UNIVERSITY

GASB 87: Leases

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Continuing education credits available

Please answer at least **three** polling questions.

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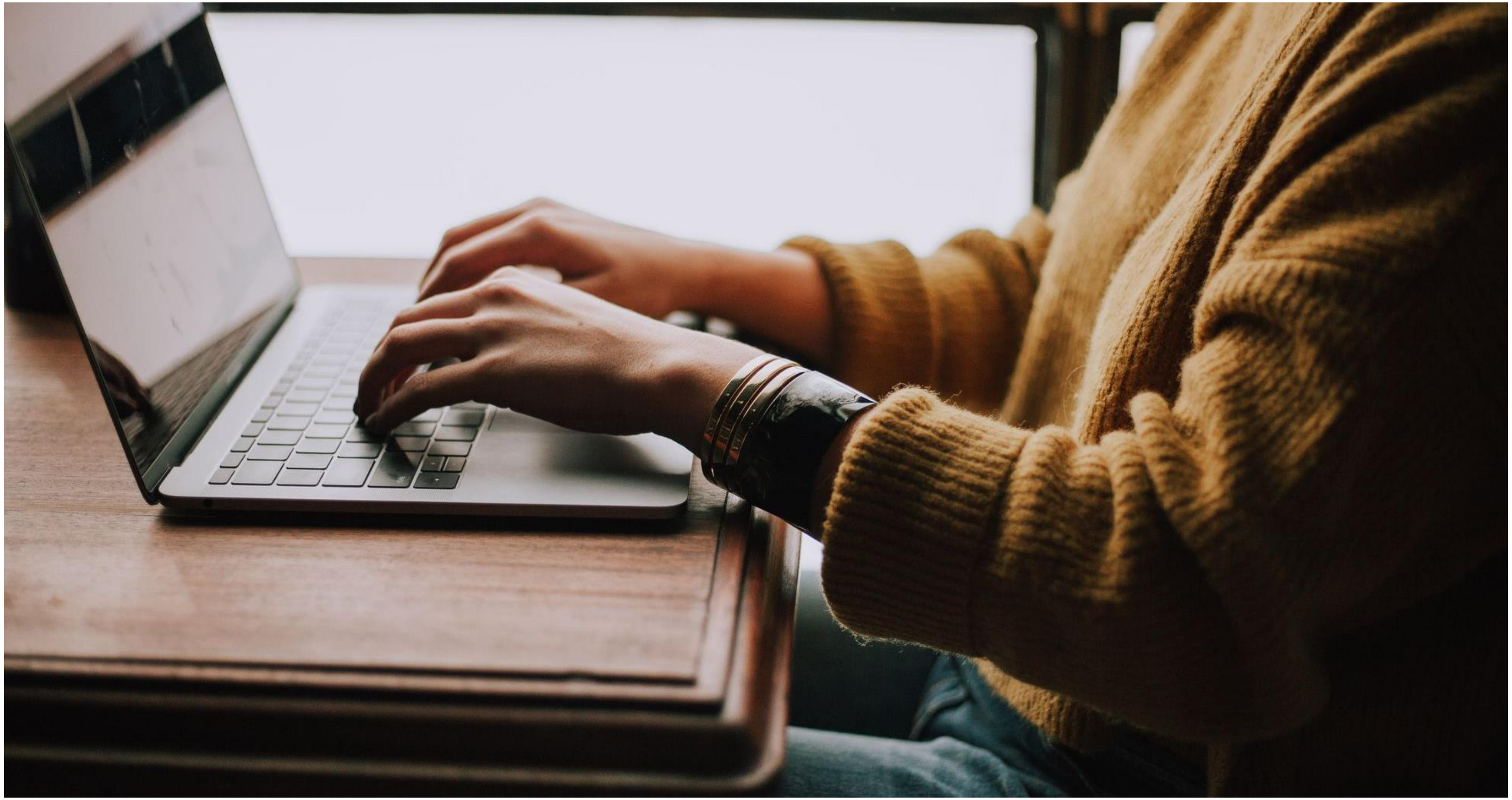
Recording & slides will be available.



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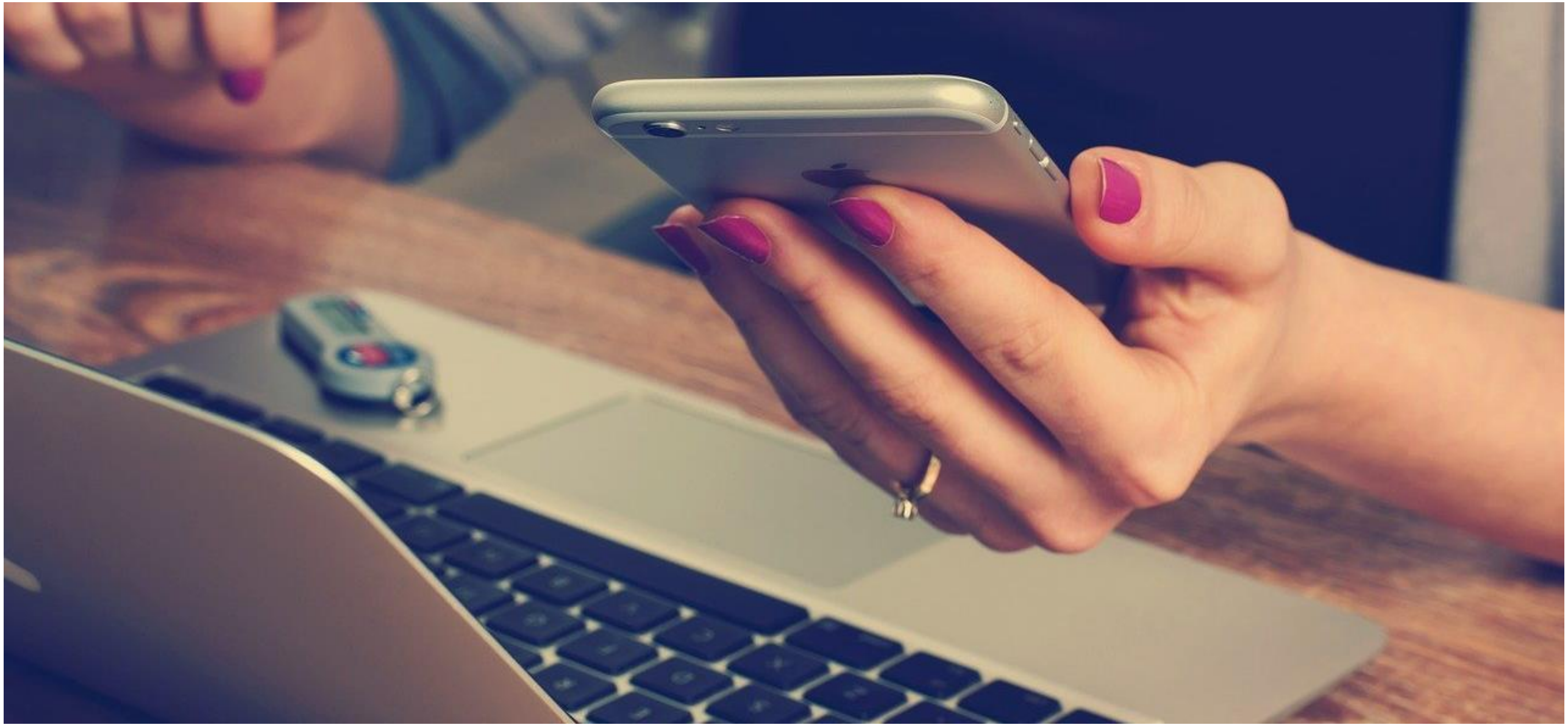
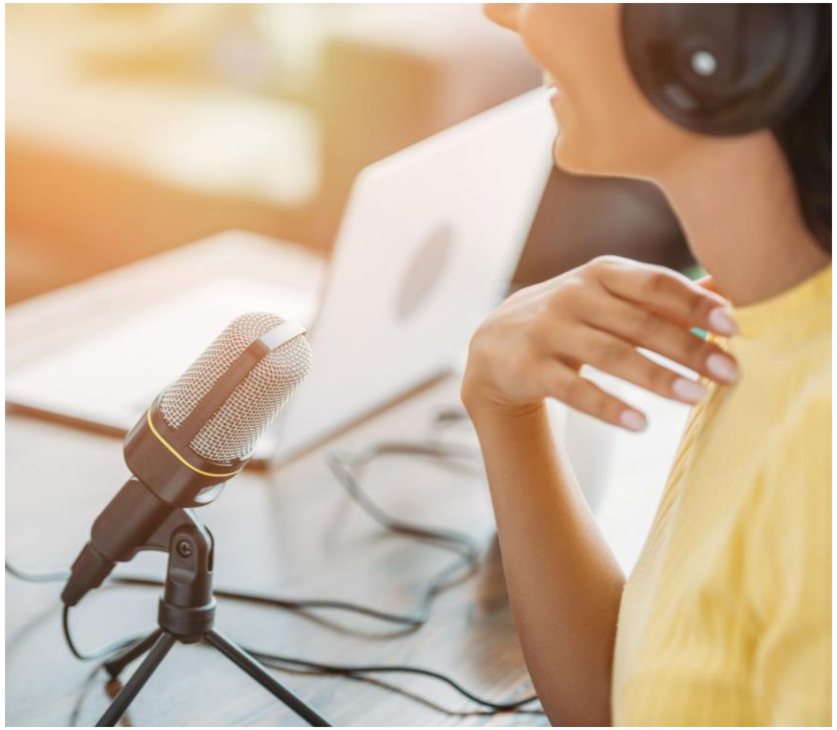


