



## Federal Accounting Standards Advisory Board

**April 11, 2017**

### Memorandum

To: Members of the Board

*Monica R. Valentine*

From: Monica R. Valentine, Assistant Director

*Wendy M. Payne*

Through: Wendy M. Payne, Executive Director

Subj: **Clarification Discussion on the Leases Exposure Draft—Tab A<sup>1</sup>**

#### MEMBER ACTION REQUESTED:

- Be prepared for an open dialog with several federal agency representatives concerning their views on the *Leases* proposal.

### MEETING OBJECTIVE

Representatives from five federal agencies will discuss their views on the *Leases* Exposure Draft (ED) with Board members. Following the clarification discussions with all five agencies, Board members will discuss with staff any high-level issues they feel should be addressed.

### BRIEFING MATERIAL

The briefing material includes this memorandum and the following attachments and appendices:

**Attachment 1:** Clarification discussion agenda

**Attachment 2:** Speaker biographies, prepared remarks, and potential questions

**Attachment 3:** Comment letters of presenter agencies

**Appendix A:** Original *Leases* exposure draft

**Appendix B:** Excerpts from February 2017 Board meeting – leases discussion

**Appendix C:** History of Board lease discussions

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<sup>1</sup> The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of FASAB or its staff. Official positions of FASAB are determined only after extensive due process and deliberations.

Each presentation will be limited to forty minutes, which will consist of ten minutes for presenter oral comments and thirty minutes for Board questions. After the clarification discussion, the Board will discuss the high-level issues that should be addressed based on information from the presenters during the clarification discussion.

## **NEXT STEPS**

Staff will further analyze the comment letters, provide additional issues with staff analysis and recommendations, and suggest edits to the original ED for Board consideration.

## **MEMBER FEEDBACK**

Please contact staff as soon as possible to convey your questions or suggestions. Communication before the meeting will help make the meeting more productive. You can contact Monica by telephone at 202-512-7362 or by e-mail at [ValentineM@fasab.gov](mailto:ValentineM@fasab.gov) with a cc to [PayneW@fasab.gov](mailto:PayneW@fasab.gov).

**Leases**  
**Clarifying Discussion Schedule**  
**April 26, 2017**

| <b>TIME</b>             | <b>AGENCY</b>                          | <b>PRESENTER'S NAMES</b>  | <b>LETTER #</b> |
|-------------------------|--|---|-----------------|
| <b>9:10 – 9:50 AM</b>   | <b>Department of Agriculture</b>       | <b>Michael Moore</b>  | <b>5</b>        |
| <b>9:55 – 10:35 AM</b>  | <b>Department of Energy</b>            | <b>William Truitt, John Wall, and Tynesha Douglass</b>                                  | <b>10</b>       |
| <b>10:35 – 10:50 AM</b> | <b>~~BREAK~~</b>                       | <b>~~BREAK~~</b>  | <b>~~</b>       |
| <b>10:50 – 11:30 AM</b> | <b>Department of the Interior</b>      | <b>Paul McEnrue</b>   | <b>19</b>       |
| <b>11:35 – 12:15 PM</b> | <b>Department of Defense</b>           | <b>Alaleh Jenkins, Edwin Oshiba, Melvin Randolph, Michael Walsh, and Steven Hurwitz</b> | <b>9</b>        |
| <b>12:15 – 1:00 PM</b>  | <b>~~LUNCH~~</b>                       | <b>~~LUNCH~~</b>  | <b>~~</b>       |
| <b>1:10 – 1:50 PM</b>   | <b>General Services Administration</b> | <b>Robert (Bob) Smalskas</b>  | <b>22</b>       |

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## Speaker Biographies, Prepared Remarks, and Potential Questions

*(Listed in order of appearance at the April 26, 2017 Leases ED Clarification Discussion)*

|                                      |    |
|--------------------------------------|----|
| Department of Agriculture .....      | 2  |
| Department of Energy .....           | 16 |
| Department of the Interior .....     | 33 |
| Department of Defense .....          | 57 |
| General Services Administration..... | 66 |
| Potential Questions .....            | 75 |

## **Department of Agriculture**

### **Michael Moore**

Michael Moore has been with USDA / Natural Resources Conservation Services (NRCS) since May 2010. He has served as the lead accountant for Property Plant & Equipment (PPE) accounting activities. The NRCS PPE portfolio includes Owned Real Property, accounting for operating and capital leases and, Owned Personal Property and Capitalized Internal Use Software. Coordinate activities for PPE with the Acquisitions' staff and staff in the state offices. He has authored and enhanced accounting policies and procedures for NRCS, and provided training to agency staff as required. His major accomplishments have been to enhance procedures and internal controls for PPE, and to have the PPE audit issues reduced from a material weakness in 2010 to a management letter comment in 2014.

Prior to NRCS Mr. Moore was a self-employed contractor (1 year), Fannie Mae (26+ years), and in public accounting (4 years). All of his work experience has centered on accounting, auditing, and business / financial analytics, as a staff person, business lead or manager.

Michael Moore  
Agency – USDA / NRCS

**NRCS Mission Statement**

"NRCS improves the health of our Nation's natural resources while sustaining and enhancing the productivity of American agriculture. We achieve this by providing voluntary assistance through strong partnerships with private landowners, managers, and communities to protect, restore, and enhance lands and waters upon which people and the environment depend".

As described in the Mission Statement, NRCS works with landowners and producers on America's working farm and ranch lands to identify, document and correct environmental concerns in a way that maintains a sustainable, highly productive agricultural land base, improves the economic viability of rural communities, improves the nation's water quality and quantity, and restores or enhances wildlife habitat through efficient and effective management of the nation's non-federal agricultural crop, hay, forest, and grazing lands.

**Capital Lease Accounting - Impact to NRCS**

Assets are leased by NRCS to provide convenience and services to the land owners and other customers; these leases have been primarily for office space, and for FY 2017, the population expands to include vehicles. These leasing activities are not a primary activity of the agency, as office leasing costs comprised approximately 1.5% of the total annual costs of operations for FY 2016. Therefore the annual lease costs are not material to the total costs for the agency. I cannot readily measure the impact to the balance sheet as the NPV / FMV data for the non-intragovernmental leases are not readily available.

The other concern with the potential transition to capital lease accounting is that more resources will be needed for the leasing, accounting, and other administrative functions, which reduces the available resources for the mission and its goals. The tasks related to lease scoring, and for accounting for and paying the operating and capital leases (excludes tasks for GSA Occupancy Agreements) are noted on pages 3 – 6.

## Overall Reaction

My motivation to address the FASAB group regarding the draft pronouncement relates my question as to what is presented as “assets” and “liabilities” on the face of the balance sheet for federal agencies, and the additional resources and costs to make this happen. Reverting back to Accounting principles, an asset is defined as “property owned by a person or company”. Subsequently FASAB No. 6 expanded the definition to include the costs of leased property that “transfers substantially all the benefits and risks of ownership to the lessee”. The exposure draft is seeking to provide relevant and meaningful lease information to Joe Public, and suggests that we include all leased property on the balance sheet, unless it is an intragovernmental lease, or a short term lease.

I have mixed thoughts on this proposal. Meaningful and relevant information is good, but are we distorting the lease accounting disclosures, and balance sheet amounts that are being presented? What is the impact to my agency (NRCS); definitely more work requiring additional resources, which detracts from the resources available to carry out the agency mission. How material are the NRCS lease transactions relative to the balance sheet and annual costs? Is there funding available to capitalize all of the non-intragovernmental leases? From a cost-benefit perspective, does this make sense? Are there other options that should be considered?

With these questions and thoughts looming, I thought through my experiences to better understand my interpretation of the exposure draft. The majority of my leasing experience has been with agreements for office space, which generally have clauses covering the noncancelable period, federal funding availability, and termination clauses. Therefore the lease costs, except for the existing NRCS capital leases, have been accounted for as period costs, i.e., pay as you go costs. For Joe Public, a federal financial statement user, is the current presentation (period cost) or the proposed presentation per the exposure draft more meaningful? Is the accounting profession proposing to make a simple transaction more complex than it needs to be? As an accountant I should be ecstatic as these requirements provide increased accounting opportunities. But as a federal

employee and taxpayer, I believe that we should be judicious in determining the tasks that we opt to do, as well as what we opt not to do when there is only slight increase, if any, to the value of the work or product.

## **Options**

There are other ways to enhance the lease info by enhancing the data provided in the notes, without having to account for all leases, excluding intragovernmental and short term leases, as capital leases.

Have all agencies report future payments for its leases in the notes to the financial statements, as presented in tables 23 and 24 on page 6. The effort and cost to provide the summary information should be far less than it would be compared to running the related lease transactions through the accounting and inventory systems in an effort to report these non-governmental leases as capital leases.

For agencies where leasing activities are a significant and material part of their activities, maybe it makes sense to capitalize the non-intragovernmental leases. But for other agencies where property leases are a tool needed to perform tasks for the mission, the accounting should be simple and cost efficient as previously stated. The agencies can continue to use their money for their mission and programs, and not have to spend it for administrative purposes, such as to enhance accounting and inventory systems, and to hire accountants.

Another option is a pro forma presentation of the Lease related accounts (asset, liability and expense) if all leases, excluding intragovernmental and short term leases, were capital leases. This assumes that the agencies can pull this information together without running all transactions through the accounting system.

