



GASB Statement 87 Leases

New England States Government Finance Officers Association

Presented By:

René Davis, CPA, MBA
Powers & Sullivan, LLC
100 Quannapowitt Parkway
Wakefield, MA 01880
781-914-1700
rdavis@powersandsullivan.com

GASB 87 - LEASES

Intended to improve lease accounting and financial reporting by governments.

Existing standards were in effect for decades without review

FASB and IASB conducted a joint project and have updated their lease standards - the GASB is following the IASB model

This is an opportunity to increase comparability and usefulness of information and reduce complexity for preparers

This statement requires the recognition of certain lease assets and liabilities for leases that were previously classified as operating leases


It establishes a *single model* for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset

Scope and Approach


- ❖ Statement 87 applies to any contract that meets the definition of a lease:
 - ❖ *“A lease is 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.”*
- ❖ Leases are financings of the right to use an underlying asset - A new single approach is applied to accounting for leases with some exceptions such as short-term leases.
- ❖ Capital/operating distinction is eliminated.
- ❖ The new distinction is short-term/financed purchase/or lease accounting

Scope and Approach

Statement 87 requires that leases be recognized and measured using the facts and circumstances as of the beginning of the period of implementation



Retrospective application is required for prior years by restating financial statements for all periods presented, unless it would be impractical to do so



If it is impractical to restate, the reason and explanation must be disclosed (i.e. lease terms not available)

Implementation

Effective for fiscal years beginning after June 15, 2021 (i.e. FY22).

Originally December 15, 2019 - postponed 18 months in GASB 95.

Does Lease Accounting Apply?

Lease Accounting Does Not Apply to Short-Term Leases or Financed Purchases

- It is a short-term Lease if at the beginning of the lease, the maximum possible term under the contract is 12 months or less. See accounting for Short-term leases.
- It is a financed purchase if ownership transfers. Account for as a sale/purchase.

Does Lease Accounting Apply?

If it is not a short-term lease and it is not a financed purchase, it is a lease under GASB 87 if it meets the 3 criteria in the definition:

1. *Conveys Control* - right to determine nature and manner of use
 - a. The government has obtained (or relinquished) the present service capacity of the asset and
 - b. The government has acquired (or relinquished) the right to determine how the asset is used
2. *Period of Time/Lease Term* - not indefinite/noncancelable period is greater than one year
3. *Exchange/Exchange-Like Transaction* - each party must receive or give up essentially equal value

Scope Exclusions

- ▶ Intangible Assets (mineral rights, patents, software, copyrights), except for the sublease of an intangible right to use asset
- ▶ Biological assets (including timber, living plants, and living animals)
- ▶ Inventory
- ▶ Service concession arrangements (statement 60)
- ▶ Arrangements associated with conduit debt obligations (statement 91)
- ▶ Supply contracts (such as power purchase agreements that do not convey control of the right to use the underlying generating facility).

Lease Term

For financial reporting purposes, when does the lease start and end?

- Start with the noncancelable portion
- Plus periods covered by options to
 - Extend lease - if reasonably certain of being exercised
 - Terminate lease - if reasonably certain of not being exercised
- Excludes cancelable periods
 - Periods for which lessee and lessor both have option to extend or terminate (such as rolling month-to-month leases)
- Fiscal funding and cancellation clauses are ignored unless reasonably certain of being exercised

Lease Term

The lease term should be adjusted if:

- An option to extend or terminate the lease is exercised that was previously deemed reasonably certain not to be exercised.
- An option to extend or terminate the lease is not exercised that was previously deemed reasonably certain to be exercised.
- The lease agreement specifies that if a certain event occurs then the lease will be extended or terminated and that event does occur.

Exchange Transactions

- ▶ Nonexchange Transactions - if you give or receive value without directly receiving or giving equal value in return (leasing land for \$100)
- ▶ Exchange Transactions - each party receives and gives essentially equal value

Considerations

Governments may need to consider changing policies and procedures for tracking and reporting leases, both as lessee and lessor - document decisions on reporting leases