Questions? Ask away!

Don't forget our survey



Tara Laughlin, CPA, CGFM

Tara has over 12 years of experience specializing in providing auditing and consulting services to a variety of governmental and not-for-profit entities.

Tara is a member of the American Institute of Certified Public Accountants and Government Finance Officers Association.

Learning Objectives

the key takeaways

Learning **objectives**

1. Learn to identify what is a lease under GASB 87
2. Learn to identify key lease contract terms needed
3. Learn how to perform GASB 87 entries and disclosures
4. Discuss best practices in implementing GASB 87

Polling question #1

Why change accounting for leases?

GASB 87 establishes a single model for lease accounting, based on the foundational principle that leases are financings of a right to use an underlying asset.

GASB 87 - What is a lease?

Lease definition

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

Definition breakdown - **contract**

- Use of term contract
  - It was debated using the term agreement v. contract
  - By using contract, it requires leases, whether written or verbal, that are legally enforceable to be within the scope of this statement
- Not all leases will have “lease contract,” “lease arrangement, or “lease agreement“ in the contract. Look for embedded leases!

Definition breakdown - **right to use**

- Must have **both**:
  1. Right to obtain present service capacity from use of the asset
  2. Right to determine the nature and manner of use of the underlying asset

Does a **right to use** exist?

A government enters into a multiyear agreement for the right to use a facility. The government has an exclusive use of the facility for three days a week. Other parties use the facility on the other days.

To meet the definition of a lease, is the government required to have uninterrupted control of the right to use asset?

No - this meets the definition of right to use.

GASB Implementation Guide 2019-3 Question 4.2

Does a **right to use** exist?

A government enters into an agreement that allows a rancher to use the government's land for grazing. The agreement states that the rancher is required to allow access to the land for compatible public recreation activities. In addition, the agreement states that the government can construct roads and buildings, or otherwise alter the land, without permission from the rancher.

Does the grazing rights agreement meet the definition of a lease?

No - does not convey rights to determine nature and manner of use.

GASB Implementation Guide 2019-3 Question 4.4

Does a **right to use** exist?

Are cell phone tower or antenna placement agreements leases?

Likely yes - if it meets the definition of a lease, including the control criterion. Control criterion is generally met if a cell phone tower or antenna placement agreement conveys control of the right to use the land on which the tower is placed or the connection point to which the antenna is fixed.

GASB Implementation Guide 2019-3 Question 4.8

Definition breakdown - **nonfinancial asset**

- A nonfinancial asset is one that is not a financial asset, as defined by GASB 72. Most commonly think of buildings, land, vehicles, and equipment. But others do exist that would qualify as leases, like cell phone tower connection points.

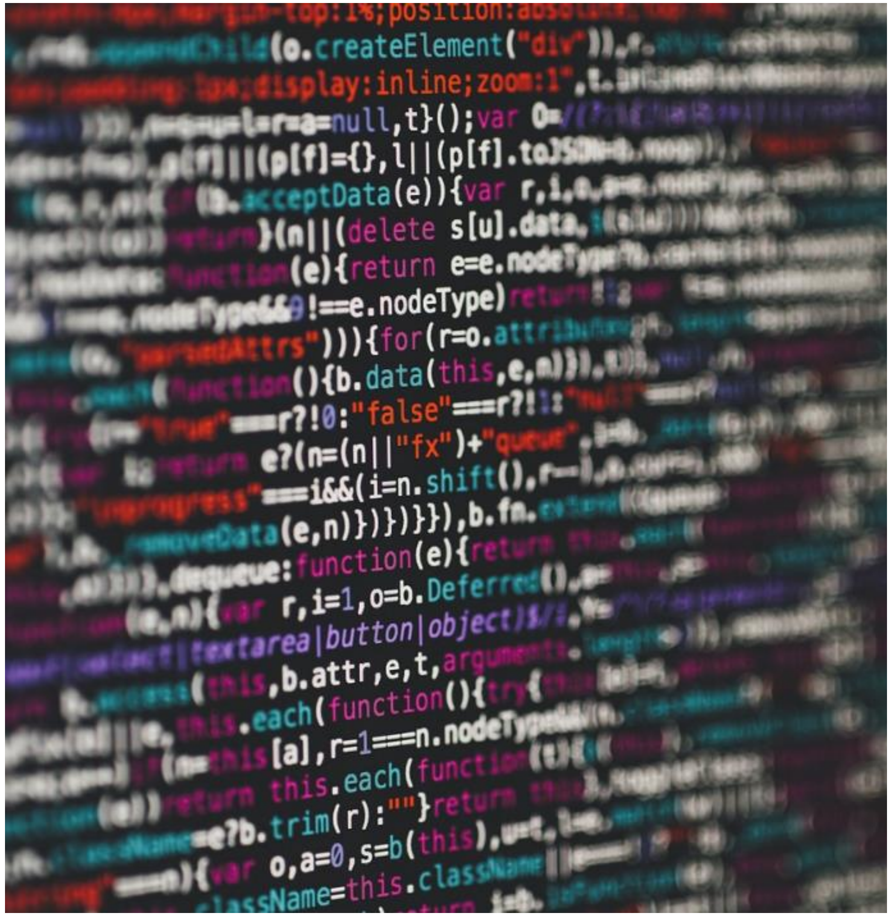
Definition breakdown - **exchange/exchange like**

- Must have economic substance. Leases for nominal values are not included under this standard.

- Likely the GASB revenue and expense project will clarify accounting for nonexchange transactions like free office space for $1 a year leases.