## **OVERVIEW OF THE NRCS LEASE ACCOUNTING**

### **Lease Determination process**

**Obtain draft lease agreement; key attributes**

- 1. Lease term**
- 2. Monthly and annual rental payment**
- 3. Lease term, inclusive of renewal options**
- 4. Leased space (rentable square footage – rsf.)**
- 5. Fully Serviced**
- 6. Lease termination clause**

**Obtain GSA Form 1217 with the operating costs for leased space**

**Obtain Property data**

- 1. Fair Market Value**
- 2. Date of construction for the building**

**Lease Determination – operating vs capital lease**

### **Accounting for an Operating lease**

**NRCS currently has approximately 600 leases with non-Federal lessors (9/30/2016)**

**FSA is planning to transfer approximately 600 leases to NRCS during FY 2017 and FY 2018**

- 1. Create framework Purchase Order (PO) for each lease which is used to pay the lessor each month during the fiscal year**
- 2. Pay lessor the same amount for respective months during fiscal year**
- 3. All payments recorded to 6100 account**
- 4. Next fiscal year – create new framework PO for each lease**

### **Accounting for a capital lease**

**NRCS currently has 10 capital leases with non-Federal lessors**

1. Create an amortization schedule based on the key attributes for the lease; asset value (lesser of NPV or FMV), lease end date and monthly payment amount (see exhibit 1 for sample)
2. Create Funds Commitment Document with 3 lines for each lease which is used to pay the lessor each month during the fiscal year; first line for annual interest amount, second line for annual executory costs, and third line for principal.
3. The disbursement authority for the principal needs to match or exceed the life of the lease; 10 year lease would require no-year funding in most cases
4. Pay lessor the same amount for respective months during fiscal year, referencing funds commitment document info, and allocating amounts based on payment date to the interest cost (account 6330), executory cost (account 6100) and principal (account 2940).
5. Record amortization entry monthly
6. Reconcile the balance sheet accounts periodically (monthly / quarterly)
7. Next fiscal year – create new lines on Funds Commitment document for current year interest and executory costs

### **Current (FY 2016) Lease Disclosure**

#### **Tables 23 and 24 – Capital Leases, balance sheet and future payments**

#### **Table 25 – Operating Leases**

### **Note 9 — Leases**

NRCS has entered into leasing agreements with the General Services Administration (GSA) and other parties through leasing authority delegated by GSA. The leases are for office space for field office operations or for buildings and land for Plant Materials Centers. The lease arrangements generally range from five to ten years, but may be longer for Plant Materials Centers, and generally contain renewal options. Most leases are subject to cancellation upon certain funding conditions and all are covered by budgetary resources. NRCS enters into operating leases primarily for office space and some equipment. Capital lease assets and future payment information for capital and operating leases are shown in the tables below.

| <b>Entity as Lessee: Capital Leases</b>      | <b>2016<br/>(in millions)</b> |
|--|-------------------------------|
| <b>Summary of Assets Under Capital Lease</b> |                               |
| Land and Buildings                           | \$2                           |
| Less: Accumulated Amortization               | (2)                           |
| <b>Total Assets Under Capital Lease</b>      | <b>\$0</b>                    |

Table 23: Capital Leases Summary

| <b>Capital Leases – Future Payments Due:</b>   | <b>Land and<br/>Buildings<br/>(in millions)</b> |
|--|---|
| Year 1 (2017)                                  | \$1   |
| Year 2 (2018)                                  | 1   |
| Year 3 (2019)                                  | 0   |
| Year 4 (2020)                                  | 0   |
| Year 5 (2021)                                  | 0   |
| After 5 Years                                  | 0   |
| <b>Total Future Lease Payments</b>             | <b>\$2</b>                                      |
| Less: Imputed Interest                         | 0   |
| Less: Executory Costs                          | (1)   |
| <b>Net Capital Lease Liability</b>             | <b>\$1</b>                                      |
| Lease liability covered by budgetary resources | 1   |

Table 24: Future Payments for Capital Leases

| <b>Operating Leases – Future Payments Due:</b> | <b>Land and<br/>Buildings<br/>(in millions)</b> |
|--|---|
| Year 1 (2017)                                  | \$55  |
| Year 2 (2018)                                  | 41  |
| Year 3 (2019)                                  | 33  |
| Year 4 (2020)                                  | 26  |
| Year 5 (2021)                                  | 21  |
| After 5 Years                                  | 49  |
| <b>Total Future Lease Payments</b>             | <b>\$225</b>                                    |

Table 25: Total Future Payments for Operating Leases





# NRCS Property Leases - Amortization Schedule

Open

## Lease: 57-4310-7-3

Division: 13 Georgia

Toccoa Headquarter Field Office

**Lessor:** Stephens County Soil and Water  
110 South Alexander St  
Toccoa, GA 30577--

**Property** Willard Kimsey Environmental Edu. Building  
250 Clary Connector  
Toccoa, GA 30577

**This Lease is classified as a Capital Lease**

| Lease Data      |               |  |  | Lease Cost         |            | Lease Terms         |           |              |                  | Building Data          |  |
|-----------------|---------------|--|--|--------------------|------------|---------------------|-----------|--------------|------------------|------------------------|--|
| BBFY:           | 2008          |  |  | Annual Lease Amt   | \$9,600.00 | Start Date          | 10/1/2007 | End Date:    | 9/30/2012        |                        |  |
| Property Type:  | Facility      |  |  | Monthly Lease Amt  | \$800.00   | OptionNumber        | 2         | Option Years | 5                |                        |  |
| Lease Type:     | Capital Lease |  |  | Leased Square Feet | 500.00     | End Date w/ Options | 9/30/2022 | Yrs          | 15               |                        |  |
| Property Class: | Real Property |  |  |                    |            |                     |           |              | Building Type:   | Multi-Unit Office Bldg |  |
|                 |               |  |  |                    |            |                     |           |              | YearConstructed: | 2005                   |  |
|                 |               |  |  |                    |            |                     |           |              | EconomicLife:    | 30                     |  |
|                 |               |  |  |                    |            |                     |           |              | FairMarketValue: | \$214,754.40           |  |

| Other |               |               |          | Other Costs           |            | Schedule Values    |             |
|-------|---------------|---------------|----------|-----------------------|------------|--------------------|-------------|
| No    | TitleTransfer | Imputed Int   | 1.16%    | Executory Costs       | \$1,000.00 | NPV                | \$44,597.28 |
| No    | TitleTransfer | DiscountRate: | 5.1      | Real Estate Taxes     | \$0.00     | 90% Adj FMV        | \$24,159.87 |
| No    | Bargain Buy   | Total SqFt    | 4,000.00 | Annual Services       | \$4,340.00 | Asset Value (1810) | \$26,844.30 |
| No    | Gov Property  | Rental Type:  | Lease    | Total Costs (Monthly) | \$445.00   |                    |             |

### Amortization Schedule:

| Payments |              |                 | Liabilities      |          |           |           |                             | Assets                               |                        |                                    |
|----------|--------------|-----------------|------------------|----------|-----------|-----------|-----------------------------|--------------------------------------|------------------------|------------------------------------|
| Payment  | Payment Date | Monthly Payment | Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) | Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| 1        | 10/31/2007   | \$800.00        | 1.16%            | \$310.08 | \$44.92   | \$445.00  | \$26,799.38                 | \$26,695.17                          | \$149.14               | \$149.14                           |
| 2        | 11/30/2007   | \$800.00        | 1.16%            | \$309.56 | \$45.44   | \$445.00  | \$26,753.94                 | \$26,546.03                          | \$149.14               | \$298.27                           |
| 3        | 12/31/2007   | \$800.00        | 1.16%            | \$309.04 | \$45.96   | \$445.00  | \$26,707.98                 | \$26,396.90                          | \$149.14               | \$447.41                           |
| 4        | 1/31/2008    | \$800.00        | 1.16%            | \$308.51 | \$46.49   | \$445.00  | \$26,661.49                 | \$26,247.76                          | \$149.14               | \$596.54                           |
| 5        | 2/29/2008    | \$800.00        | 1.16%            | \$307.97 | \$47.03   | \$445.00  | \$26,614.46                 | \$26,098.63                          | \$149.14               | \$745.68                           |
| 6        | 3/31/2008    | \$800.00        | 1.16%            | \$307.43 | \$47.57   | \$445.00  | \$26,566.89                 | \$25,949.49                          | \$149.14               | \$894.81                           |
| 7        | 4/30/2008    | \$800.00        | 1.16%            | \$306.88 | \$48.12   | \$445.00  | \$26,518.77                 | \$25,800.36                          | \$149.14               | \$1,043.95                         |
| 8        | 5/31/2008    | \$800.00        | 1.16%            | \$306.32 | \$48.68   | \$445.00  | \$26,470.09                 | \$25,651.22                          | \$149.14               | \$1,193.08                         |
| 9        | 6/30/2008    | \$800.00        | 1.16%            | \$305.76 | \$49.24   | \$445.00  | \$26,420.85                 | \$25,502.09                          | \$149.14               | \$1,342.22                         |
| 10       | 7/31/2008    | \$800.00        | 1.16%            | \$305.19 | \$49.81   | \$445.00  | \$26,371.04                 | \$25,352.95                          | \$149.14               | \$1,491.35                         |
| 11       | 8/31/2008    | \$800.00        | 1.16%            | \$304.62 | \$50.38   | \$445.00  | \$26,320.66                 | \$25,203.82                          | \$149.14               | \$1,640.49                         |



**NRCS Property Leases - Amortization Schedule****Lease: 57-4310-7-3****Division: 13 Georgia****Amortization Schedule:**

| Payments |              |                 |
|----------|--------------|-----------------|
| Payment  | Payment Date | Monthly Payment |
| 12       | 9/30/2008    | \$800.00        |
| 13       | 10/31/2008   | \$800.00        |
| 14       | 11/30/2008   | \$800.00        |
| 15       | 12/31/2008   | \$800.00        |
| 16       | 1/31/2009    | \$800.00        |
| 17       | 2/28/2009    | \$800.00        |
| 18       | 3/31/2009    | \$800.00        |
| 19       | 4/30/2009    | \$800.00        |
| 20       | 5/31/2009    | \$800.00        |
| 21       | 6/30/2009    | \$800.00        |
| 22       | 7/31/2009    | \$800.00        |
| 23       | 8/31/2009    | \$800.00        |
| 24       | 9/30/2009    | \$800.00        |
| 25       | 10/31/2009   | \$800.00        |
| 26       | 11/30/2009   | \$800.00        |
| 27       | 12/31/2009   | \$800.00        |
| 28       | 1/31/2010    | \$800.00        |
| 29       | 2/28/2010    | \$800.00        |
| 30       | 3/31/2010    | \$800.00        |
| 31       | 4/30/2010    | \$800.00        |
| 32       | 5/31/2010    | \$800.00        |
| 33       | 6/30/2010    | \$800.00        |
| 34       | 7/31/2010    | \$800.00        |
| 35       | 8/31/2010    | \$800.00        |
| 36       | 9/30/2010    | \$800.00        |
| 37       | 10/31/2010   | \$800.00        |
| 38       | 11/30/2010   | \$800.00        |
| 39       | 12/31/2010   | \$800.00        |
| 40       | 1/31/2011    | \$800.00        |

