognizing a liability and expense (cost of services) when the sick leave is earned—government becomes obligated at that point

Isn't that an overstatement of a liability when most of the sick leave does not get used?

- Illustration 1b – the liability may not be the entire amount of sick leave – only the portion that is more likely than not to be used

Illustration 1—Application of the Recognition Criteria for Leave That Has Not Been Used

Leave that has not been used is recognized as a liability if it (a) is attributable to services already rendered, (b) accumulates, and (c) is more likely than not to be used for time off or otherwise paid in cash or settled through noncash means.

- Sick leave that is earned each month and carries over without limits at the end of the fiscal year, but any unused leave is not paid upon termination of employment.*

Governments often offer leave to employees that can be used only when an employee is sick. Some governments allow employees to accumulate sick leave during their employment, but any unused amounts are forfeited upon termination of employment. Such leave is attributable to services already rendered because employees earn a certain number of hours or days for each month that they are employed. The leave accumulates because it carries over at the end of the fiscal year. The government estimates how much of the leave is more likely than not to be used as paid leave and recognizes that portion as a liability for compensated absences.

What flows assumption do I use?

- Basis for Conclusions paragraphs B43-B45—Key component in determining the estimate of the amount due within one year is the flows assumption for the pattern of usage of compensated absences.
- Is the amount the government expects to pay in the next reporting period attributed first to
 - The recognized liability at the date of the financial statements (FIFO)
 - The leave earned in the next reporting period (LIFO)
- Exposure Draft proposed FIFO requirement
- Statement 101 does not require either FIFO or LIFO
 - Professional judgment in setting policy or establishing practice

Do I have to calculate the liability for each employee?

- There is **NO requirement** to calculate a liability for each employee
- Matter of **professional judgment** based on the facts and circumstances, taking into account materiality

More likely than not for the leave to be paid at a rate different from the employee's pay rate at the time of payment

- Generally, calculating the liability using the pay rate at the financial statement date
- Paragraph 17 in Statement 101:

If some or all of the leave is more likely than not to be paid at a rate different from the employee's pay rate at the time the payment is made, a government should measure that portion of the liability **using that different rate as of the date of the financial statements**. For example, if leave is paid upon termination of employment at one-half of an employee's pay rate at the time of payment, the leave that is more likely than not to be paid upon termination of employment (instead of being used for time off) should be measured using one-half of the employee's pay rate as of the date of the financial statements.

More likely than not for the leave to be paid at a rate different from the employee's pay rate at the time of payment—2025 Implementation Guidance Update

4.15. Q—Is a future pay rate that is known (for example, because the next year's salary increases are approved or a collective bargaining agreement is in place) a rate different from the employee's pay rate at the time the payment is made as described in paragraph 17 of Statement 101?

A—No. Paragraph 17 of Statement 101 describes a circumstance in which leave is more likely than not to be paid at a rate different from the employee's pay rate in effect at the future date when the payment is made, such as a percentage of that pay rate or a set dollar amount. Governments should not use future pay rates, even if known, in the measurement of the liability for leave that is more likely than not to be paid at the future pay rate. Paragraph 20 of Statement 101 requires future pay rate changes to be recognized in the period of the change.

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GFOA's Award Program Compensated Absences

Review Comments Provided



- Compensated absences liabilities (similar to PEB, claims & judgements, pollution remediation obligations, etc.) are not capital-related and should not factor into the calculation of net investment in capital assets
- Long-term liability “roll-forward” note disclosure should:
 - Include compensated absences and show either (1) increases and decreases separately or (2) as a net increase or net decrease *with the netting specifically disclosed*
 - Distinguish between the amount due within one year and the amount due after one year