Scope exclusions

- Excluded leases include:
  - Leases of intangible assets
    (i.e. licensing contracts for computer software)
  - Leases for biological assets
  - Leases of inventory
  - Service concession arrangement contracts
  - Leases where the underlying asset is financed with outstanding conduit debt
  - Supply contracts (power purchase agreements)



Polling question #2

Identifying the *lease term*

GASB 87 - Paragraphs 12-15

Lease term equation

Noncancelable period
+ Lessee's option to extend, if reasonably certain to exercise
+ Lessee's option to terminate, if reasonably certain ***not*** to exercise
+ Lessor's option to extend, if reasonably certain to exercise
+ Lessor's option to terminate, if reasonably certain ***not*** to exercise

= Total lease term

Lease term equation - breakdown

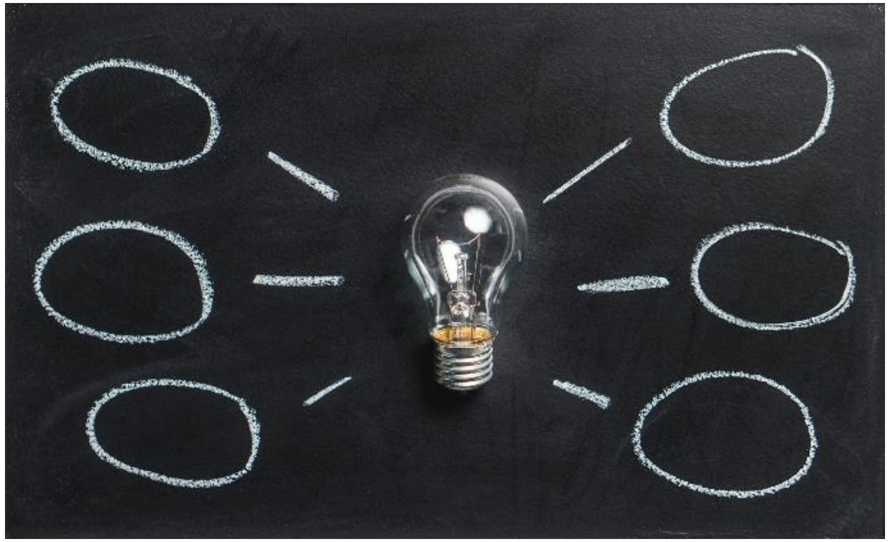
Noncancelable period

Periods, where both the lessee and lessor have an option to terminate without permission from the other party (or if both parties must agree to extend), are cancelable periods and not included in the lease term.

- Rolling month-to-month leases

Lease term equation - breakdown

- What should you consider in determining if option periods are reasonably certain or not?
  - Significant economic incentives
  - Significant economic disincentives
  - History of exercising options
  - How essential the underlying asset is to operations



Lease term equation - breakdown

I have a fiscal funding or cancellation clause. How should I take this into account?

Fiscal funding clauses do not impact the lease term unless it is reasonably certain the clause will be exercised.

Lease term reassessment

The lease term should be reassessed if one of the following occurs:

- Lessee or lessor exercises an option even though it was previously determined that it was reasonably certain they would not exercise.
- Lessee or lessor elects to not exercise an option even though it was previously determined that it was reasonably certain they would.
- Event specified in the lease contract that requires an extension or termination of the lease take place.

NOTE: all these items are events that took place. These are not changes in your probability assessment. You would not reassess if you went from reasonably certain to reasonably uncertain.

What is the **lease term**?

A lease contract has a noncancelable period of 5 years and specifies at the end of the 5 years, both the lessee and lessor have the right to cancel the lease or continue the lease on the same terms month-to-month. What is the lease term?

5 years - the month-to-month is a cancelable period.

GASB Implementation Guide 2019-3 Question 4.13

What is the **lease term**?

How does a bargain renewal option, such as a 20-year lease at a market rate with a lessee option to renew for an additional 5 years at a 30% discount, affect the lessee's initial assessment of the lease term?

Presenter answer: Likely would include the 5 years as there is an economic incentive to renew by the lessee.

GASB Answer: A government should assess all factors relevant to the likelihood that the option will be exercised.

GASB Implementation Guide 2019-3 Question 4.14

What is the **lease term**?

A lease contract allows either party to unilaterally terminate the lease at any time, but also provides for cancellation penalties. The penalties are so great that it is reasonably certain that neither party will terminate the lease. Should the cancelable periods be excluded from the lease term?

Yes

GASB Implementation Guide 2019-3 Question 4.15

Exceptions: Short-term/transfer of ownership

GASB 87 - Paragraphs 16-19

Short-term leases

- Leases that are "short-term" continue to be accounted for more like an operating lease.

- Leases are short-term if:

  At the commencement of the lease term, the maximum possible term under the lease contract is 12 months or less including any options to extend regardless of the probability of exercising the option.

Polling question #3

Short-term leases on implementation

- A city has a 10-year lease that began 7/1/2012 and ends 6/20/2022. GASB 87 is effective for their FYE 6/30/2022 financial statements. How should this lease be treated?
  - If single year financials are presented, this would be a short-term lease. The final payment that occurred from 7/1/2021-6/30/2022 would be a period expenditure/expense.
  - If comparative financials are presented, this would **not** be a short-term lease and you would need to restate 6/30/2021 financial statements using the facts and circumstances of the lease as of 7/1/2020 (first day of the fiscal year restated).

Transfer of ownership

- Leases that transfer ownership are treated as a financed purchase by the lessee and a sale of assets by the lessor.

  Transfer of ownership does not include a purchase option, or a bargain purchase option until the option is exercised.

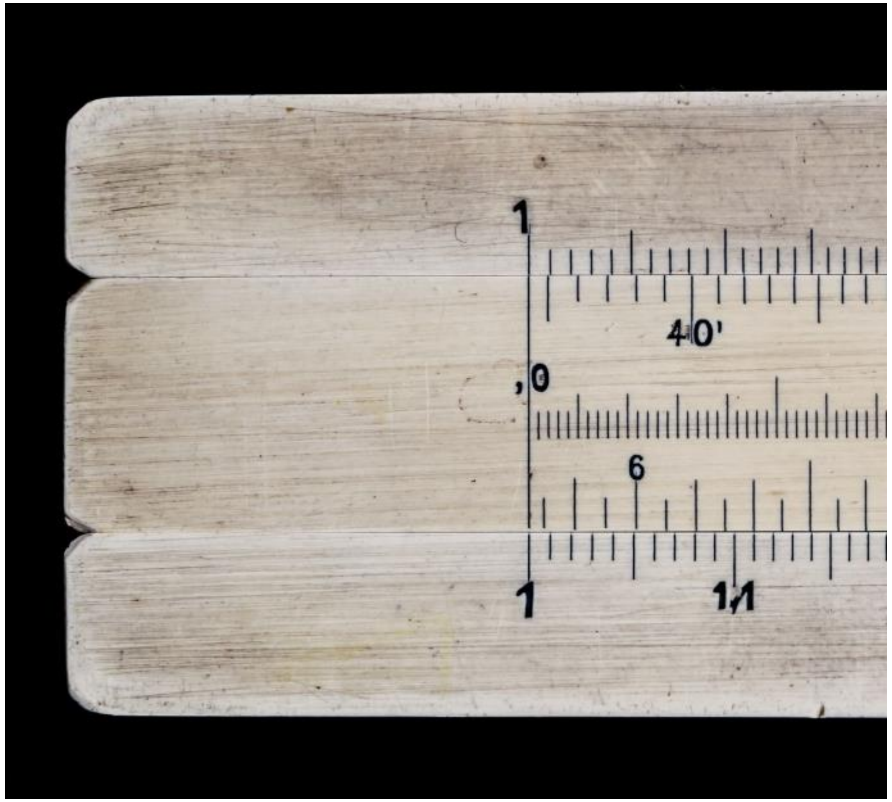
Lessee accounting

GASB 87 - Paragraphs 20-39

Lessee accounting - **recognition and measurement**

- Recognize a liability for future lease payments and an intangible capital asset for the right to use the underlying asset

- Government Fund Reporting:
  - Report payables when due
  - Don't report capital assets



Lessee accounting – lease liability measurement

- Present value of payments expected to be made during the lease term.