| Liabilities      |          |           |           |                             |
|------------------|----------|-----------|-----------|-----------------------------|
| Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) |
| 1.16%            | \$304.03 | \$50.97   | \$445.00  | \$26,269.69                 |
| 1.16%            | \$303.45 | \$51.55   | \$445.00  | \$26,218.14                 |
| 1.16%            | \$302.85 | \$52.15   | \$445.00  | \$26,165.99                 |
| 1.16%            | \$302.25 | \$52.75   | \$445.00  | \$26,113.24                 |
| 1.16%            | \$301.64 | \$53.36   | \$445.00  | \$26,059.88                 |
| 1.16%            | \$301.02 | \$53.98   | \$445.00  | \$26,005.90                 |
| 1.16%            | \$300.40 | \$54.60   | \$445.00  | \$25,951.30                 |
| 1.16%            | \$299.77 | \$55.23   | \$445.00  | \$25,896.07                 |
| 1.16%            | \$299.13 | \$55.87   | \$445.00  | \$25,840.20                 |
| 1.16%            | \$298.48 | \$56.52   | \$445.00  | \$25,783.68                 |
| 1.16%            | \$297.83 | \$57.17   | \$445.00  | \$25,726.51                 |
| 1.16%            | \$297.17 | \$57.83   | \$445.00  | \$25,668.68                 |
| 1.16%            | \$296.50 | \$58.50   | \$445.00  | \$25,610.18                 |
| 1.16%            | \$295.83 | \$59.17   | \$445.00  | \$25,551.01                 |
| 1.16%            | \$295.14 | \$59.86   | \$445.00  | \$25,491.15                 |
| 1.16%            | \$294.45 | \$60.55   | \$445.00  | \$25,430.60                 |
| 1.16%            | \$293.75 | \$61.25   | \$445.00  | \$25,369.35                 |
| 1.16%            | \$293.05 | \$61.95   | \$445.00  | \$25,307.40                 |
| 1.16%            | \$292.33 | \$62.67   | \$445.00  | \$25,244.73                 |
| 1.16%            | \$291.61 | \$63.39   | \$445.00  | \$25,181.34                 |
| 1.16%            | \$290.87 | \$64.13   | \$445.00  | \$25,117.21                 |
| 1.16%            | \$290.13 | \$64.87   | \$445.00  | \$25,052.34                 |
| 1.16%            | \$289.38 | \$65.62   | \$445.00  | \$24,986.72                 |
| 1.16%            | \$288.63 | \$66.37   | \$445.00  | \$24,920.35                 |
| 1.16%            | \$287.86 | \$67.14   | \$445.00  | \$24,853.21                 |
| 1.16%            | \$287.08 | \$67.92   | \$445.00  | \$24,785.29                 |
| 1.16%            | \$286.30 | \$68.70   | \$445.00  | \$24,716.59                 |
| 1.16%            | \$285.50 | \$69.50   | \$445.00  | \$24,647.09                 |
| 1.16%            | \$284.70 | \$70.30   | \$445.00  | \$24,576.79                 |

| Assets                               |                        |                                    |
|--------------------------------------|------------------------|------------------------------------|
| Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| \$25,054.68                          | \$149.14               | \$1,789.62                         |
| \$24,905.55                          | \$149.14               | \$1,938.76                         |
| \$24,756.41                          | \$149.14               | \$2,087.89                         |
| \$24,607.28                          | \$149.14               | \$2,237.03                         |
| \$24,458.14                          | \$149.14               | \$2,386.16                         |
| \$24,309.01                          | \$149.14               | \$2,535.30                         |
| \$24,159.87                          | \$149.14               | \$2,684.43                         |
| \$24,010.74                          | \$149.14               | \$2,833.57                         |
| \$23,861.60                          | \$149.14               | \$2,982.70                         |
| \$23,712.47                          | \$149.14               | \$3,131.84                         |
| \$23,563.33                          | \$149.14               | \$3,280.97                         |
| \$23,414.20                          | \$149.14               | \$3,430.11                         |
| \$23,265.06                          | \$149.14               | \$3,579.24                         |
| \$23,115.93                          | \$149.14               | \$3,728.38                         |
| \$22,966.79                          | \$149.14               | \$3,877.51                         |
| \$22,817.66                          | \$149.14               | \$4,026.65                         |
| \$22,668.52                          | \$149.14               | \$4,175.78                         |
| \$22,519.39                          | \$149.14               | \$4,324.92                         |
| \$22,370.25                          | \$149.14               | \$4,474.05                         |
| \$22,221.12                          | \$149.14               | \$4,623.19                         |
| \$22,071.98                          | \$149.14               | \$4,772.32                         |
| \$21,922.85                          | \$149.14               | \$4,921.46                         |
| \$21,773.71                          | \$149.14               | \$5,070.59                         |
| \$21,624.58                          | \$149.14               | \$5,219.73                         |
| \$21,475.44                          | \$149.14               | \$5,368.86                         |
| \$21,326.31                          | \$149.14               | \$5,518.00                         |
| \$21,177.17                          | \$149.14               | \$5,667.13                         |
| \$21,028.04                          | \$149.14               | \$5,816.27                         |
| \$20,878.90                          | \$149.14               | \$5,965.40                         |





## NRCS Property Leases - Amortization Schedule

Lease: 57-4310-7-3

Division: 13 Georgia

### Amortization Schedule:

| Payments |              |                 |
|----------|--------------|-----------------|
| Payment  | Payment Date | Monthly Payment |
| 41       | 2/28/2011    | \$800.00        |
| 42       | 3/31/2011    | \$800.00        |
| 43       | 4/30/2011    | \$800.00        |
| 44       | 5/31/2011    | \$800.00        |
| 45       | 6/30/2011    | \$800.00        |
| 46       | 7/31/2011    | \$800.00        |
| 47       | 8/31/2011    | \$800.00        |
| 48       | 9/30/2011    | \$800.00        |
| 49       | 10/31/2011   | \$800.00        |
| 50       | 11/30/2011   | \$800.00        |
| 51       | 12/31/2011   | \$800.00        |
| 52       | 1/31/2012    | \$800.00        |
| 53       | 2/29/2012    | \$800.00        |
| 54       | 3/31/2012    | \$800.00        |
| 55       | 4/30/2012    | \$800.00        |
| 56       | 5/31/2012    | \$800.00        |
| 57       | 6/30/2012    | \$800.00        |
| 58       | 7/31/2012    | \$800.00        |
| 59       | 8/31/2012    | \$800.00        |
| 60       | 9/30/2012    | \$800.00        |
| 61       | 10/31/2012   | \$800.00        |
| 62       | 11/30/2012   | \$800.00        |
| 63       | 12/31/2012   | \$800.00        |
| 64       | 1/31/2013    | \$800.00        |
| 65       | 2/28/2013    | \$800.00        |
| 66       | 3/31/2013    | \$800.00        |
| 67       | 4/30/2013    | \$800.00        |
| 68       | 5/31/2013    | \$800.00        |
| 69       | 6/30/2013    | \$800.00        |

| Liabilities      |          |           |           |                             |
|------------------|----------|-----------|-----------|-----------------------------|
| Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) |
| 1.16%            | \$283.89 | \$71.11   | \$445.00  | \$24,505.68                 |
| 1.16%            | \$283.07 | \$71.93   | \$445.00  | \$24,433.75                 |
| 1.16%            | \$282.24 | \$72.76   | \$445.00  | \$24,360.99                 |
| 1.16%            | \$281.40 | \$73.60   | \$445.00  | \$24,287.39                 |
| 1.16%            | \$280.55 | \$74.45   | \$445.00  | \$24,212.94                 |
| 1.16%            | \$279.69 | \$75.31   | \$445.00  | \$24,137.63                 |
| 1.16%            | \$278.82 | \$76.18   | \$445.00  | \$24,061.45                 |
| 1.16%            | \$277.94 | \$77.06   | \$445.00  | \$23,984.39                 |
| 1.16%            | \$277.05 | \$77.95   | \$445.00  | \$23,906.44                 |
| 1.16%            | \$276.15 | \$78.85   | \$445.00  | \$23,827.59                 |
| 1.16%            | \$275.24 | \$79.76   | \$445.00  | \$23,747.83                 |
| 1.16%            | \$274.31 | \$80.69   | \$445.00  | \$23,667.14                 |
| 1.16%            | \$273.38 | \$81.62   | \$445.00  | \$23,585.52                 |
| 1.16%            | \$272.44 | \$82.56   | \$445.00  | \$23,502.96                 |
| 1.16%            | \$271.49 | \$83.51   | \$445.00  | \$23,419.45                 |
| 1.16%            | \$270.52 | \$84.48   | \$445.00  | \$23,334.97                 |
| 1.16%            | \$269.55 | \$85.45   | \$445.00  | \$23,249.52                 |
| 1.16%            | \$268.56 | \$86.44   | \$445.00  | \$23,163.08                 |
| 1.16%            | \$267.56 | \$87.44   | \$445.00  | \$23,075.64                 |
| 1.16%            | \$266.55 | \$88.45   | \$445.00  | \$22,987.19                 |
| 1.16%            | \$265.53 | \$89.47   | \$445.00  | \$22,897.72                 |
| 1.16%            | \$264.49 | \$90.51   | \$445.00  | \$22,807.21                 |
| 1.16%            | \$263.45 | \$91.55   | \$445.00  | \$22,715.66                 |
| 1.16%            | \$262.39 | \$92.61   | \$445.00  | \$22,623.05                 |
| 1.16%            | \$261.32 | \$93.68   | \$445.00  | \$22,529.37                 |
| 1.16%            | \$260.24 | \$94.76   | \$445.00  | \$22,434.61                 |
| 1.16%            | \$259.15 | \$95.86   | \$445.00  | \$22,338.75                 |
| 1.16%            | \$258.04 | \$96.96   | \$445.00  | \$22,241.79                 |
| 1.16%            | \$256.92 | \$98.08   | \$445.00  | \$22,143.71                 |

| Assets                               |                        |                                    |
|--------------------------------------|------------------------|------------------------------------|
| Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| \$20,729.77                          | \$149.14               | \$6,114.54                         |
| \$20,580.63                          | \$149.14               | \$6,263.67                         |
| \$20,431.50                          | \$149.14               | \$6,412.81                         |
| \$20,282.36                          | \$149.14               | \$6,561.94                         |
| \$20,133.23                          | \$149.14               | \$6,711.08                         |
| \$19,984.09                          | \$149.14               | \$6,860.21                         |
| \$19,834.96                          | \$149.14               | \$7,009.35                         |
| \$19,685.82                          | \$149.14               | \$7,158.48                         |
| \$19,536.69                          | \$149.14               | \$7,307.62                         |
| \$19,387.55                          | \$149.14               | \$7,456.75                         |
| \$19,238.42                          | \$149.14               | \$7,605.89                         |
| \$19,089.28                          | \$149.14               | \$7,755.02                         |
| \$18,940.15                          | \$149.14               | \$7,904.16                         |
| \$18,791.01                          | \$149.14               | \$8,053.29                         |
| \$18,641.88                          | \$149.14               | \$8,202.43                         |
| \$18,492.74                          | \$149.14               | \$8,351.56                         |
| \$18,343.61                          | \$149.14               | \$8,500.70                         |
| \$18,194.47                          | \$149.14               | \$8,649.83                         |
| \$18,045.34                          | \$149.14               | \$8,798.97                         |
| \$17,896.20                          | \$149.14               | \$8,948.10                         |
| \$17,747.07                          | \$149.14               | \$9,097.24                         |
| \$17,597.93                          | \$149.14               | \$9,246.37                         |
| \$17,448.80                          | \$149.14               | \$9,395.51                         |
| \$17,299.66                          | \$149.14               | \$9,544.64                         |
| \$17,150.53                          | \$149.14               | \$9,693.78                         |
| \$17,001.39                          | \$149.14               | \$9,842.91                         |
| \$16,852.26                          | \$149.14               | \$9,992.05                         |
| \$16,703.12                          | \$149.14               | \$10,141.18                        |
| \$16,553.99                          | \$149.14               | \$10,290.32                        |





