

# Accounting and Auditing Changes that Every Pool Administrator Should Know

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# Accounting and Auditing Changes that Every Pool Administrator Should Know

# Presenters



**+**  
**Carrie Rice, CPA**  
Partner  
Johnson Lambert



**+**  
**Anne Carlson**  
Director of Administration &  
Finance Controller  
MIIA Inc.

# Agenda

## ➤ Accounting Update

### ➤ GASB 87 - Leases

### ➤ GASB 96 - SBITA

## ➤ Auditing Update

### ➤ Changes in Auditing Standards SAS 143-145: Estimates, Specialists and Risk Assessment

## ➤ General Ledger Integration



# **GASB 87 - *Leases***

# What is a lease?

## Lease definition

**A contract that conveys control of the right to use another entity's nonfinancial asset (underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction**

*Examples - building, vehicles or equipment*



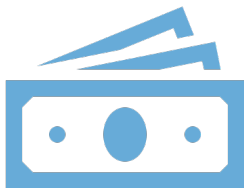
# Accounting Treatments



**Short term lease** - maximum lease term < 12 months or less



**Finance Purchase** - Lease contracts that transfer ownership at the end of a lease term and do not contain termination provisions



**All other Leases** - all other that do not fall into short term lease or finance purchase are accounted for using this single model approach

# What is the Impact on Financial Reporting?

	Line Item	Initial Measurement	Subsequent Measurement
Lessee	Right to use asset	Total of the lease liability plus lease prepayments, less impairment and initial costs to place the leased asset in service	Present value of future lease payments (includes fixed payments, variable payments based on index or rate, reasonably certain residual guarantees)
	Lease Liability	Present value of lease payments over the lease term, less any lease incentives	Reduced for principal payments made



# What is the Impact on Financial Reporting?

	Line Item	Initial Measurement	Subsequent Measurement
Lessor	Lease Receivable	Present value of lease payments over the lease term, less provisions for uncollectible amounts	Reduced for principal payments received
	Deferred Inflow of Resources	Total of the lease receivable plus lease prepayments	Amortized over the shorter of the lease term or the useful life of the right-to-use asset

# Exceptions



- + Short-term leases
- + Leases that transfer ownership
- + Intangibles
- + Biological assets (timber, plants, animals, etc.)
- + Inventory



- + Assets financed with outstanding conduit debt
- + Supply contracts, such as power purchase agreement  
(do not convey control of the underlying asset)



# Lease Term

## Includes the following

- + *the non cancellable period;*
- + *periods for which it can be reasonably certain that renewal options **will be** exercised;*
- + *periods for which it is reasonably certain that termination clauses **will not** be exercised*





## Example 1 - Short Term Lease

**Company A enters into a lease with the following terms:**

- Effective date: July 1, 2021
- Length: 12 months
- Asset type: Equipment with 10-year useful life
- Payments: \$1,000/month
- Transfer of ownership: No
- Purchased options: None

**The lease will be treated as a short-term lease and Company A will record the following monthly entry:**

**On July 1, 2021:**

DR Equipment rent expense:	\$1,000	
CR Cash		\$1,000



## Example 2

**Company B enters into a non-cancelable lease with the following terms:**

Effective date: July 1, 2020

Length: 5 years

Asset type: Building with 60-year useful life

Interest rate: 4%

Payments: \$3,000/month

Transfer of ownership: No

Purchase options: None

**Because the lease term is greater than twelve months and ownership is not transferred, the lessee recognizes a right-to-use asset and a lease liability as such:**

Present value of lease payments (rounded) = \$159,615

Total lease payments = \$180,000



## Example 2

Because the lease term is greater than twelve months and ownership is not transferred, the lessee recognizes a right-to-use asset and a lease liability as such:

Present value of lease payments (rounded) = \$159,615

Total lease payments = \$180,000

Straight line amortization  
over the shorter of the  
lease term or the useful  
life



		Components of the lease payment:		Balances for lessee to recognize:	
Date	Lease Payment	Interest rate 4%	Loan Amortization	Asset	Liability
7/1/2021				\$159,615	\$159,615
6/30/2022	\$36,000	\$7,181	\$28,819	\$127,692	\$130,796
6/30/2023	\$36,000	\$5,706	\$30,294	\$95,769	\$100,502
6/30/2024	\$36,000	\$4,157	\$31,843	\$63,846	\$68,659
6/30/2025	\$36,000	\$2,527	\$33,473	\$31,923	\$35,185
6/30/2026	\$36,000	\$815	\$35,185		
Totals	\$180,000	\$20,385	\$159,615		