- Payments include:

1. Fixed payments (less any lease incentive receivable from the lessor)
2. Variable payments that depend on an index or rate
3. Variable payments that are fixed in substance
4. Reasonably certain payments related to residual value guarantees
5. Exercise price of purchase option if reasonably certain that option will be exercised
6. Payments for penalties for terminating lease if lease term reflects the lessee exercising an option to terminate or exercise of funding clause
7. Any other payments that are reasonably certain to be paid

Lessee accounting – **lease liability example**

Lease payments for a 5-year lease are indexed to the CPI. The lease payments for the first year are $5,000 per month, which is the market rate based on current CPI, and payments for subsequent years will increase/decrease based on the change in CPI during the preceding year. The CPI at the commencement of the lease is 251. How should the initial lease liability be calculated?

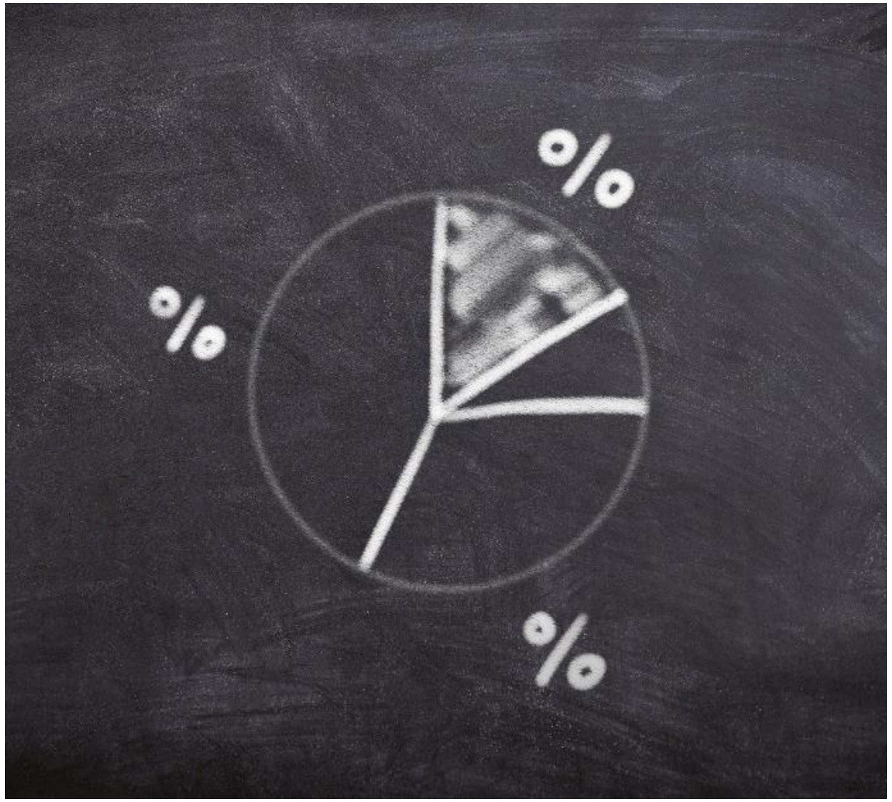
Present value of $5,000 per month for 60 months. Any additional payments made in the future due to CPI increases would be period expenses/expenditures and any decreases in payments due to CPI decreases would reduce that period's expenses/expenditures.

GASB Implementation Guide 2019-3 Question 4.26

Lessee accounting – lease liability measurement

- What discount rate should be used?
  (In order of preference)

  1. Interest rate lessor charges lessee (may be implicit in the contract)
  2. Lessee's incremental borrowing rate



Lessee accounting – **lease liability subsequent periods**

- Amortize the discount rate into expense and reduce the lease liability

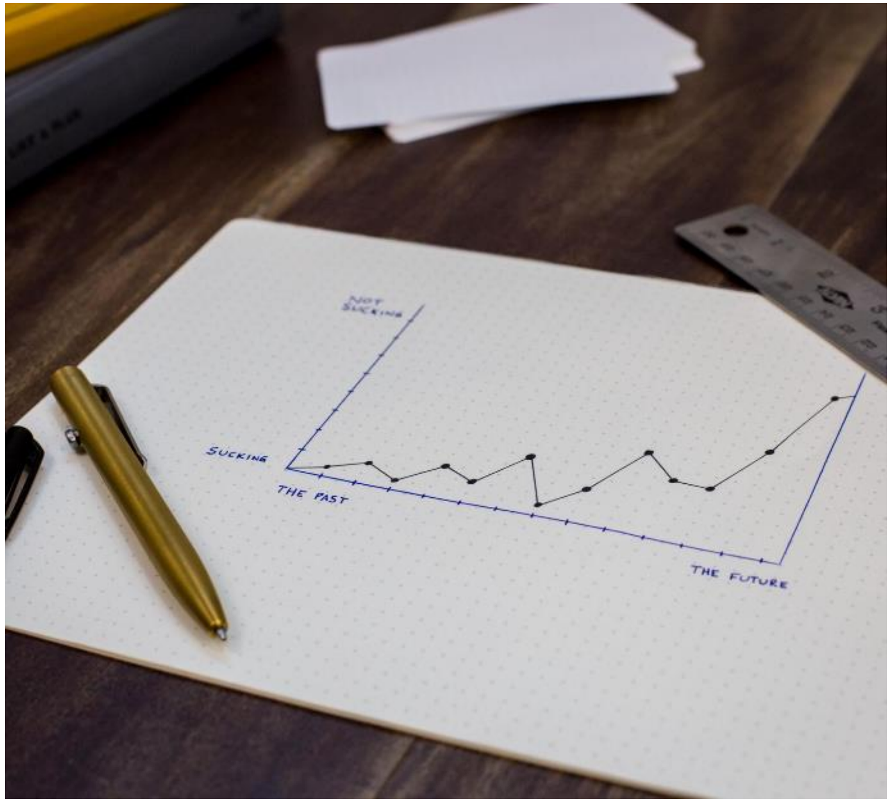
Lessee accounting – lease liability remeasurement

- Remeasurement of the lease liability if one of the following occurs and is significant to the lease liability:
  - Change in lease term
  - Residual value guarantee that was considered reasonably certain is now not (or vice versa)
  - Purchased option being exercised has changed
  - Change in estimated amounts to be included in the measurement of the lease liability
  - Change in interest rate charged to the lessee, if used as the initial discount rate
  - Contingency on variable payments is resolved such that those payments now meet the criteria for measuring the lease liability

Lessee accounting – lease liability remeasurement

- If the liability is remeasured the index or rate used in variable payments should also be adjusted if expected to significantly affect the liability.

- Note: these are for changes on assumptions and not on the contract itself changing. If the contract is amended, that would be a lease modification treated differently.



Lessee accounting – **lease liability remeasurement**

- Discount rates should be remeasured if one or both happen:
  1. Lease term changes
  2. Purchase option assumption changes

- Don't remeasure the discount rate solely for change in lessee's incremental borrowing rate!