## NRCS Property Leases - Amortization Schedule

Lease: 57-4310-7-3

Division: 13 Georgia

### Amortization Schedule:

| Payments |              |                 |
|----------|--------------|-----------------|
| Payment  | Payment Date | Monthly Payment |
| 70       | 7/31/2013    | \$800.00        |
| 71       | 8/31/2013    | \$800.00        |
| 72       | 9/30/2013    | \$800.00        |
| 73       | 10/31/2013   | \$800.00        |
| 74       | 11/30/2013   | \$800.00        |
| 75       | 12/31/2013   | \$800.00        |
| 76       | 1/31/2014    | \$800.00        |
| 77       | 2/28/2014    | \$800.00        |
| 78       | 3/31/2014    | \$800.00        |
| 79       | 4/30/2014    | \$800.00        |
| 80       | 5/31/2014    | \$800.00        |
| 81       | 6/30/2014    | \$800.00        |
| 82       | 7/31/2014    | \$800.00        |
| 83       | 8/31/2014    | \$800.00        |
| 84       | 9/30/2014    | \$800.00        |
| 85       | 10/31/2014   | \$800.00        |
| 86       | 11/30/2014   | \$800.00        |
| 87       | 12/31/2014   | \$800.00        |
| 88       | 1/31/2015    | \$800.00        |
| 89       | 2/28/2015    | \$800.00        |
| 90       | 3/31/2015    | \$800.00        |
| 91       | 4/30/2015    | \$800.00        |
| 92       | 5/31/2015    | \$800.00        |
| 93       | 6/30/2015    | \$800.00        |
| 94       | 7/31/2015    | \$800.00        |
| 95       | 8/31/2015    | \$800.00        |
| 96       | 9/30/2015    | \$800.00        |
| 97       | 10/31/2015   | \$800.00        |
| 98       | 11/30/2015   | \$800.00        |

| Liabilities      |          |           |           |                             |
|------------------|----------|-----------|-----------|-----------------------------|
| Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) |
| 1.16%            | \$255.78 | \$99.22   | \$445.00  | \$22,044.49                 |
| 1.16%            | \$254.64 | \$100.36  | \$445.00  | \$21,944.13                 |
| 1.16%            | \$253.48 | \$101.52  | \$445.00  | \$21,842.61                 |
| 1.16%            | \$252.31 | \$102.69  | \$445.00  | \$21,739.92                 |
| 1.16%            | \$251.12 | \$103.88  | \$445.00  | \$21,636.04                 |
| 1.16%            | \$249.92 | \$105.08  | \$445.00  | \$21,530.96                 |
| 1.16%            | \$248.71 | \$106.29  | \$445.00  | \$21,424.67                 |
| 1.16%            | \$247.48 | \$107.52  | \$445.00  | \$21,317.15                 |
| 1.16%            | \$246.24 | \$108.76  | \$445.00  | \$21,208.39                 |
| 1.16%            | \$244.98 | \$110.02  | \$445.00  | \$21,098.37                 |
| 1.16%            | \$243.71 | \$111.29  | \$445.00  | \$20,987.08                 |
| 1.16%            | \$242.42 | \$112.58  | \$445.00  | \$20,874.50                 |
| 1.16%            | \$241.12 | \$113.88  | \$445.00  | \$20,760.62                 |
| 1.16%            | \$239.81 | \$115.19  | \$445.00  | \$20,645.43                 |
| 1.16%            | \$238.48 | \$116.52  | \$445.00  | \$20,528.91                 |
| 1.16%            | \$237.13 | \$117.87  | \$445.00  | \$20,411.04                 |
| 1.16%            | \$235.77 | \$119.23  | \$445.00  | \$20,291.81                 |
| 1.16%            | \$234.39 | \$120.61  | \$445.00  | \$20,171.20                 |
| 1.16%            | \$233.00 | \$122.00  | \$445.00  | \$20,049.20                 |
| 1.16%            | \$231.59 | \$123.41  | \$445.00  | \$19,925.79                 |
| 1.16%            | \$230.17 | \$124.83  | \$445.00  | \$19,800.96                 |
| 1.16%            | \$228.72 | \$126.28  | \$445.00  | \$19,674.68                 |
| 1.16%            | \$227.26 | \$127.74  | \$445.00  | \$19,546.94                 |
| 1.16%            | \$225.79 | \$129.21  | \$445.00  | \$19,417.73                 |
| 1.16%            | \$224.30 | \$130.70  | \$445.00  | \$19,287.03                 |
| 1.16%            | \$222.79 | \$132.21  | \$445.00  | \$19,154.82                 |
| 1.16%            | \$221.26 | \$133.74  | \$445.00  | \$19,021.08                 |
| 1.16%            | \$219.71 | \$135.29  | \$445.00  | \$18,885.79                 |
| 1.16%            | \$218.15 | \$136.85  | \$445.00  | \$18,748.94                 |

| Assets                               |                        |                                    |
|--------------------------------------|------------------------|------------------------------------|
| Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| \$16,404.85                          | \$149.14               | \$10,439.45                        |
| \$16,255.72                          | \$149.14               | \$10,588.59                        |
| \$16,106.58                          | \$149.14               | \$10,737.72                        |
| \$15,957.45                          | \$149.14               | \$10,886.86                        |
| \$15,808.31                          | \$149.14               | \$11,035.99                        |
| \$15,659.18                          | \$149.14               | \$11,185.13                        |
| \$15,510.04                          | \$149.14               | \$11,334.26                        |
| \$15,360.91                          | \$149.14               | \$11,483.40                        |
| \$15,211.77                          | \$149.14               | \$11,632.53                        |
| \$15,062.64                          | \$149.14               | \$11,781.67                        |
| \$14,913.50                          | \$149.14               | \$11,930.80                        |
| \$14,764.37                          | \$149.14               | \$12,079.94                        |
| \$14,615.23                          | \$149.14               | \$12,229.07                        |
| \$14,466.10                          | \$149.14               | \$12,378.21                        |
| \$14,316.96                          | \$149.14               | \$12,527.34                        |
| \$14,167.83                          | \$149.14               | \$12,676.48                        |
| \$14,018.69                          | \$149.14               | \$12,825.61                        |
| \$13,869.56                          | \$149.14               | \$12,974.75                        |
| \$13,720.42                          | \$149.14               | \$13,123.88                        |
| \$13,571.29                          | \$149.14               | \$13,273.02                        |
| \$13,422.15                          | \$149.14               | \$13,422.15                        |
| \$13,273.02                          | \$149.14               | \$13,571.29                        |
| \$13,123.88                          | \$149.14               | \$13,720.42                        |
| \$12,974.75                          | \$149.14               | \$13,869.56                        |
| \$12,825.61                          | \$149.14               | \$14,018.69                        |
| \$12,676.48                          | \$149.14               | \$14,167.83                        |
| \$12,527.34                          | \$149.14               | \$14,316.96                        |
| \$12,378.21                          | \$149.14               | \$14,466.10                        |
| \$12,229.07                          | \$149.14               | \$14,615.23                        |





# NRCS Property Leases - Amortization Schedule

Lease: 57-4310-7-3

Division: 13 Georgia

## Amortization Schedule:

| Payments |              |                 |
|----------|--------------|-----------------|
| Payment  | Payment Date | Monthly Payment |
| 99       | 12/31/2015   | \$800.00        |
| 100      | 1/31/2016    | \$800.00        |
| 101      | 2/29/2016    | \$800.00        |
| 102      | 3/31/2016    | \$800.00        |
| 103      | 4/30/2016    | \$800.00        |
| 104      | 5/31/2016    | \$800.00        |
| 105      | 6/30/2016    | \$800.00        |
| 106      | 7/31/2016    | \$800.00        |
| 107      | 8/31/2016    | \$800.00        |
| 108      | 9/30/2016    | \$800.00        |
| 109      | 10/31/2016   | \$800.00        |
| 110      | 11/30/2016   | \$800.00        |
| 111      | 12/31/2016   | \$800.00        |
| 112      | 1/31/2017    | \$800.00        |
| 113      | 2/28/2017    | \$800.00        |
| 114      | 3/31/2017    | \$800.00        |
| 115      | 4/30/2017    | \$800.00        |
| 116      | 5/31/2017    | \$800.00        |
| 117      | 6/30/2017    | \$800.00        |
| 118      | 7/31/2017    | \$800.00        |
| 119      | 8/31/2017    | \$800.00        |
| 120      | 9/30/2017    | \$800.00        |
| 121      | 10/31/2017   | \$800.00        |
| 122      | 11/30/2017   | \$800.00        |
| 123      | 12/31/2017   | \$800.00        |
| 124      | 1/31/2018    | \$800.00        |
| 125      | 2/28/2018    | \$800.00        |
| 126      | 3/31/2018    | \$800.00        |
| 127      | 4/30/2018    | \$800.00        |