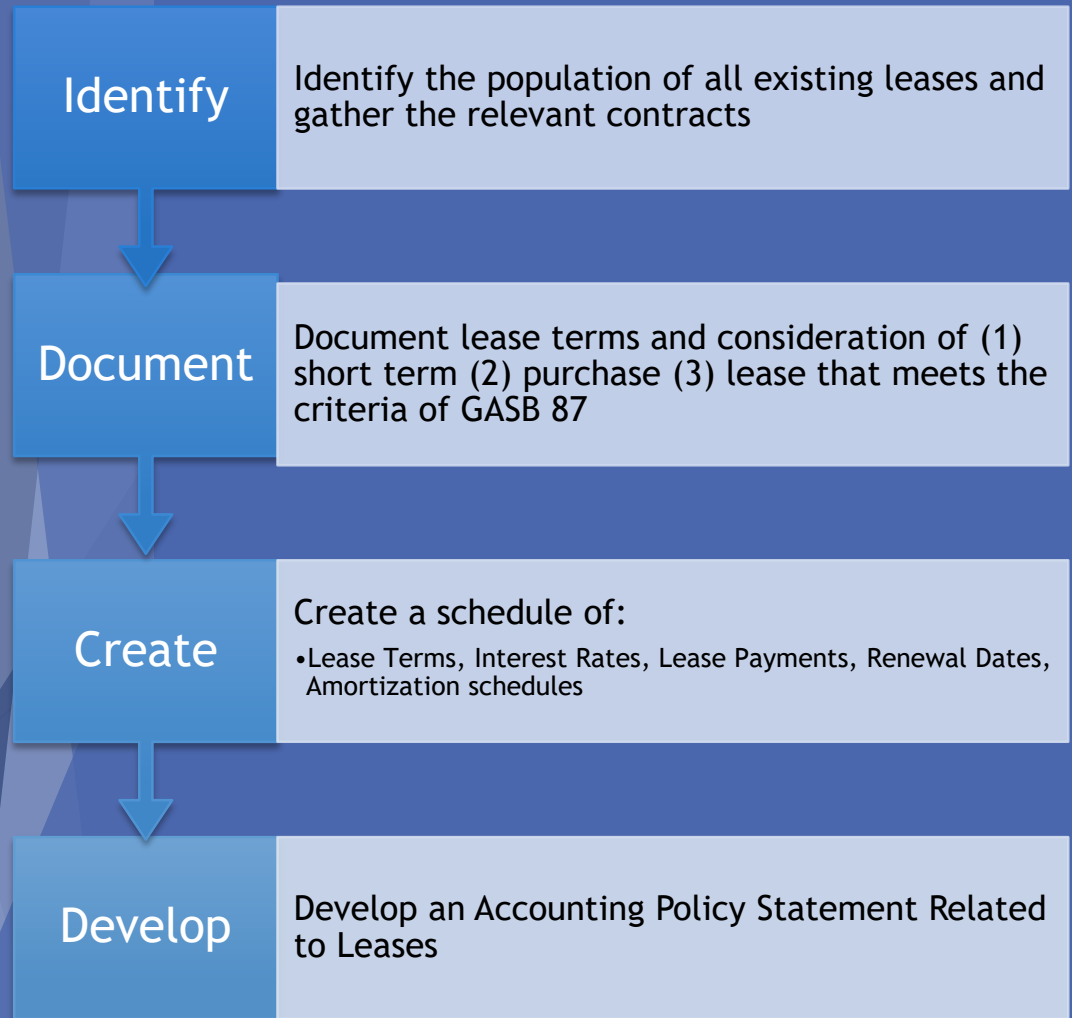
May need better communication between departments that enter into leases and central accounting staff to ensure proper reporting

Need procedures that identify when lease agreements have been initiated and when existing leases are modified (such as changes in lease term or estimated payment amounts)

Should review capital asset policies, such as the capitalization thresholds, especially in-light-of the need to report intangible right-to-use assets

Immaterial assets or leases would never be reported

First Step, Gather Information





Lease Policy Statement

Accounting Policy Statement will outline the process for making judgment on the measurement of the right-of-use assets and related obligations.

Document the likelihood of exercising an optional lease extension or the likelihood of using a fiscal funding or cancellation clause to terminate a lease early.

This should be documented with a listing of leases, lease terms, and the determination of the accounting treatment.

Document if it is practical to retrospectively adjust financial statements for prior periods or if disclosure is necessary to explain reasoning.

Initial
Reporting
Lessees
recognize a
lease liability
and an
intangible
right to use a
leased asset

Record Liability - Present value of future lease payments (incl. fixed payments, variable payments based on index or rate, reasonably certain residual guarantees, etc.)

Record the Right To Use the Underlying Leased Asset - Intangible lease asset - value of lease liability plus prepayments and initial direct costs that are ancillary to place asset in use

On the Modified Accrual (fund) basis - this is recorded as an expenditure, similar to a capital purchase and an other financing source - lease financing.

Similar to the issuance of long-term debt, you are borrowing funds to create an asset. Both the asset and the liability need to be recorded for full-accrual accounting.