Lessee accounting - **lease asset measurement**

Lease Liability
+ Payments made to lessor at or before commencement of the lease
- Lessor incentives paid at or before commencement of the lease
+ Certain direct costs (costs to place asset into use)

= Lease asset

Lessee accounting – lease asset subsequent periods

- Amortized in a systematic and rational manner over the shorter of the lease term or useful life of the underlying asset.

- If you have a purchase option that is reasonably certain to be exercised should amortize over the useful life of the asset (or not amortize if land).

Lessee accounting – **lease asset remeasurement**

- Leased asset should generally be adjusted by the same amount as a lease liability.
- For the adjustment reduces the asset below zero, report the difference as a gain.
- Leased assets can be impaired!

Lessee accounting – **note disclosures**

- General description of leasing arrangements

  Include basis, terms and conditions on which variable payments are not included in the lease liability and existence, terms and conditions of residual value guarantees provided by the lessee not included in the lease liability

- Total amount of lease assets and related amortization disclosed separately from other capital assets.
- Amount of lease assets by major classes of underlying assets disclosed separately from other assets.
- Amount of outflows recognized in the reporting period for variable payments not included in the liability.
- Amount of outflows recognized for other payments like residual value guarantees or termination penalties not previously included in the liability.

Lessee accounting – note disclosures (cont.)

- Principal and interest requirements to maturity, presented separately, for lease liability for each subsequent 5 years and then in 5-year increments.
- Commitments under lease for commencement of lease.
- Components of any loss associated with impairment.
- Other disclosures related to sublease/sale-leaseback and lease-leaseback transactions.
  - Will be included in those respective sections
- Do not have to disclose collateral, if the collateral is the underlying asset.

Polling question #4

Lessee accounting - **example**

Facts

- Lease starts at 4/1/20 or 60 months; $1,000 monthly payment due 1st of each month.
- Lessee incurs $2,500 transportation costs and other expenditures to make equipment ready for use.
- Government has an option to purchase the equipment for $2,000 at the end of the lease which it is reasonably certain it will exercise.
- Government lessee estimates that the useful life of the capital equipment will be 7 years (84 months).
- Discount rate (provided by lessor) is 3%.

The following slides are excerpts from the GFOA Lease tool example, available to GFOA members at GFOA.org

Lessee accounting - **example**
- *liability calculation*

		PV of Lease Payments	PV calc term		PV of purchase option
A	monthly payments	$ 1,000	*Pmt*		$ -
B	number of periods	60	*Nper*		5
C	Annual interest rate	3.00%			3.00%
D	Monthly interest rate (C / 12 months)	0.250%	*Rate*		
E	Future Value	$ -	*Fv*		$ 2,000
F	Type: "1" if payments are made at beginning of period, "0" if payments are made at end of period	1	*Type*		1
G	First payment date	4/1/2020			
H	Increments between payments (if monthly "1", if bi-monthly "2")	1			
	Present value of lease payments	**$55,791**			
	Present value of purchase option	**$1,725**			
	Total PV of lease liability	**$57,517**			

Lessee accounting - **example** - *liability amortization*

	Amortization of lease payments				
Payment					
Number	Month, Year	Payment	Interest	Principal	Balance
					$ 57,517
1	April, 2020	$ 1,000	$ -	$ 1,000	56,517
2	May, 2020	1,000	141	859	55,658
3	June, 2020	1,000	139	861	54,797
4	July, 2020	1,000	137	863	53,934
5	August, 2020	1,000	135	865	53,069
6	September, 2020	1,000	133	867	52,202
7	October, 2020	1,000	131	869	51,333
8	November, 2020	1,000	128	872	50,461
9	December, 2020	1,000	126	874	49,587

Lessee accounting - **example**
- *asset calculation*

Lease Asset		
Total lease liability	$	57,517
Government lessee incurs transportation costs and other expenditures to make equipment ready for use	$	2,500
Total lease asset at inception of lease	$	60,017

Lessee accounting - **example** - *asset amortization*

	Month Number	Amortization	Balance
			$ 60,017
1	April, 2020	$ 714	59,303
2	May, 2020	714	58,589
3	June, 2020	714	57,875
4	July, 2020	714	57,161
5	August, 2020	714	56,447
6	September, 2020	714	55,733
7	October, 2020	714	55,019
8	November, 2020	714	54,305
9	December, 2020	714	53,591

Lessee Accounting - Example - JE 4/1/20 - General Fund

To record inception of lease		
Expenditures - Capital outlay	$57,517	
Other financing source		$57,517
To record expenses to get asset ready		
Expenditures - Capital Outlay	$2,500	
Cash		$2,500

Lessee Accounting - Example - JE 4/1/20 (continued) - Government Wide

To recognize lease liability		
Other financing source	$57,517	
Lease liability		$57,517
To recognize lease asset		
Lease asset (intangible right to use)	$60,017	
Expenditures - Capital Outlay		$60,017

Lessee Accounting - Example - Total 1st Year Entry - General Fund

To record first year lease payments		
Expenditures - Principal	➡	$7,930
Expenditures - Interest	➡	$1,070
Cash	➡	$9,000

Lessee Accounting - Example - Total 1st Year Entry - Government Wide

To record lease payments		
Lease liability	➡	$7,930
Expenditures - Principal	➡	$7,930
To record asset amortization		
Amortization expense	➡	$6,426
Accumulated amortization - lease asset	➡	$6,426

Lessee accounting - **example** - *disclosures*

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets not being depreciated				
Land	12,038,276		(4,230)	12,034,046
Construction in progress	31,222,996	12,890,833	(3,025,559)	41,088,270
Total capital assets not being depreciated	43,261,272	12,890,833	(3,029,789)	53,122,316
Other capital assets				
Buildings	240,126,741	30,072,509	(1,949,759)	268,249,491
Equipment and fixtures	26,200,540	2,239,879	(31,254)	28,409,165
Leased buildings	636,731	60,017	-	696,748
Leased equipment and fixtures	5,005,414	-	-	5,005,414
Total other capital assets at historical cost	271,969,426	32,372,405	(1,981,013)	302,360,818
Less accumulated depreciation for				
Buildings and improvements	(67,806,215)	(7,317,012)	1,579,277	(73,543,950)
Equipment and fixtures	(18,380,429)	(2,365,552)	31,254	(20,714,727)
Less accumulated depreciation for				
Leased assets	(1,938,346)	(1,105,860)	-	(3,044,206)
Total accumulated depreciation and amortization	(88,124,990)	(10,788,424)	1,610,531	(97,302,883)
Other capital assets, net	183,844,436	21,583,981	(370,482)	205,057,935
Capital assets, net	227,105,708	34,474,814	(3,400,271)	258,180,251

Lessee accounting - **example** - *disclosures*

Future debt service payments for note disclosure			
Year	Principal	Interest	Total
2021	$ 10,657	$ 1,343	$ 12,000
2022	10,982	1,018	12,000
2023	11,316	684	12,000
2024	11,660	340	12,000
2025	4,972	28	5,000
Totals	$ 49,587	$ 3,413	$ 53,000

Lessor accounting

GASB 87 - Paragraphs 40-60

Lessor accounting – **recognition and measurement**

- Recognize a lease receivable and deferred inflow of resources.
- Do not derecognize the underlying asset and do not recognize a residual asset. If agreement requires lessee to return the asset in original or enhanced condition, do not depreciate the asset during the lease term.
- Governmental Fund Reporting:
  - Recognize lease receivable and deferred inflow of resources
  - Recognize deferred inflow of resources as revenue when “available”

Lessor accounting – **lease receivable measurement**

- Present value of payments expected to be received during the lease term.