| Liabilities      |          |           |           |                             |
|------------------|----------|-----------|-----------|-----------------------------|
| Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) |
| 1.16%            | \$216.57 | \$138.43  | \$445.00  | \$18,610.51                 |
| 1.16%            | \$214.97 | \$140.03  | \$445.00  | \$18,470.48                 |
| 1.16%            | \$213.36 | \$141.64  | \$445.00  | \$18,328.84                 |
| 1.16%            | \$211.72 | \$143.28  | \$445.00  | \$18,185.56                 |
| 1.16%            | \$210.06 | \$144.94  | \$445.00  | \$18,040.62                 |
| 1.16%            | \$208.39 | \$146.61  | \$445.00  | \$17,894.01                 |
| 1.16%            | \$206.70 | \$148.30  | \$445.00  | \$17,745.71                 |
| 1.16%            | \$204.98 | \$150.02  | \$445.00  | \$17,595.69                 |
| 1.16%            | \$203.25 | \$151.75  | \$445.00  | \$17,443.94                 |
| 1.16%            | \$201.50 | \$153.50  | \$445.00  | \$17,290.44                 |
| 1.16%            | \$199.72 | \$155.28  | \$445.00  | \$17,135.16                 |
| 1.16%            | \$197.93 | \$157.07  | \$445.00  | \$16,978.09                 |
| 1.16%            | \$196.12 | \$158.88  | \$445.00  | \$16,819.21                 |
| 1.16%            | \$194.28 | \$160.72  | \$445.00  | \$16,658.49                 |
| 1.16%            | \$192.42 | \$162.58  | \$445.00  | \$16,495.91                 |
| 1.16%            | \$190.55 | \$164.45  | \$445.00  | \$16,331.46                 |
| 1.16%            | \$188.65 | \$166.35  | \$445.00  | \$16,165.11                 |
| 1.16%            | \$186.73 | \$168.27  | \$445.00  | \$15,996.84                 |
| 1.16%            | \$184.78 | \$170.22  | \$445.00  | \$15,826.62                 |
| 1.16%            | \$182.82 | \$172.18  | \$445.00  | \$15,654.44                 |
| 1.16%            | \$180.83 | \$174.17  | \$445.00  | \$15,480.27                 |
| 1.16%            | \$178.81 | \$176.19  | \$445.00  | \$15,304.08                 |
| 1.16%            | \$176.78 | \$178.22  | \$445.00  | \$15,125.86                 |
| 1.16%            | \$174.72 | \$180.28  | \$445.00  | \$14,945.58                 |
| 1.16%            | \$172.64 | \$182.36  | \$445.00  | \$14,763.22                 |
| 1.16%            | \$170.53 | \$184.47  | \$445.00  | \$14,578.75                 |
| 1.16%            | \$168.40 | \$186.60  | \$445.00  | \$14,392.15                 |
| 1.16%            | \$166.25 | \$188.75  | \$445.00  | \$14,203.40                 |
| 1.16%            | \$164.07 | \$190.94  | \$445.00  | \$14,012.46                 |

| Assets                               |                        |                                    |
|--------------------------------------|------------------------|------------------------------------|
| Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| \$12,079.94                          | \$149.14               | \$14,764.37                        |
| \$11,930.80                          | \$149.14               | \$14,913.50                        |
| \$11,781.67                          | \$149.14               | \$15,062.64                        |
| \$11,632.53                          | \$149.14               | \$15,211.77                        |
| \$11,483.40                          | \$149.14               | \$15,360.91                        |
| \$11,334.26                          | \$149.14               | \$15,510.04                        |
| \$11,185.13                          | \$149.14               | \$15,659.18                        |
| \$11,035.99                          | \$149.14               | \$15,808.31                        |
| \$10,886.86                          | \$149.14               | \$15,957.45                        |
| \$10,737.72                          | \$149.14               | \$16,106.58                        |
| \$10,588.59                          | \$149.14               | \$16,255.72                        |
| \$10,439.45                          | \$149.14               | \$16,404.85                        |
| \$10,290.32                          | \$149.14               | \$16,553.99                        |
| \$10,141.18                          | \$149.14               | \$16,703.12                        |
| \$9,992.05                           | \$149.14               | \$16,852.26                        |
| \$9,842.91                           | \$149.14               | \$17,001.39                        |
| \$9,693.78                           | \$149.14               | \$17,150.53                        |
| \$9,544.64                           | \$149.14               | \$17,299.66                        |
| \$9,395.51                           | \$149.14               | \$17,448.80                        |
| \$9,246.37                           | \$149.14               | \$17,597.93                        |
| \$9,097.24                           | \$149.14               | \$17,747.07                        |
| \$8,948.10                           | \$149.14               | \$17,896.20                        |
| \$8,798.97                           | \$149.14               | \$18,045.34                        |
| \$8,649.83                           | \$149.14               | \$18,194.47                        |
| \$8,500.70                           | \$149.14               | \$18,343.61                        |
| \$8,351.56                           | \$149.14               | \$18,492.74                        |
| \$8,202.43                           | \$149.14               | \$18,641.88                        |
| \$8,053.29                           | \$149.14               | \$18,791.01                        |
| \$7,904.16                           | \$149.14               | \$18,940.15                        |





## NRCS Property Leases - Amortization Schedule

Lease: 57-4310-7-3

Division: 13 Georgia

### Amortization Schedule:

| Payments |              |                 |
|----------|--------------|-----------------|
| Payment  | Payment Date | Monthly Payment |
| 128      | 5/31/2018    | \$800.00        |
| 129      | 6/30/2018    | \$800.00        |
| 130      | 7/31/2018    | \$800.00        |
| 131      | 8/31/2018    | \$800.00        |
| 132      | 9/30/2018    | \$800.00        |
| 133      | 10/31/2018   | \$800.00        |
| 134      | 11/30/2018   | \$800.00        |
| 135      | 12/31/2018   | \$800.00        |
| 136      | 1/31/2019    | \$800.00        |
| 137      | 2/28/2019    | \$800.00        |
| 138      | 3/31/2019    | \$800.00        |
| 139      | 4/30/2019    | \$800.00        |
| 140      | 5/31/2019    | \$800.00        |
| 141      | 6/30/2019    | \$800.00        |
| 142      | 7/31/2019    | \$800.00        |
| 143      | 8/31/2019    | \$800.00        |
| 144      | 9/30/2019    | \$800.00        |
| 145      | 10/31/2019   | \$800.00        |
| 146      | 11/30/2019   | \$800.00        |
| 147      | 12/31/2019   | \$800.00        |
| 148      | 1/31/2020    | \$800.00        |
| 149      | 2/29/2020    | \$800.00        |
| 150      | 3/31/2020    | \$800.00        |
| 151      | 4/30/2020    | \$800.00        |
| 152      | 5/31/2020    | \$800.00        |
| 153      | 6/30/2020    | \$800.00        |
| 154      | 7/31/2020    | \$800.00        |
| 155      | 8/31/2020    | \$800.00        |
| 156      | 9/30/2020    | \$800.00        |

| Liabilities      |          |           |           |                             |
|------------------|----------|-----------|-----------|-----------------------------|
| Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) |
| 1.16%            | \$161.86 | \$193.14  | \$445.00  | \$13,819.32                 |
| 1.16%            | \$159.63 | \$195.37  | \$445.00  | \$13,623.95                 |
| 1.16%            | \$157.37 | \$197.63  | \$445.00  | \$13,426.32                 |
| 1.16%            | \$155.09 | \$199.91  | \$445.00  | \$13,226.41                 |
| 1.16%            | \$152.78 | \$202.22  | \$445.00  | \$13,024.19                 |
| 1.16%            | \$150.44 | \$204.56  | \$445.00  | \$12,819.63                 |
| 1.16%            | \$148.08 | \$206.92  | \$445.00  | \$12,612.71                 |
| 1.16%            | \$145.69 | \$209.31  | \$445.00  | \$12,403.40                 |
| 1.16%            | \$143.27 | \$211.73  | \$445.00  | \$12,191.67                 |
| 1.16%            | \$140.83 | \$214.17  | \$445.00  | \$11,977.50                 |
| 1.16%            | \$138.35 | \$216.65  | \$445.00  | \$11,760.85                 |
| 1.16%            | \$135.85 | \$219.15  | \$445.00  | \$11,541.70                 |
| 1.16%            | \$133.32 | \$221.68  | \$445.00  | \$11,320.02                 |
| 1.16%            | \$130.76 | \$224.24  | \$445.00  | \$11,095.78                 |
| 1.16%            | \$128.17 | \$226.83  | \$445.00  | \$10,868.95                 |
| 1.16%            | \$125.55 | \$229.45  | \$445.00  | \$10,639.50                 |
| 1.16%            | \$122.90 | \$232.10  | \$445.00  | \$10,407.40                 |
| 1.16%            | \$120.22 | \$234.78  | \$445.00  | \$10,172.62                 |
| 1.16%            | \$117.51 | \$237.49  | \$445.00  | \$9,935.13                  |
| 1.16%            | \$114.76 | \$240.24  | \$445.00  | \$9,694.89                  |
| 1.16%            | \$111.99 | \$243.01  | \$445.00  | \$9,451.88                  |
| 1.16%            | \$109.18 | \$245.82  | \$445.00  | \$9,206.06                  |
| 1.16%            | \$106.34 | \$248.66  | \$445.00  | \$8,957.40                  |
| 1.16%            | \$103.47 | \$251.53  | \$445.00  | \$8,705.87                  |
| 1.16%            | \$100.56 | \$254.44  | \$445.00  | \$8,451.43                  |
| 1.16%            | \$97.62  | \$257.38  | \$445.00  | \$8,194.05                  |
| 1.16%            | \$94.65  | \$260.35  | \$445.00  | \$7,933.70                  |
| 1.16%            | \$91.64  | \$263.36  | \$445.00  | \$7,670.34                  |
| 1.16%            | \$88.60  | \$266.40  | \$445.00  | \$7,403.94                  |

| Assets                               |                        |                                    |
|--------------------------------------|------------------------|------------------------------------|
| Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| \$7,755.02                           | \$149.14               | \$19,089.28                        |
| \$7,605.89                           | \$149.14               | \$19,238.42                        |
| \$7,456.75                           | \$149.14               | \$19,387.55                        |
| \$7,307.62                           | \$149.14               | \$19,536.69                        |
| \$7,158.48                           | \$149.14               | \$19,685.82                        |
| \$7,009.35                           | \$149.14               | \$19,834.96                        |
| \$6,860.21                           | \$149.14               | \$19,984.09                        |
| \$6,711.08                           | \$149.14               | \$20,133.23                        |
| \$6,561.94                           | \$149.14               | \$20,282.36                        |
| \$6,412.81                           | \$149.14               | \$20,431.50                        |
| \$6,263.67                           | \$149.14               | \$20,580.63                        |
| \$6,114.54                           | \$149.14               | \$20,729.77                        |
| \$5,965.40                           | \$149.14               | \$20,878.90                        |
| \$5,816.27                           | \$149.14               | \$21,028.04                        |
| \$5,667.13                           | \$149.14               | \$21,177.17                        |
| \$5,518.00                           | \$149.14               | \$21,326.31                        |
| \$5,368.86                           | \$149.14               | \$21,475.44                        |
| \$5,219.73                           | \$149.14               | \$21,624.58                        |
| \$5,070.59                           | \$149.14               | \$21,773.71                        |
| \$4,921.46                           | \$149.14               | \$21,922.85                        |
| \$4,772.32                           | \$149.14               | \$22,071.98                        |
| \$4,623.19                           | \$149.14               | \$22,221.12                        |
| \$4,474.05                           | \$149.14               | \$22,370.25                        |
| \$4,324.92                           | \$149.14               | \$22,519.39                        |
| \$4,175.78                           | \$149.14               | \$22,668.52                        |
| \$4,026.65                           | \$149.14               | \$22,817.66                        |
| \$3,877.51                           | \$149.14               | \$22,966.79                        |
| \$3,728.38                           | \$149.14               | \$23,115.93                        |
| \$3,579.24                           | \$149.14               | \$23,265.06                        |