The liability is reduced by the difference between the interest expense and lease payment

## Example 2

**Company B will record the following entries:**

**On July 1, 2021:**

DR Right-to-Use Asset (office space)  
\$159,615

CR Lease Liability  
\$159,615

*To record the original lease*

**On June 30, 2022:**

DR Lease Liability  
\$28,819

DR Interest expense  
\$7,181

CR Cash  
\$36,000

*To record first year payments*

DR Amortization  
\$28,819

CR Right-to-Use Asset - Accumulated Depreciation \$28,819

*To record first year amortization*





## Example 3 - Financed Purchase

**Company C enters into a non-cancelable lease with the following terms:**

Effective date: July 1, 2020

Length: 5 years

Asset type: HVAC system

Interest rate: 4%

Payments: \$3,000/month

Transfer of ownership: Yes

*The transaction is recorded as a financed purchase as the title to the equipment transfers to the lessee by the end of the contract, the transaction is not accounted for as a lease for financial reporting purposes.*





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**GASB 96 - SBITA**

# Keeping You Up-to-Date

## Government Accounting Standards Board's (GASB) Statement No. 96

- + *Subscription-Based Information Technology Agreements*
  - **SBITA**
- + *Affects the statement of net position and note disclosures*
- + *Effective for fiscal years beginning after June 15, 2022*



## Background

- + *May 2020: GASB issued Statement No. 96*



## New Guidance

- + *Defines SBITAs and establishes accounting for right-to-use subscription assets and corresponding liability*
- + *Provides capitalization criteria for outlays beyond subscription payments*
- + *Based on and shares many key concepts from GASB Statement No. 87*



# Definition, Classification, & Measurement

## What is an SBITA?

- + *A contract which conveys control for the right to use another party's IT software*

## Government should assess the following:

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

## SBITA contracts exclude those that solely provide IT support services

- + *But still include those that contain both a right-to-use IT asset component and an IT support services component*



# GASB 96 Exceptions



**Contracts that fall under GASB 87, *Leases***

**Subscribers that provide the right-to-use their IT software and associated tangible capital assets to other entities through SBITAs**

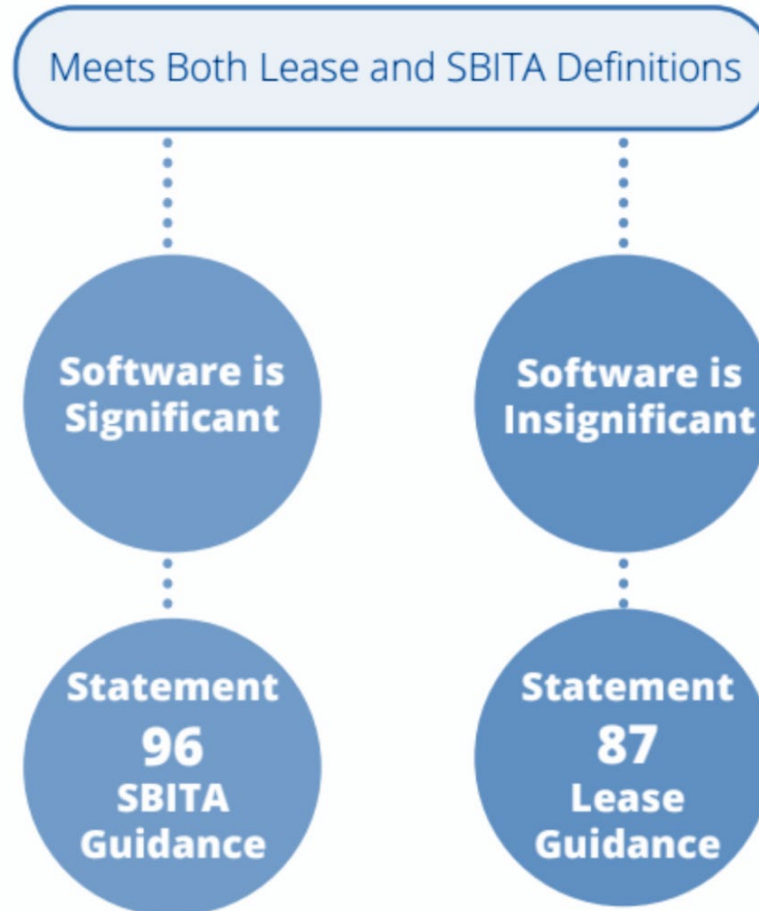


**Contracts that meet the definition of the public-private and public-public partnerships**



**Licensing arrangements that provide a perpetual license to Governments to use a vendor's computer software**

# Lease or SBITA?



# SBITA Examples

## Software-as-a-Service (SaaS)

- + *Using the vendor's cloud-based software*
  - + *Cloud-based software applications*
  - + *Cloud-based software systems*
  - + *Cloud-based conferencing systems*