- Payments include:

1. Fixed payments (less any lease incentive payable to the lessee)
2. Variable payments that depend on an index or rate
3. Variable payments that are fixed in substance
4. Residual value guarantees that are fixed
5. Less provision for uncollectible accounts

Polling question #5

Lessor accounting - lease receivable **example**

A government leases retail space to a vendor for three years. The payment in the first year is $100,000 (minimum annual guarantee). The payment in the second year depends on the sales in the first year. If first year sales exceed $1,000,000, the minimum annual guarantee in year 2 is $110,000, if less it stays at $100,000 for year 2 and drops to $90,000 in year 3. What amounts should be included in the lease receivable at the commencement of the lease?

$290,000 is the sum of the lowest possible minimum annual guarantees.

GASB Implementation Guide 2019-3 Question 4.47

Lessor accounting – **lease receivable measurement**

- What discount rate should be used? (in order of preference)

1. Rate stated in contract (unless no rate charged)
2. Interest rate lessor charges lessee (may be stated or implicit in the contract)
3. Prevailing or published rates for similar instruments and credit ratings
4. Lessee's incremental borrowing rate
5. Lessor's estimated incremental borrowing rate

Lessor accounting – **lease receivable subsequent periods**

- Amortize the discount rate into revenue and reduce the lease receivable.

Lessor accounting – **lease receivable remeasurement**

- Remeasurement of the lease receivable if one of the following occurs and is significant to the lease receivable:
  - Change in lease term
  - Change in interest rate charged to the lessee, if used as the initial discount rate
  - Contingency on variable payments is resolved such that those payments now meet the criteria for measuring the lease receivable

Lessor accounting – **lease receivable remeasurement**

If the receivable is remeasured the index or rate used in variable payments should also be adjusted if expected to significantly affect the receivable.

Note: these are for changes on assumptions and not on the contract itself changing. If the contract is amended that would be a lease modification and treated differently.

Lessor accounting – **lease receivable remeasurement**

Discount rate remeasurement

Discount rates should be remeasured if one or both happen:

1. Lease term changes
2. Change in interest rate charged

Lessor accounting - **deferred inflow of resources measurement**

Lease receivable

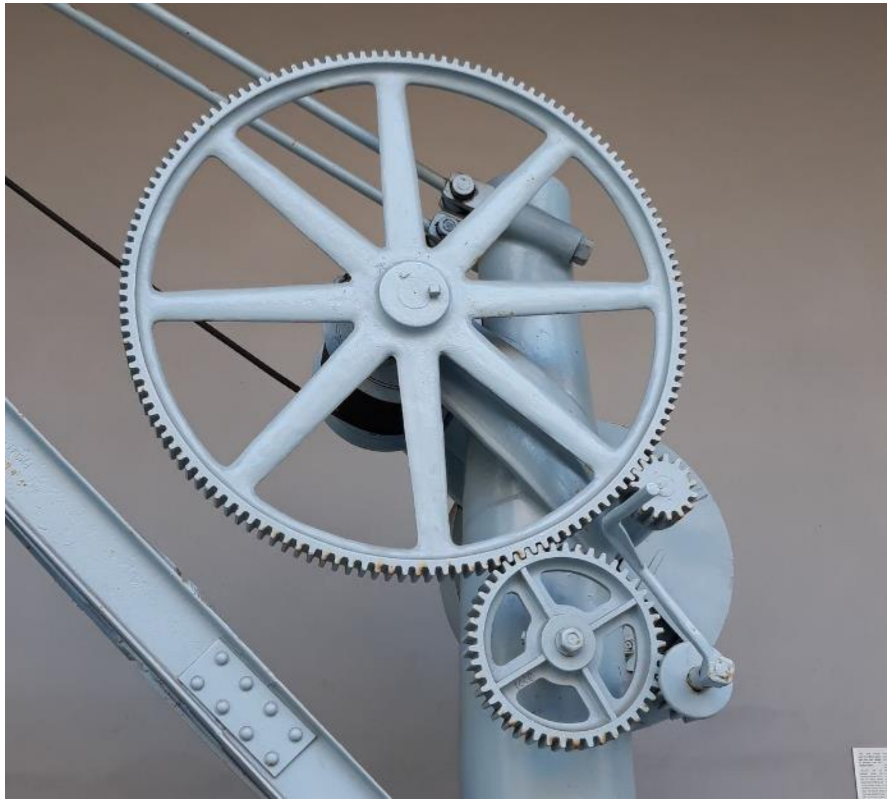
+ payments received from lessee at or before commencement of the lease related to future periods
- lessor incentives paid at or before commencement of the lease

= Deferred inflow of resources

Direct costs should be expensed in the period incurred

Lessor accounting – **deferred inflow subsequent periods**

- Amortized in a systemic and rational manner over the term of the lease.



Lessor accounting – **deferred inflow remeasurement**

- Deferred inflow should generally be adjusted by the same amount as a lease receivable.
- For the adjustment reduces the deferred inflow below zero, report the difference as a loss.

Lessor accounting - **note disclosures**

1. General description of leasing arrangements.
   Including basis, terms and conditions on which variable payments are not included in the receivable.
2. Total amount of inflows of resources (lease revenue, interest revenue and any other lease related inflows) recognized in the reporting period from leases, if amounts can't be determined on the face of the financials.
3. Amount of inflows recognized in the reporting period for variable and other payments not previously included in the measurement of the lease receivable, including inflows related to residual value guarantees and termination penalties.
4. Existence, terms and conditions of options by the lessee to terminate the lease or abate payments if the lessor government has issued debt for which the principal and interest payments are secured by lease payments.

Lessor accounting - **note disclosures (cont.)**

5 Disclosure requirements for if assets are investments, regulated leases, sublease transactions, sale-leaseback transactions, lease-leaseback transactions – all discussed separately.

6 If the lessor's principal operations consist of leasing assets to other entities, should disclose a schedule of future payments of the lease receivable showing principal and interest separately for subsequent five years and five-year increments.

7 Do not have to report the carrying amounts of asset on lease or held for leasing and related accumulation depreciation anymore.

Lessor accounting - **exceptions**

- Lessors have two additional exceptions to GASB 87 reporting, but these exceptions still have disclosure requirements
- Leases of tangible assets that are investments are defined by GASB 72
  - No lease receivable reported for leased investment assets because investments are reported at fair value
  - Must disclose the existence, terms and conditions of options by the lessee to terminate the lease or abate payments if the lessor government has issued debt for which principal and interest are secured by the lease payments
- Regulated leases - covered in next slide

Lessor accounting - **exceptions (cont.)**

- Certain regulated leases:
- Lessors should recognize inflows of resources based on payment provisions of the lease contract and provide certain disclosures for leases for which external laws, regulations or legal rulings establish all the following requirements:
  - Lease rates cannot exceed a reasonable amount, reasonableness is subject to determination by an external regulator
  - Lease rates should be similar for lessees that are similarly situated
  - Lessor cannot deny potential lessees the right to enter a lease if facilities are available, provided that the lessee's use of facilities complies with generally applicable use restrictions

Lessor accounting - exceptions (cont.)