# NRCS Property Leases - Amortization Schedule

Lease: 57-4310-7-3

Division: 13 Georgia

## Amortization Schedule:

| Payments |              |                 |
|----------|--------------|-----------------|
| Payment  | Payment Date | Monthly Payment |
| 157      | 10/31/2020   | \$800.00        |
| 158      | 11/30/2020   | \$800.00        |
| 159      | 12/31/2020   | \$800.00        |
| 160      | 1/31/2021    | \$800.00        |
| 161      | 2/28/2021    | \$800.00        |
| 162      | 3/31/2021    | \$800.00        |
| 163      | 4/30/2021    | \$800.00        |
| 164      | 5/31/2021    | \$800.00        |
| 165      | 6/30/2021    | \$800.00        |
| 166      | 7/31/2021    | \$800.00        |
| 167      | 8/31/2021    | \$800.00        |
| 168      | 9/30/2021    | \$800.00        |
| 169      | 10/31/2021   | \$800.00        |
| 170      | 11/30/2021   | \$800.00        |
| 171      | 12/31/2021   | \$800.00        |
| 172      | 1/31/2022    | \$800.00        |
| 173      | 2/28/2022    | \$800.00        |
| 174      | 3/31/2022    | \$800.00        |
| 175      | 4/30/2022    | \$800.00        |
| 176      | 5/31/2022    | \$800.00        |
| 177      | 6/30/2022    | \$800.00        |
| 178      | 7/31/2022    | \$800.00        |
| 179      | 8/31/2022    | \$800.00        |
| 180      | 9/30/2022    | \$800.00        |

| Liabilities      |          |           |           |                             |
|------------------|----------|-----------|-----------|-----------------------------|
| Imputed Interest | Interest | Principle | Executory | Liability Balance (GL 2940) |
| 1.16%            | \$85.52  | \$269.48  | \$445.00  | \$7,134.46                  |
| 1.16%            | \$82.41  | \$272.59  | \$445.00  | \$6,861.87                  |
| 1.16%            | \$79.26  | \$275.74  | \$445.00  | \$6,586.13                  |
| 1.16%            | \$76.08  | \$278.92  | \$445.00  | \$6,307.21                  |
| 1.16%            | \$72.86  | \$282.14  | \$445.00  | \$6,025.07                  |
| 1.16%            | \$69.60  | \$285.40  | \$445.00  | \$5,739.67                  |
| 1.16%            | \$66.30  | \$288.70  | \$445.00  | \$5,450.97                  |
| 1.16%            | \$62.97  | \$292.04  | \$445.00  | \$5,158.93                  |
| 1.16%            | \$59.59  | \$295.41  | \$445.00  | \$4,863.52                  |
| 1.16%            | \$56.18  | \$298.82  | \$445.00  | \$4,564.70                  |
| 1.16%            | \$52.73  | \$302.27  | \$445.00  | \$4,262.43                  |
| 1.16%            | \$49.24  | \$305.76  | \$445.00  | \$3,956.67                  |
| 1.16%            | \$45.70  | \$309.30  | \$445.00  | \$3,647.37                  |
| 1.16%            | \$42.13  | \$312.87  | \$445.00  | \$3,334.50                  |
| 1.16%            | \$38.52  | \$316.48  | \$445.00  | \$3,018.02                  |
| 1.16%            | \$34.86  | \$320.14  | \$445.00  | \$2,697.88                  |
| 1.16%            | \$31.16  | \$323.84  | \$445.00  | \$2,374.04                  |
| 1.16%            | \$27.43  | \$327.58  | \$445.00  | \$2,046.46                  |
| 1.16%            | \$23.64  | \$331.36  | \$445.00  | \$1,715.10                  |
| 1.16%            | \$19.81  | \$335.19  | \$445.00  | \$1,379.91                  |
| 1.16%            | \$15.94  | \$339.06  | \$445.00  | \$1,040.85                  |
| 1.16%            | \$12.03  | \$342.97  | \$445.00  | \$697.88                    |
| 1.16%            | \$8.06   | \$346.94  | \$445.00  | \$350.94                    |
| 1.16%            | \$4.06   | \$350.94  | \$445.00  | \$0.00                      |

| Assets                               |                        |                                    |
|--------------------------------------|------------------------|------------------------------------|
| Asset Balance (GL 1810 less GL 1819) | Depreciation (GL 1819) | Accumulated Depreciation (GL 1819) |
| \$3,430.11                           | \$149.14               | \$23,414.20                        |
| \$3,280.97                           | \$149.14               | \$23,563.33                        |
| \$3,131.84                           | \$149.14               | \$23,712.47                        |
| \$2,982.70                           | \$149.14               | \$23,861.60                        |
| \$2,833.57                           | \$149.14               | \$24,010.74                        |
| \$2,684.43                           | \$149.14               | \$24,159.87                        |
| \$2,535.30                           | \$149.14               | \$24,309.01                        |
| \$2,386.16                           | \$149.14               | \$24,458.14                        |
| \$2,237.03                           | \$149.14               | \$24,607.28                        |
| \$2,087.89                           | \$149.14               | \$24,756.41                        |
| \$1,938.76                           | \$149.14               | \$24,905.55                        |
| \$1,789.62                           | \$149.14               | \$25,054.68                        |
| \$1,640.49                           | \$149.14               | \$25,203.82                        |
| \$1,491.35                           | \$149.14               | \$25,352.95                        |
| \$1,342.22                           | \$149.14               | \$25,502.09                        |
| \$1,193.08                           | \$149.14               | \$25,651.22                        |
| \$1,043.95                           | \$149.14               | \$25,800.36                        |
| \$894.81                             | \$149.14               | \$25,949.49                        |
| \$745.68                             | \$149.14               | \$26,098.63                        |
| \$596.54                             | \$149.14               | \$26,247.76                        |
| \$447.41                             | \$149.14               | \$26,396.90                        |
| \$298.27                             | \$149.14               | \$26,546.03                        |
| \$149.14                             | \$149.14               | \$26,695.17                        |
| \$0.00                               | \$149.14               | \$26,844.30                        |

## **Department of Energy**

### **William Truitt**

William Truitt currently serves as Director of the Department of Energy's (DOE's) Financial Policy Division within the Office of the Chief Financial Officer. Prior to joining DOE, he was Functional Manager of the Department of Justice's department-wide Unified Financial Management System (UFMS). In that capacity, he led the functional requirements analysis, configuration, and testing for implementation of UFMS in the Bureau of Alcohol, Tobacco, Firearms and Explosives; United States Marshals Service; and the Federal Bureau of Investigation. Mr. Truitt has served in numerous other senior level financial management positions including Chief, Office of Finance in the United States Marshals Service, and Chief of Financial Integrity in the Drug Enforcement Administration. His federal career spans more than 30 years with management experience in financial systems, operations, policy, accounting, and reporting. Mr. Truitt is a graduate of the University of Maryland with B.S. degrees in accounting and personnel/labor relations.

### **John Wall**

Mr. Wall began his Federal career in June 1984 when he joined the Department of Navy, Accounts Payable Division, as a Federal Junior Fellowship program participant. After graduation from college, Mr. Wall joined the Department of Energy, Office of the Inspector General, as an Auditor, where he was twice named Auditor-of-the-year and progressed to become an Audit Team Leader. In 2006, he joined the Department of Energy, Office of the Chief Financial Officer, as a Staff Accountant in the Office of Financial Policy. Mr. Wall has over 32 years of Federal experience. He is a native Washingtonian and is a 1984 graduate of Paul Laurence Dunbar Senior High School and a 1988 graduate of the University of the District of Columbia.

### **Tynesha Douglass**

Ms. Douglass joined the Department of Energy in May 2015. She has 13 years of accounting experience, with 3 years in the federal government. She began her career with the Defense Contract Audit Agency (DCAA) where she performed incurred cost audits of small contractors, as part of a mobile audit team. From there, she worked for several regional accounting firms performing contract audits, financial statement audits, and property management system reviews. Ms. Douglass has a bachelor's degree in accounting from the University of Maryland and a master's degree in accounting from Strayer University. She is a member of the Association of Government Accountants and the Maryland Association of Certified Public Accountants.





# FASAB Proposed Changes to Lease Reporting

Presented by:

William Truitt

Tynesha Douglass

John Wall

# Proposed Significant Changes in Recording Leases

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- The recording of leases will rely on the non-cancellable portion of the lease term instead of the traditional measures for recording leases.
- Recording leases (proprietary) and scoring of leases (budgetary) will not be as closely aligned as in the past. Budgetary references would still use the terms “capital” and “operating” leases.
- Clarification of the definition of a lease. In the exposure draft forwarded to agencies a lease would be defined as “a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.”

# Department of Energy Leases

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- As of September 30, 2016, the Department and its management and operating contractors have entered into leases (both capital and operating) with a total of future lease payments of approximately \$4.1 B with a total net assets under capital leases of approximately \$2.1 B.
- These agreements include leases for real estate as well as power lines for the Power Marketing Administrations.

# Summary of DOE Concerns

- While the Department of Energy (DOE) generally concurred with the FASAB exposure draft on *Leases*, issued September 26, 2016, we did have some concerns which we requested the Board to reconsider:

| Topic for Discussion                    | Lease Exposure Draft Question |
|---|-------------------------------|
| Recognition of Lease Liability          | 3                             |
| Measurement of Lease Liability          | 4                             |
| Definition of “Significantly Affect”    | 6(a)                          |
| Carrying Value of Re-measured Liability | 6(c)                          |
| Recognition of a Short Term Lease       | 9                             |
| Intragovernmental Leases                | 10                            |
| Accounting for Software                 | Other Matters                 |

# Recognition of Lease Liability

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- At paragraph 19, the Board proposed that at the beginning of a lease term, a lessee should recognize a lease liability and a property, plant, and equipment right to use lease asset, except for intragovernmental and short term leases.
- DOE agreed with the proposed guidance for lease recognition. However, we suggested the new “right to use” Standard General Ledger account be available when the standard is implemented. In addition, we recommend that USSGL in Treasury develop a posting model for these transactions to ensure uniformity in recognizing the liability and right to use lease asset.

# Measurement of Lease Liability

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- At paragraph 21(a – g), the Board proposed measurement of a lease liability should include several types of payments required by a lease.
- DOE agreed with the types of proposed payments. However, we believe payments required to be made by the lessee under non-routine or unique circumstances, such as triple net leasing arrangements (please see slide 7), should be considered when measuring a lease liability.
- Some lease payments required under non-routine or unique circumstances, such as triple net leasing, could impact how the lease is ultimately scored for budgetary purposes.