## Platform-as-a-Service (PaaS)

- + *Using the vendor's platform for software development*
  - + *User controls code, but not underlying resources*



## Infrastructure-as-a-Service (IaaS)

- + *Using the vendor's cloud-based computer, networking, RAM, and storage*

## Warehouse-as-a-Service (WaaS)

- + *Using the vendor's cloud-based, on-demand access to warehouse space*

# Accounting Treatment

## Short-Term SBITAs



- + Includes a maximum possible term of 12 months or less
- + Accounting for these is overall consistent to present day

## Other SBITAs

- + Accounted for using the economic resource measurement focus

## Measurement Focus



- + Upon commencement, a subscription liability and intangible right-to-use asset should be recognized as follows:



Line Item	Initial Measurement	Subsequent Measurement
<b>Subscription Asset</b>	Initial subscription liability, plus any prepayments made prior to subscription term, plus capitalizable implementation costs, less any incentives received at or before commencement	Amortized over the shorter of the subscription term or the useful life of the underlying IT assets
<b>Subscription Liability</b>	Present value of subscription payments (fixed and certain variable) and contract incentives receivable from the SBITA vendor	Reduced for principal payments made

# Subscription Term

**The noncancelable period of right-to-use underlying IT assets**

**Periods of reasonable certainty that the option to extend will be exercised**

**Periods of reasonable certainty that termination options will not be exercised**

**Factors to consider include:**

- + *Significant economic incentive or disincentive*
- + *Potential changes in technological developments*
- + *Potential significant changes in demand for SBITA vendor's IT assets*
- + *History of exercising options to extend or terminate*
- + *Extent to which IT assets are essential to the subscribers' services*

**Reassess subscription terms if one of more of the following occur:**

- + *Either party elects to or not to exercise an option that was not previously determined*
- + *An event specified in the SBITA contract occurs that requires an extension or termination of the SBITA*





# Implementation Costs

Activities associated with an SBITA—besides making subscription payments—are grouped into the following categories:

Stage	Activities	Accounting
<b>Preliminary Project Stage</b>	<ul style="list-style-type: none"> <li>• Formulate and evaluate alternatives</li> <li>• Determine existence of needed technology</li> <li>• Selection among alternatives</li> </ul>	Expensed as incurred
<b>Initial Implementation Stage</b>	<ul style="list-style-type: none"> <li>• Design, configure, code, install, and test</li> <li>• Convert data needed to make underlying assets operational (completed when the asset is placed in service)</li> </ul>	Capitalized, except for short-term SBITA
<b>Operation &amp; Additional Implementation Stage</b>	Troubleshooting and maintenance <ul style="list-style-type: none"> <li>• Convert data (other than that needed to make underlying assets operational)</li> <li>• Maintain software (and hardware)</li> </ul>	Expensed as incurred
<b>All stages</b>	Training	Expense as incurred



# Implementation Costs Continued

**If SBITA has more than 1 module, and multiple modules are implemented at different times, the first module implementation and subscription asset is placed into service upon the completion of the first module**

- + *The implementation stage is considered complete regardless of all module implementation status*

**Data conversion should be included in the implementation stage**

- + *Include if necessary to place the subscription asset into service*
- + *Other data conversions should be considered an operations and additional implementation stage*

**Capitalized implementation costs are included as a component of the asset and amortized over the shorter of the subscription term or asset's useful life**



# Discount Rate

**If a discount rate is not explicitly stated, the rate shall default to the Government's incremental borrowing rate.**

**Should be reassessed if there is a change in the subscription term and it has a significant effect on the subscription liability.**

**Subscription liability is not required to be measured, nor is the discount rate required to be reassessed solely for a change in the borrowing rate.**

***Note: There is not an option to use risk free rate under GASB.***

# Contracts with Multiple Components

**Governments may enter contracts containing both subscription and non-subscription elements, each component should be accounted for as a separate contract**

**If a SBITA involved multiple IT assets with different subscription terms, each underlying IT asset should be accounted as a separate subscription component**

**To allocate contract price to diff. components, subscriber should:**

- + *Identify prices for components included in the contract*
- + *If no price is stated in the contract, then standalone prices that would be paid for the right-to-use the component should be applied*
- + *If there are bundling discounts, it is applied to all elements*