- Regulated Lease Disclosure Requirements:

1. General description of agreements
2. Extent capital assets are subject to preferential or exclusive use by counterparties under agreements, by major class of assets and major counterparty
3. Total amount of inflows (lease revenue, interest revenue, and any other lease related inflows) recognized in the reporting period from these agreements, if you can't determine it based on amounts displayed on the financial statements
4. Schedule of expected future minimum payments for each subsequent 5 years and then 5-year increments
5. Inflows recognized in reporting period for variable payments not included in future minimum payments
6. Existence, terms and conditions of options by lessee to terminate the lease or abate lease payments if lessor issues debt that is secured by lease payments

Polling question #6

Lessor accounting - example

Facts

- Lease starts 7/1/20 for 10 years with a 3rd party and leases two floors of one of its buildings to the 3rd party.
- Monthly payments due at the beginning of the month for $3,000. Lessor receives last month's rent upon inception of the lease.
- Total due from lessee at inception is $357,000 ($360,000 less $3,000 last month's payment received at inception).
- Interest rate assumed to be charged is 2.5%, its estimated return on investments.
- Government continues to report the building and depreciates it on a straight-line basis ($10,000,000 for 75 years or $133,333 annual depreciation).

Following slides are excerpts from GFOA Lease tool example.
Available to GFOA members at GFOA.org

Lessee accounting - **example**
- *receivable calculation*

			PV calc term
A	monthly payments	$ 3,000	*Pmt*
B	number of periods	119	*Nper*
C	Annual interest rate	2.5%	
D	Monthly interest rate (C / 12 months)	0.2083333%	*Rate*
E	Future Value	0	*Fv*
F	Type: "1" if payments are made at beginning of period, "0" if payments are made at end of period.	1	*Type*
G	First payment date	7/1/2020	
H	Increments between payments (if monthly "1", if bi-monthly "2")	1	
	Present value of lease payments	**$ 316,556**	

Lessee accounting - **example** - *receivable amortization*

	Amortization of lease receipts				
Payment Number	Month, Year	Payment	Interest	Principal	Balance
					$ 316,556
1	July, 2020	$ 3,000	$ -	$ 3,000	313,556
2	August, 2020	3,000	653	2,347	311,209
3	September, 2020	3,000	648	2,352	308,857
4	October, 2020	3,000	643	2,357	306,500
5	November, 2020	3,000	639	2,361	304,139
6	December, 2020	3,000	634	2,366	301,773

fiscal year 1 payments	
Interest	Principal
3,217	**14,783**

Lessee accounting - **example** - *deferred inflow calculation*

Deferred inflow of resources		
Total lease receivable at inception	$	316,556
Government lessor receives last month's rent upon inception of lease	$	3,000
Total deferred inflow of resources at inception of lease	$	319,556

Lessee accounting - **example**
- *deferred inflow amortization*

	Month, Year	Amortization	Balance
			$ 319,556
1	July, 2020	$ 2,663	316,893
2	August, 2020	2,663	314,230
3	September, 2020	2,663	311,567
4	October, 2020	2,663	308,904
5	November, 2020	2,663	306,241
6	December, 2020	2,663	303,578

Lessor Accounting - Example - JE 7/1/20 - General Fund

To record receipt of last month's payment	
Cash	$3,000
Deferred inflow of resources	$3,000
To record inception of release	
Lease receivable	$316,556
Deferred inflow of resources	$316,556

Lessor Accounting - Example (Cont.) - JE 7/1/20 - Government Wide

NONE	➡	0

Lessor Accounting - Example - Total 1st year entry - General Fund

To record first year lease payments		
Cash	➡	$18,000
Lease receivable	➡	$14,783
Interest revenue	➡	$3,217
To record first year lease revenue recognition		
Deferred inflow of resources	➡	$15,978
Lease revenue	➡	$15,978

Lessor Accounting - Example - Total 1st year entry - Government Wide

To record depreciation on building

Depreciation expense	➡	$133,333
Accumulated depreciation	➡	$133,333

Lease incentives

GASB 87 - Paragraphs 61-62

Lease incentives - definition

Payments made to or on behalf of the lessee or other concessions granted to the lessee

Examples:

- Rebates
- Discounts
- Assumption of lessee's preexisting lease obligations to 3rd parties
- Other reimbursements of lessee costs
- Rent holidays
- Reduction of interest/principal charges by the lessor

Lease incentives - **accounting**

- Incentives paid at or before commencement of the lease
  - Include an initial measurement by directly reducing the amount of the lease asset
- Incentives paid after commencement of the lease
  - Reduce payments to be made when performing the initial lease liability and receivable calculations
  - If variable do not include

Contracts with multiple components

GASB 87 - Paragraphs 63-70

Contracts with multiple components - **general**

- Separate out lease and non-lease components of a contract

- If a contract has multiple underlying assets in certain cases should account for each asset separately (for example, if they have different lease terms or are in different major class of asset)

- If multiple contracts are entered into at or near the same time and both the following is met, should treat as one lease contract with multiple components:

  1. Contracts negotiated as a package with single objective
  2. Amount of consideration to be paid in one contract depends on the price performance of another

Contracts with multiple components - **accounting**

- Account for multiple components as follows (in order of preference)
  - Allocate prices to components at the contract price if known and appears reasonable
  - If not known use best estimate
  - If this can't be done, treat all components as a single lease unit
- If this is done, base accounting on the primary lease component in that unit. For example, if there are multiple assets with different terms, use the term for the primary asset.

Lease modifications and terminations

GASB 87 - Paragraphs 71-79

Lease modifications and terminations - general

- Amendment to the contracts should be accounted for as a lease modification
  - Unless the lessee's right to use the asset decreases, then it should be accounted for as a partial or full termination
- **Amendments modify the provisions of a contract**
- Examples:
  - Changing contract price
  - Lengthening or shortening the lease term
  - Adding/removing an underlying asset

Lease modifications

- Both the lessee and lessor should treat a modification as a new lease agreement if both of the following exist:

  1. Lease modification gives the lessee an additional lease asset by adding one or more underlying assets not included in original lease.
  2. Increase in lease payments for additional lease asset does not appear to be unreasonable based on terms of the amended lease and professional judgment maximizing use of observable information.

Lease modifications

- If both criteria on the previous slide are not met, should account for the modification by remeasuring the lease liability/lease receivable.
  - The lease asset/deferred inflow should be adjusted by the same amount.
  - If the resulting adjustment results in the lease asset/deferred inflow going to zero report gain/loss for the difference.
  - For lessors to the extent the change relates to the current period, should recognize in the period of change.

Lease terminations

- Lessee
  - Reduce the carrying value of the asset and liability and recognize gain/loss for difference.
  - If lease is terminated due to purchasing of the asset, should reclass the asset to the proper class of owned assets.
- Lessor
  - Reduce the carrying value of receivable and deferred inflow and recognize gain/loss for difference.
  - If it is due to purchase, should derecognize the asset and include it in the gain/loss calculation.

Polling question #7

Sublease and leaseback transactions

GASB 87 - Paragraphs 80-87

Sublease

- Subleases have three parties involved:
  - Original lessor – Follow normal lessor accounting
  - Original lessee (sublease lessor) – treats the transaction as two separate leases. Should disclose separately subleases from original leases
  - Sublease lessee – Follow normal lessee accounting

Sale-leaseback

- Qualifying sale required (otherwise it is a borrowing)
- Treat sale and lease as separate transactions
  - Except the difference between the carrying value of the capital asset and net proceeds from sale should be deferred and recognized over the term of the lease.
- If it has off-market terms, difference should be reported based on the substance of the transaction.
  - Borrowing, nonexchange transaction, advance lease payment
- Disclose terms and conditions of sale-leaseback

Lease-leaseback

Example: A school district leases land to a developer. The developer builds a school and leases the school and land back to the school district.

- Account for as a net transaction.
- Gross amounts of each portion should be disclosed.

Intra-entity leases

GASB 87 - Paragraphs 88-89

Intra-entity leases

Blended Component Units

- Reporting requirements of this statement do not apply
  - When the lessor is a blended component unit, the debt and assets of the lessor are included with the primary government's assets and debt.