# Measurement of Lease Liability (continued)

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- The definition of a triple net lease is as follows:

*“A triple net lease is a lease agreement that designates the lessee, which is the tenant, as being solely responsible for all the costs relating to the asset being leased, in addition to the rent fee applied under the lease. The structure of this type of lease requires the lessee to pay the net amount for three types of costs, including net real estate taxes on the leased asset, net building insurance and net common area maintenance. This type of lease can also be referred to as a net-net-net (NNN) lease.”*

- For example, if a property owner leases out a building to a business using a triple net lease, the tenant is responsible for paying the building's property taxes, building insurance and the cost of any maintenance or repairs the building may require during the term of the lease. Because the tenant is covering these costs, which would otherwise be the responsibility of the property owner, the rent charged in the triple net lease is generally lower than the rent charged in a standard lease agreement.
- Source: <http://www.investopedia.com/terms/n/netnetnet.asp>

# Measurement of Lease Liability (continued)

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- According to OMB Circular A-11 (2016)
  - ❑ Appendix A, Paragraph 11 (Scoring Purchases), Page 3:  
*“Property taxes will not be considered to be an operating cost.”*
  - ❑ Appendix B, Paragraph 2(b) (Budget Presentation), Page 4  
*“The up-front budget authority required for both lease-purchases and capital leases is called the asset cost. This equals the present value of the minimum lease and other contractually required payments excluding payments for identifiable annual operating expenses that would be paid by the Government as owner, such as utilities, minor maintenance, and insurance. Property taxes will not be considered to be an operating expense and will be included in the calculation of the up-front budget authority. Other contractually required payments include any and all costs related to the asset being leased in addition to the rent fee applied under the lease.”*



## Definition of “Significantly Affect”

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- At paragraph 25, the Board proposed a lessee should re-measure its lease liabilities at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability.
- The term “significantly affect” is not defined in the current version of the FASAB Handbook.
- Without clear guidance on how “significantly affect” is defined in the context of the re-measurement of leases, the term is subject to government-wide interpretation and potential misapplication with respect to re-measuring lease liabilities.

# Carrying Value of a Re-measured Lease Liability

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- Paragraph 33 states, *“The lease asset generally should be adjusted by the same amount when the corresponding lease liability is re-measured based on paragraphs 25–29. However, if this change reduces the carrying value of the lease asset to zero, any remaining amount should be reporting in the flows statement as a gain”* on the asset.
- The Department requests FASAB provide examples for each of the circumstances in paragraphs 25-29 in which a leased asset could have a carrying value left over to be reported as a gain when the associated lease liability has been reduced to zero.
- Our concern is there is a high likelihood it would not be any “gain” to report on a lease liability, once the lease liability has been reduced to zero.
- Are we now to record the remaining value of the asset as a gain?

# Recognition of a Short Term Lease

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- Generally, the Department agreed with the proposed definition, measurement, and recognition of a short term lease.
- However, we are concerned there is a possible misinterpretation between paragraphs 14 and 59 on the determination of a lease. We would like the Board to clarify whether its intent was that Paragraph 14 would be the final qualifier for defining a lease term.

# Recognition of a Short Term Lease (continued)

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- Please consider the following scenarios:
  - ☐ Scenario 1: The Department enters into a lease contract as a lessee for 16 months with an option period of 9 months. If the Department has the option to cancel the 9 month option period of its lease, the maximum lease term to be evaluated would be 16 months (the non-cancellable portion of the lease) under paragraphs 14 and 59.
  - ☐ Scenario 2: The Department enters into a lease contract as a lessee for 16 months, with the probable exercise of a 9 month lease option period. Based on the Department's interpretation of paragraph 14, this lease contract would not qualify as a short term lease because the lease term is 25 months. Therefore, this lease will have to be tracked and recorded as a lease asset and lease liability.

# Intragovernmental Leases

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- The Department partially agrees with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases.
- At Paragraphs 82 – 85 and 90 – 92 we would like the FASAB to clarify the importance of the distinction between a "lease incentive" and "lease concession," when the effect of both types of incentives as applied to intragovernmental leases, appear to be the same.
- Lease incentives and lease concessions are provided by a lessor to entice the lessee to sign the lease. They both result in reduced rental income received by the lessor and paid by the lessee. The basis for conclusions at paragraph A29, which states "lease incentives and concessions should be recognized by the lessee/lessor as reductions of lease rental expense/lease rental income", supports the analogous interpretation of these two terms.

# Accounting for Software

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- Although an update to SFFAS 10 (Accounting for Internal Use Software) is not specifically a topic for discussion under this exposure draft, for future FASAB activities, we believe it may be helpful to provide the following questions pertaining to the treatment of software under the new lease standards.
  - ☐ Question #1: SFFAS 10 already classifies internal use software as PP&E. What other software besides internal use software is expected to be treated as a lease?
  - ☐ Question #2: Is internal use software included as a right-to-use asset? What assets would this definition include — only plant and equipment assets and internal use software? For example, would agreements for “software as a service” (SaaS) or cloud applications or data storage fall under this guidance, or are these items considered services and therefore exempt?
  - ☐ Question #3: Since SaaS applications are not controlled by the lessee in the same manner as a more customized Enterprise Resource Planning (i.e., Oracle) system, does that warrant different accounting treatment?

# Accounting for Software (continued)

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- ❑ Question #4: Are annual payments for software licenses considered leases? If yes, are the annual renewals considered short term leases?
  
- ❑ Question #5: Can the Board clarify or define “if and when” to include software licenses or maintenance licenses as a “lease” if the license is for a period longer than 2 years? For example:
  - *One-time perpetual leases with annual maintenance agreements.*
  - *Non-perpetual licenses “lease” software for use for a specified period of time. Users are required to remove the software from their computer if they cease paying for the license fee.*
  - *Some license agreements allow the user to purchase “maintenance” or “software assurance” along with the original license fee, which entitles the user to receive new versions of the software until the maintenance agreement expires.*
  
- ❑ Question #6: How are umbrella software agreements accounted for?

# Points of Contacts

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- Thanks for the opportunity to address the Board and discuss our concerns and give suggestions:
- Chief Financial Officer Contacts:
  - Tynesha Douglass: [Tynesha.Douglass@hq.doe.gov](mailto:Tynesha.Douglass@hq.doe.gov) (202) 586-6144
  - William Truitt: [William.Truitt@hq.doe.gov](mailto:William.Truitt@hq.doe.gov) (202) 586-1065
  - John Wall: [John.Wall@hq.doe.gov](mailto:John.Wall@hq.doe.gov) (202) 586-5728
- Office of Management Contact:
  - David Steinau: [David.Steinau@hq.doe.gov](mailto:David.Steinau@hq.doe.gov) (202) 287-1503



## **Department of the Interior**

### **Paul McEnrue**

Paul McEnrue has been Chief, Financial Reporting Division and Audit Liaison in the Office of Financial Management for the Department of the Interior since September 2012. Paul was Chief, Office of Accounting and Financial Management for 7 years at the U.S. Geological Survey. Paul spent 9 years in public accounting before starting his career in Government. He spent 4 years with the Department of Commerce auditing the sales and cost of production of foreign corporations that are the subject of an antidumping investigation. He spent 5 years in Commerce's Office of Financial Management, preparing the Department's consolidated financial statements and revising its Financial Management Handbooks. He was detailed for a year to assist with financial management at the Census Bureau during the Decennial Census and acted as audit liaison during the financial statement audits. In 2001, Paul was in the CFO Council Fellows Program and did his Fellowship with the Department of Interior's Office of Financial Management.

# DOI Comments on Leases Exposure Draft

April 26, 2017 FASAB Monthly Meeting

# Lease Definition

- A lease is a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.
- Suggest clarifying where easements and land rights, licenses, concession agreements, etc. fall under this definition. Update: After internal discussion, DOI agrees that easements, land rights, and licenses fall under the proposed definition, and concession agreements do not meet the criteria for leases.

# Lease Term

- The lease term is determined as *the period during which a lessee has a noncancelable right to use an underlying asset* (referred to as the noncancelable period) plus each option period if it is probable, based on all relevant factors, that the lessee will exercise that option to extend the lease.
- DOI disagrees with the use of the phrase “lessee’s noncancelable right” as it implies that the lessee’s right to use the underlying asset cannot be canceled by the lessor, which may not be an accurate statement. DOI suggests rephrasing such as “.....*the period during which the lessee cannot cancel the lease without penalty*” to avoid confusion.

# Lease Term (continued)

- The definition of “Lease Term” does not address the period between noncancelable period (firm term) and expiration date of the initial lease period.
- Example: 10-year lease, with noncancelable period or firm term from year 1 to year 5, and option years (after 10 year) 11, 12, 13, and 14. The proposed lease term does not address year 6 to year 10.
- Although in Paragraph 15b an attempt is made to redefine “noncancelable period” to include the period between the “firm term” and the expiration date of the lease (year 6 to year 10 in the example), it’s confusing as noncancelable period is the “firm term” in the leasing world.

# Lease Term (continued)

- Paragraph 15 of Leases ED:

The noncancelable period is the shorter of

- a. the initial lease period, before considering renewal options for additional periods;
- **b. the period of the lease preceding an option for the lessee to terminate the lease if it is probable, based on all relevant factors, that the lessee will exercise that option to terminate;** or
- c. the period of the lease preceding a point at which either the lessor only or both the lessee and the lessor have an option to terminate the lease, regardless of the probability of termination.

# Lease Term (continued)

- **DOI suggestion:** *The lease term is determined as the period during which the lessee cannot cancel the lease without penalty (noncancelable period or firm term), plus the cancelable period of the lease before the expiration date if it's probable that the lessee will not cancel, plus each option period if it's probable, based on all relevant factors, that the lessee will exercise that option to extend the lease.*

# Lease Term (continued)

- Determining probabilities of extensions will pose problems.
  - Leases are usually long-term. Determining the probability of exercising the option at the beginning of the lease may be difficult;
  - May be inconsistencies;
  - May be subjective.



# Lease Liability Recognition

- At the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases.

# Lease Liability Recognition (continued)

- Clarification and/or confirmation of interpretation of the subleases section of the ED needed. Our interpretation of subleases: when GSA is the original lessee with a non-intragovernmental lessor and then leases that non-intragovernmental lease to another government entity, the other government entity is the new lessee and should apply the “intragovernmental” general lessee guidance for this lease. Is this the correct interpretation? Update: Resolved after internal discussion. The lease between GSA and another government entity is an intragovernmental lease.