**Subscriber should account for multiple components when one of the following occurs:**

- + *If it is not practical to determine a best price allocation estimate*
- + *If there are multiple modules in which the subscription term commences at the same time, then all modules will be based on the primary subscription term*



# Transition



**GASB 96 is effective for fiscal years beginning after June 15, 2022**

+ *Early application permitted*



**Guidance should be applied retroactively by restating financial statements for all prior periods presented**



**If impractical, the effect of applying GASB 96 should be reported as a restatement of beginning net position for the easiest fiscal year stated (Requires specific disclosure of why impractical)**



**Assets and liabilities should be recognized and measured using the facts and circumstances that existed at the beginning of the earliest fiscal year restated**



**First implementation needs to be reviewed by Carrie, Josh or Mag - similar to lease implementation.**

# Estimates, Specialists, and Pricing Services

**SAS 143 & 144**

***Year Ends after 12.15.23***

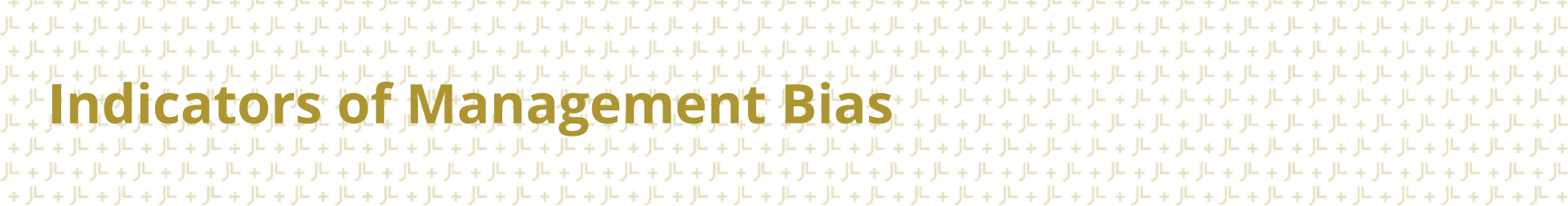
# Changes in Auditing Standards SAS 143-145: Estimates, Specialists and Risk Assessment

## SAS 143: Accounting Estimates

- Clarifies **auditor's** responsibilities for evaluating accounting estimates, including fair value accounting estimates

## What to Expect?

- More detailed **inquiries** of management regarding the system of internal controls to identify and assess risks that could result in material misstatement related to estimates
- Indications of Management bias in recording of estimates
- Includes understanding the underlying data, methodology and assumptions used in the estimation process



# Indicators of Management Bias

## Examples of Management Bias

- Management's point estimates consistently trends toward one end of auditor's range of reasonable outcomes - that provide a more favorable financial reporting outcome for management
- Changes in accounting estimates, or methods - that led to certain favorable outcomes
- Selection or development of significant assumptions or data that yield a point estimate favorable for management objectives