Subsequent Reporting Lessee

The intangible leased assets are amortized in a systematic manner over shorter of useful life of asset or lease term

The lease liability is reduced by the lease payments (less amount for interest expense)

Example

Date	Lease Payment	Interest Rate 5%	Loan Amortization	Balances	
				Asset	Liability
7/1 year 1				\$27,232	\$27,232
6/30 year 1	\$ 10,000	\$ 1,362	\$ 8,638	18,155	18,594
6/30 year 2	10,000	\$ 930	9,070	9,027	9,524
6/30 year 3	10,000	\$ 476	9,524	0	0
Totals	<u>\$ 30,000</u>	<u>\$ 2,768</u>	<u>\$ 27,232</u>		

present value =ROUND(PV(0.05,3,-10000,0,0),0) = 27,232

Asset is amortized straight line

Liability is amortized by the difference between the interest expense and the lease payment



The debits & credits

Long-term Lease Liabilities - Year 1 - Full Accrual Accounting

Record the Asset and the Lease:

Right of Use Asset	\$27,232
Lease Liability	\$27,232

Record the first year's amortization on the right-of-use asset equal to one-third of the asset value:

Amortization Expense	\$9,077
Accumulated Amortization	\$9,077

Record 1st payment on Lease:

Lease Liability	\$8,638
Interest Expense	\$1,362
Cash	\$10,000



The debits & credits

Long-term Lease Liabilities - Year 1 - Modified Accrual Accounting

Record the Lease Agreement:

Expenditure: Lease Right of Use Asset	\$27,232	
Other Financing Source: Lease Financing		\$27,232

Record 1st payment on Lease:

Expenditure: Liability Financing Principal	\$8,638	
Expenditure: Interest	\$1,362	
Cash		\$10,000

Disclosures Lessee

Lessee disclosures are similar to capital leases:

- Description of leasing arrangements
- A summary of lease assets'
- Historical cost
- Accumulated amortization by type of asset
- A delineation of principal and interest payments required over each of the next five years and beyond in five-year increments.

Initial
Reporting
Lessors
recognize a
lease
receivable
and a
deferred
inflow of
resources

Assets - Lease receivable (generally includes same items as lessee's liability)

Assets - Also continue to report the leased asset

Deferred Inflows of Resources - Equal to lease receivable plus any cash received up front that relates to a future period

Subsequent Reporting Lessor

Depreciate leased asset (unless indefinite life or required to be returned in its original or enhanced condition)

Reduce the receivable by lease payments received (less amount needed to cover accrued interest)

Deferred inflow - Recognize revenue over the lease term in a systematic and rational manner

Disclosures Lessor

Include in notes:

- Description of leasing arrangements
- Total amount of inflows of resources recognized from leases

Short Term Leases

- ▶ Definition - at the beginning of the lease, maximum possible term under the contract is 12 months or less
- ▶ Lease accounting -
 - ▶ Recognize expense/expenditures based on the terms of the contract
 - ▶ Do not recognize assets or liabilities associated with the right to use the underlying asset
- ▶ Lessor accounting -
 - ▶ Recognize lease payments as revenue based on the payment provisions of the contract
 - ▶ Do not recognize receivables or deferred inflows



The debits & credits

Short Term Leases - No Asset/No Liability

Modified Accrual Accounting:

Rent Expenditure	\$2,000	
Cash		\$2,000

Full Accrual Accounting:

Rent Expense	\$2,000	
Cash		\$2,000



Implementation Guide 2019-3

AUGUST 2019

**Governmental
Accounting Standards Series**

**Implementation Guide No. 2019-3,
*Leases***

GASB

GOVERNMENTAL ACCOUNTING STANDARDS BOARD
OF THE FINANCIAL ACCOUNTING FOUNDATION



Implementation Guide 2019-3

- ▶ 77 Questions & Answers
- ▶ Scope and Applicability Issues
- ▶ Determining the term of the lease
- ▶ Eligibility for exception for short-term leases
- ▶ Recognition, measurement, and disclosure for lessees and lessors
- ▶ Lease incentives
- ▶ Contracts with multiple components and contract combinations
- ▶ Terminations and modifications
- ▶ Sale-leasebacks, lease-leasebacks, and intra-equity leases



Multiple Components

Contracts with multiple components

Generally, account for lease and non-lease components as separate contracts and multiple underlying assets as separate lease components in certain circumstances (paragraphs 64 and 65)

Allocate contract price to different components (paragraph 66)

Implementation guide 2019-3

one component meets scope exclusions and one does not?

separate and account for them individually q459

separate utilities and janitorial costs of building lease? = yes if practicable to do so q4.60

Other Topics Covered

If you have specific circumstances,

- ▶ Contract Combinations (implementation guide 4.63, 4.64)
- ▶ Lease Modifications and Terminations (implementation guide 4.65-4.70)
- ▶ Lease Incentives (implementation guide 4.56, 4.57)
- ▶ Subleases - treat as separate transactions from original lease
- ▶ Sales - Leasebacks (implementation guide 4.71, 4.72)
- ▶ Lease - Leasebacks (implementation guide 4.73, 4.74)



Thank You

Powers & Sullivan, LLC
100 Quannapowitt Parkway
Wakefield, MA 01880
781-914-1700
Fax 781-914-1701
powersandsullivan.com