Discretely Presented Component Units

- Should follow this statement
  - Keep the related receivables/payables separate from other due to/due from or other lease receivable/payables with 3rd party organizations.

Related party leases

GASB 87 - Paragraphs 90-91

Related party leases

- Treat the same as other leases with unrelated parties unless the terms have been significantly impacted by the relationship.
- Should disclose the nature and extent of leasing transactions with related parties.
- **Example:**

  If the lease is structured as a short-term lease, but both parties know it will be in place for several years, should not account for it as a short-term lease.

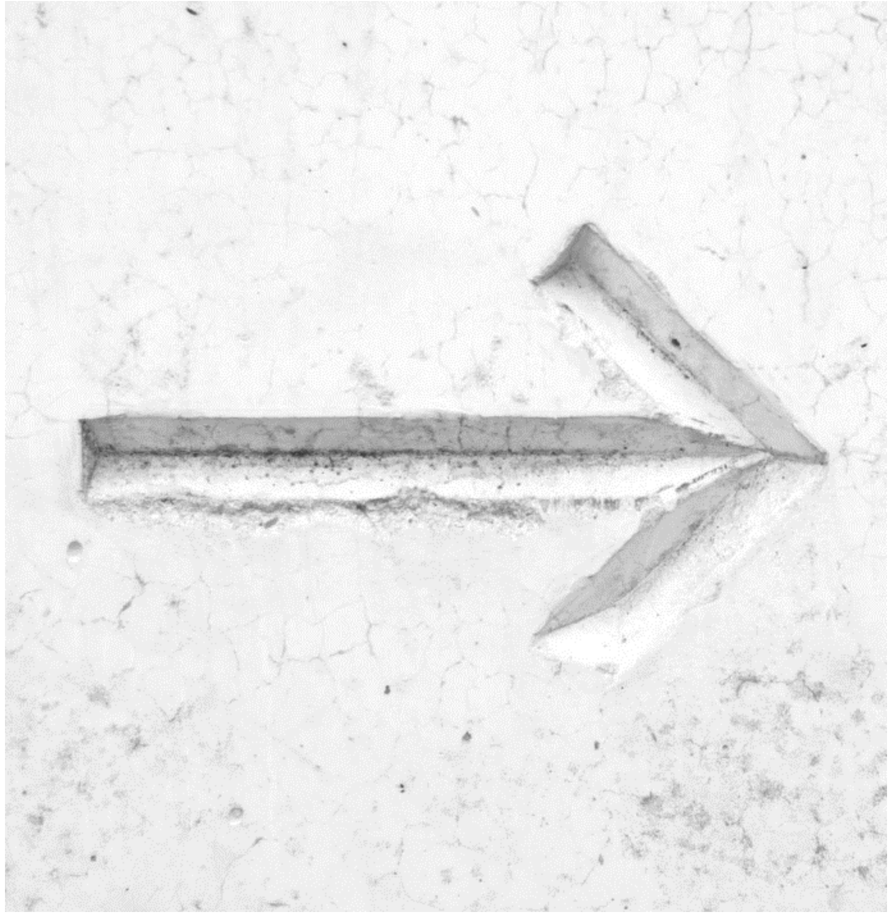
Transition

Transition

- Measure using facts and circumstances that exist at the beginning of the period of implementation (or earliest period restated).

- Lessors should not restate the assets underlying their existing sales-type or direct financing leases.

  Any residual assets for the leases become the carrying values of the underlying assets.



Transition

- Should apply retroactively by restating financial statements for all prior periods presented. If that isn’t practical the cumulative effect should be reported as a restatement of beginning net position for earliest period restated.

- Notes should disclose nature of restatement and its effect and reasoning for not restating prior periods should be disclosed.

Polling question #8

Implementation

Best practices - as provided by GFOA

Implementation - **step 1**

- Identify who currently maintains the information on various leases:
  - Finance
  - Legal
  - Purchasing
  - Administration or other departments (decentralized)
  - Are agreements approved at a centralized location or is it decentralized?

Implementation - **step 2**

- Look for agreements that are not currently reported as a lease (likely embedded leases)
  - Rental agreements
  - Search vendor payments and/or general ledger chart of accounts
  - From known lessors, request reports that list out all agreements
  - Review board minutes

Implementation - **step 3 - important!**

- Discuss the changes in lease accounting with all professionals across the government:
  - Purchasing needs to be informed on what to look out for as contracts are approved to help flag potential leases
  - Legal could also help with identification and with structuring agreements
  - Review how this might impact debt limits and other covenant requirements
  - Update financial policies that reference operating and capital leases

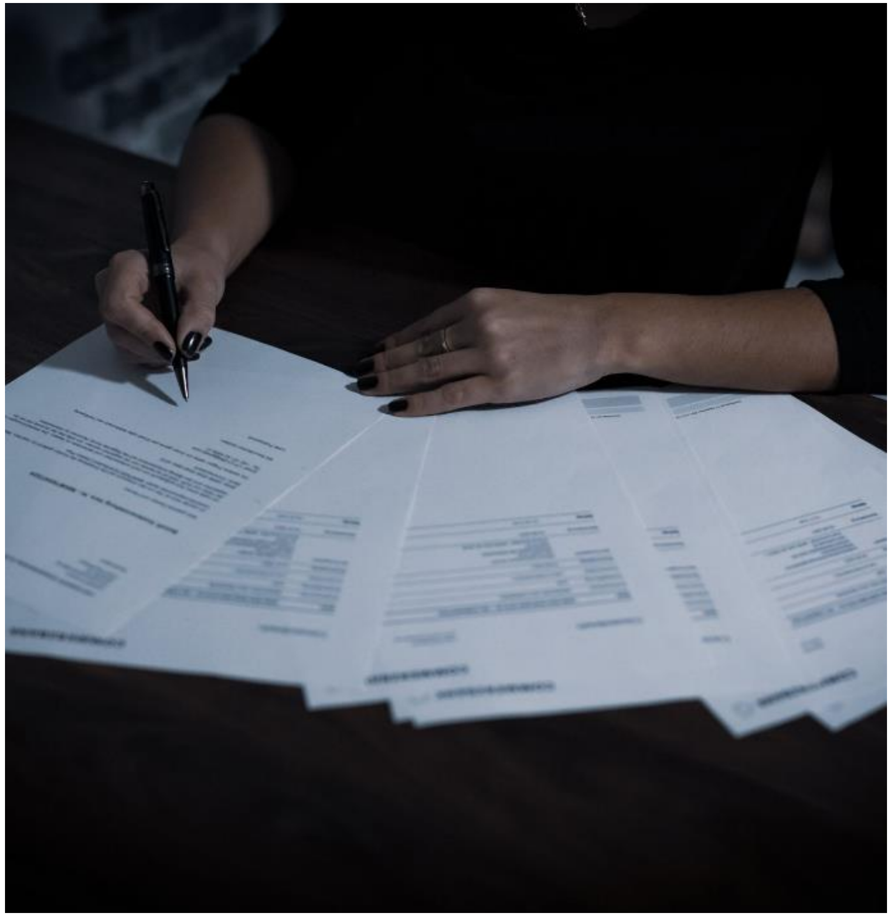
Implementation - **step 4**

- Review all lease agreements and consider renegotiating the terms to make them more explicit and easier to understand, specifically as it relates to the length of the agreement and the interest rate applied.

Implementation - **step 5**

- Review details of each lease contract to ensure they meet the scope of GASB 87 reporting.

- Accumulate data from the contracts needed to perform the journal entries and meet disclosure requirements.



Thank you!

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