# GASB 10 year revenue and claims

## Premium data

## Total claim cost at 1st year

## Paid claim data

## Re-estimated claim cost over 10 years

		2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
	Earned	26,661,504	23,855,363	22,498,572	26,378,033	22,841,627	23,436,676	24,604,027	27,536,807	28,188,855	28,214,808
	Ceded	7,910,904	9,023,603	8,067,599	8,189,369	6,733,767	8,136,471	7,721,985	8,834,820	8,452,958	6,650,420
(1)	Net contribution and inv revenues	18,750,600	14,831,761	14,430,973	18,188,663	16,107,860	15,300,205	16,882,042	18,701,987	19,735,897	21,564,388
(2)	Unallocated expenses	2,414,740	2,495,018	2,805,497	2,577,124	2,120,466	1,959,660	2,203,168	2,528,259	2,790,761	3,205,359
	Incurred	13,354,433	12,747,698	14,495,018	15,212,092	14,940,243	14,781,922	16,656,196	18,811,828	18,319,937	18,330,197
	Ceded	-	-	-	-	-	-	-	-	-	-
(3)	Estimated incurred claims and exp	13,354,433	12,747,698	14,495,018	15,212,092	14,940,243	14,781,922	16,656,196	18,811,828	18,319,937	18,330,197
(4)	Net paid (cumulative) as of:										
	End of policy year	4,641,052	3,311,514	6,206,105	4,548,616	5,603,692	5,779,827	7,447,598	7,476,833	7,317,203	6,972,897
	One year later	5,507,755	5,257,635	7,068,950	7,099,309	8,397,607	8,288,969	10,450,947	11,152,578	10,823,974	
	Two years later	6,665,073	6,649,794	8,274,976	8,226,294	9,933,267	9,706,961	11,904,093	12,940,047		
	Three years later	7,742,175	7,769,884	9,483,952	8,909,584	11,351,070	10,864,449	12,554,003			
	Four years later	8,366,117	8,499,564	10,100,728	9,569,227	11,909,976	12,103,699				
	Five years later	8,741,975	9,073,261	10,828,147	10,506,907	12,535,696					
	Six years later	9,027,274	9,590,488	11,528,252	11,303,247						
	Seven years later	9,427,836	10,135,627	11,681,963							
	Eight years later	9,448,709	10,170,998								
	Nine years later	9,771,282									
(5)	Reestimated net incurred claims and expenses:										
	End of policy year	13,354,433	12,747,698	14,495,018	15,212,092	14,940,243	14,781,922	16,656,196	18,811,828	18,319,937	18,330,197
	One year later	12,014,038	12,886,923	14,194,894	14,455,611	15,211,274	14,093,104	16,563,057	18,179,791	19,072,077	
	Two years later	11,877,001	12,295,880	14,906,201	14,002,494	14,373,493	14,320,796	16,601,720	17,712,073		
	Three years later	12,054,875	12,620,620	14,658,914	13,895,191	13,941,123	14,826,653	16,268,227			
	Four years later	11,660,134	12,245,728	14,594,926	13,889,034	13,909,648	14,669,303				
	Five years later	11,462,502	12,306,132	14,259,484	13,887,171	14,262,720					
	Six years later	11,311,171	12,010,951	14,086,391	14,546,094						
	Seven years later	11,177,830	12,431,633	13,713,143							
	Eight years later	11,292,760	12,315,731								
	Nine years later	11,261,386									
(6)	Increase (decrease) in estimated incurred claims and expense from end of policy year										
		(2,093,047)	(431,967)	(781,875)	(665,998)	(677,523)	(112,619)	(387,969)	(1,099,755)	752,140	-



# Changes in Auditing Standards SAS 143-145: Estimates, Specialists and Risk Assessment

## SAS 144: Use of Specialists and Pricing Information

- Enhances guidance for (1) the auditor's evaluation of management's use of an external specialist and (2) the use of an auditor's specialist
- Evaluate competencies, objectivity, obtain an understanding of their work and it's appropriateness
- Also applies to pricing information from external source (to assist in pricing investment portfolios with holdings at level 2 or level 3)
- Impact is primarily to auditor procedures rather than deliverables

### •What to Expect?

- More detailed inquiries of management and its specialists
- Management should ensure they have:
  - ◆ Procedures to evaluate competency of specialists and the quality of the source data provided to them
  - ◆ An understanding of their pricing sources and the involvement of pricing services and specialists

# Changes in Auditing Standards SAS 143-145: Estimates, Specialists and Risk Assessment

## SAS 145: Risk Assessment

- Supersedes AU-C 315
- Focus is on enhanced risk assessments to support audit quality and defines auditor responsibilities for understanding the system of internal controls
- New terminology is introduced and familiar terms are re-defined

## What to Expect?

- An increased emphasis on the risk assessment phase of the audit
- Performance of audit procedures that are responsive to the risks identified

# General Ledger Considerations and Integration

# What's New in General Ledger Functionality

## General Ledger Functionality

- Accounts Payable and AI – OCR scanning and fillable forms
- Bank interfaces directly into GL for easy bank reconciliation functionality
- Interfaces with claim and policy systems
- Accounts receivable functionality for holding members' credits

## Reporting and Dashboards

- **General Ledgers have integrated Dashboards**
  - Accounts receivable on-time reporting with member details
  - Accounts Payable trends
  - Year over year financial comparisons
- **Real time budget to actual analysis**



# Considering a new General Ledger?

## Determine your must have business requirements

- Cloud-based or local server
- Bank interfaces
- Workflow approval processes
- Budget to actual reporting in real time
- Statutory vs GAAP vs GASB reporting requirements

## Requests For Proposal - RFPs

- **Consider an outside consultant to help prepare the RFP**
- **Interview key stakeholders and understand your business requirements**
  - Ask about A/R system add-ons
  - Ask about A/P system automation
- **Consult with your current banking institutions if planning to interface**





# Integration Considerations:

## Common Pitfalls to Integrating a new GL

- Allow enough time for parallel testing along side retiring GL
- Bring over all your beginning balance detail – don't lump sum beg balances
- Spend time training staff and with the User Acceptance Testing - UAT

## Consider bringing in your auditors early to discuss the project

- Allow time to walk auditors through the remapping to prior audited statements

# + Questions





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