# Lease Liability Recognition (continued)

- There is no definition of what ‘general lessee guidance’ is in the ED. ‘General lessee guidance’, specifically, is only used under the Subleases section (Paragraph 68, page 22), but ‘general guidance’ is used only under the ‘intragovernmental’ section of the ED (under Recognition and Measurement section, page 25).
  - Suggest removing “general” from the last sentence in Paragraph 68, “The new lessee should apply the **general** lessee guidance”, to avoid confusion.
  - Comment on page 25 has been resolved as the intragovernmental leases section has a section for general guidance and a section for specific topics.

# Lease Liability Recognition (continued)

- Liability may not exist due to abrupt change in administration or project termination.
  - Circumstances may be unpredictable. The President or Congress may decide to terminate the funding for the lease if the rents are determined too expensive or the lease is determined to be nonessential (i.e., reduce the footprint initiative).

# Lease Liability Recognition (continued)

- Inflate Balance Sheet by recording an asset and a liability with no net impact on Net Position.
  - The asset and liability may not exist as circumstances may change anytime (see previous comment).

# Lease Liability Recognition (continued)

- Increase reporting burden.
  - Recording a lease liability at the present value of probable future payments and constantly adjusting the liability and recognizing an interest expense as monthly rents are paid would create numerous transactions in the financial system.
  - The constant efforts do not justify the benefits, especially in the current political landscape when agencies face budget cuts and must decide what activities need to be reduced or eliminated.
  - The current Future Minimum Lease Payments disclosure provides sufficient information to stakeholders and is consistent with OMB Circular A-11 on budget scoring.
  - If the reason for the proposed standard is to recognize the interest expense on leases, the interest expense can be calculated when rent payments are made by comparing the actual payment to the discounted amount using the future minimum lease payment report, without recognizing an asset and a liability for every lease. To DOI, interest expense related to rent may be immaterial.

# Lease Liability Measurement

- A lessee should measure the **lease liability** initially at the present value of payments to be made for the lease term.

# Lease Liability Measurement (continued)

- Amounts that are probable of being required to be paid by a lessee under residual value guarantees (Paragraph 21d) may not be measurable at the beginning of the lease.
  - Residual value guarantee includes property tax adjustment which is not known at beginning of the lease (not until the lessor provides the tax bill).
  - Property tax adjustment may go up or down, and is paid as lump sum based on % of occupancy.
  - Note: Future Minimum Lease Payments do not include lump sum payments.



# Lease Liability Measurement (continued)

- Penalties (21f in ED) for terminating the lease should be considered in remeasurement of the liability when considering terminating the lease and not in the initial liability calculation.
- Penalties are usually the unamortized (or unpaid) balance of leasehold improvement. This balance is different depending on when the lease is canceled during the noncancelable period.
- The unamortized balance cannot be determined at the beginning of the lease as agencies do not determine when and if to cancel at this point.
- Penalties can be waived at beginning of lease or negotiated at time of termination (such as when the new lessee can make use of the leasehold improvement).

# Lease Liability Measurement (continued)

- **NEW Comment:** The proposed lease liability measurement may result in the recording of both a **funded liability** and an **unfunded liability**. Tracking both liabilities will increase reporting burden for agencies.
  - 31 U.S.C. SS 1501 a (1), the recording statute, requires the recording of an obligation the amount representing the **legally binding** obligation of the U.S. Government.
  - Also per OMB Circular A-11 Appendix A Scorekeeping Guidelines: For operating leases, budget authority will be scored against the legislation in the year in which the budget authority is first made available in the amount necessary to cover the Government's **legal** obligations.
  - The recording of the lease obligation in the financial system would create a **funded liability**.
  - The amount calculated for lease obligation does not include some “probable” amounts described in the leases ED as those may not be legally binding at the beginning of the lease.
  - The difference between the funded liability and liability calculated under the proposed standard would be recorded as an **unfunded liability** at the beginning of the lease.
  - As funds are obligated in subsequent periods, the funded liability will be created and the unfunded liability will be adjusted accordingly.

# Lease Liability Measurement (continued)

- Specifically, there are two types of non-intragovernmental leases:
  - For leases executed under **GSA delegated authorities** (Direct Leases), the annual rent payments are required to be obligated at the beginning of the fiscal year. For these leases the amount of the funded liability (at the beginning of the lease is the sum of the rent payments for year 1, and the unfunded liability would be the total rent payments for the rest of the noncancelable period through the probable cancelable periods and probable option periods. At subsequent periods the unfunded liability would be reclassified as funded when funds are obligated.
  - For leases executed under the **Independent Statutory Authority**, the **full** amount of the contractual liability is required to be obligated (funded liability) against the funds available at the time the contract was executed. Any “probable” costs that are not legally binding would be recorded as an unfunded liability, and the unfunded liability would be reclassified to funded when funds are obligated.
  - The reclassification of unfunded to funded liability would increase reporting burden to agencies.

# Future Lease Payments

- The future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the lessee's incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used.

# Future Lease Payments (continued)

- Obtaining the rate the lessor charges the lessee may be difficult (although the Contracting Officer should have the information);
- The discount rate may not be accurate account for escalating the rents as in most cases only operating expenses are escalated and it's based on CPI rate;
- Unable to determine the incremental borrowing rate for Government lessees (Resolved as footnote 9 addresses this);
- The benefit of discounting the lease and reporting the interest expense may not justify the burden for tracking each lease and adjusting for monthly reporting.

# Lease Liability Remeasurement

- Liability remeasurement may cause undue burden.
  - This is in addition to the monthly liability adjustment for rent payment made.

# Lease Asset Measurement

- A lessee should measure the lease asset initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service.

# Lease Asset Measurement

- The asset should be recorded at the amount equal to the liability only and not include other costs, as the benefit of recording other costs as an asset and then amortize may outweigh the benefits. The difference in asset and liability would impact the net position when there is no real gain or loss involved.



# DOI Position on Proposed Standard

- The majority of DOI's space needs are met through GSA Occupancy Agreements, which are not required to record an asset and a liability under the proposed standard.
- The majority of DOI's direct leases that may meet the reporting requirements are categorical and special purpose leases e.g., airport hangars, boat ramps, storage units, etc. These leasing activities are both qualitative and quantitatively immaterial to DOI's mission.
- Although the proposed need not be applied to immaterial items, analysis is still needed at the lease level to support not recording a right-to-use lease asset and a liability.
- System change may be needed to capture the information required in the proposed standard, increasing costs.
- Considering the budget constraint, the burden of the reporting requirements outweighs the benefits.
- The existing Future Minimum Lease Payment disclosure, in conjunction with the lease obligation and funded liability recording, provides sufficient information to stakeholders.

## **Department of Defense**

### **Alaleh Jenkins**

#### **Assistant Deputy Chief Financial Officer, Office of the Under Secretary of Defense (Comptroller)**

Mrs. Jenkins is the Assistant Deputy Chief Financial Officer (ADCFO) within the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)). She provides direct support to the Deputy Chief Financial Officer on developing and interpreting Department of Defense accounting and finance policy, promoting standard financial management processes and systems, as well as ensuring an enterprise wide audit strategy is properly implemented. Prior to becoming the ADCFO, she served as the Director for Financial Improvement and Audit Readiness (FIAR) within the OUSD(C). In this position, she was responsible for advising the Deputy Chief Financial Officer on all issues related to financial management reform and audit readiness. Mrs. Jenkins was responsible for the implementation and oversight of financial improvement plans across the DoD. She is a Certified Public Accountant and has more than twenty years of experience in federal and private-sector financial statement audit, business transformation, and large scale and complex financial management engagements.

### **Edwin H. Oshiba**

#### **Deputy Director, U.S. Air Force**

Mr. Oshiba is the Deputy Director of Civil Engineers, Deputy Chief of Staff for Logistics, Engineering and Force Protection, Headquarters U.S. Air Force, Washington, D.C. He is responsible for supporting the Director of Civil Engineers by providing executive leadership, direction and technical knowledge for installation support functions at a total of 182 Air Force bases worldwide with an annual budget over \$11 billion. He is also responsible for organizing, training and equipping the 51,000-person engineering force along with providing policy and oversight for the planning, development, construction, maintenance, utilities and environmental quality of Air Force bases worldwide valued at more than \$297 billion. This responsibility includes housing, fire protection, aircraft crash and rescue, explosive ordnance disposal and emergency management services. He commanded three civil engineer squadrons and an expeditionary Prime Base Engineer Emergency Force group and served in a variety of positions at garrison, major command, and Headquarters U.S. Air Force levels.

### **Melvin Randolph**

#### **Director, U.S. Naval Facilities Engineering Command (NAVFAC)**

Mr. Randolph has recently been named as the new Real Estate Director for the Naval Facilities Engineering Command. He holds multiple degrees including a MBA in Finance and a BA in Real Estate. Prior to his current position, Mr. Randolph was the Branch Chief of the West Coast Portfolio Management Valuations Division. In this role, he performed a comprehensive evaluation of the organization's methodologies and procedures to identify areas for improvement. He ensured compliance with the Uniform Standards for Federal Land Acquisition, resulting in a measurable increase in the productivity of the Division. In 2008, he joined the U.S. GSA as the Acting Chief Appraiser of the Portfolio Management Division, directing the entire Southeast Sunbelt Region. In this role, he performed in-depth appraisals of a large portfolio of multiple and varied real estate holdings, ensuring the best-use scenarios for each property.

**Michael E. Walsh****Finance and Accounting Officer, U.S. Army Corps of Engineers (USACE)**

Mr. Walsh joined the Federal Government in 1991. He received a bachelor's degree in accounting from the University of Scranton and later received a Masters in Business from Syracuse University via the Army Comptrollership Program. In addition, Mr. Walsh is a Certified Public Accountant. Mr. Walsh began his Federal career with the Army Audit Agency in which he progressed from staff auditor to auditor in charge. The majority of his audit background was related to CFO Act audits, which has provided a very sound working knowledge of all applicable accounting policies from GAAP standards down. In June 2000 he joined the Corps of Engineers in the Finance and Accounting Policy Division of the Resource Management Directorate. As the HQUSACE Finance and Accounting Officer, his major duties include oversight on the CFO Financial Statement Audits and providing sound accounting policy to all Corps field activities.

**Steven M Hurwitz****Special Assistant to the Director, Defense Logistics Agency (DLA)**

Mr. Hurwitz began his DLA career as a Staff Accountant in the DLA Directorate of Financial Operations in 2005. From 2005 to present, he has held various and progressively more responsible positions in the DLA Financial Operations Directorate. From 2002-2005, Mr. Hurwitz worked in public accounting performing CFO Act Audits and providing Accounting/Auditing support to the Federal Government. Mr. Hurwitz received his B.S. in Accounting and B.S in Business (Finance) degrees from the University of Delaware. He holds the Certified Government Financial Management certification and completed the CFO Leadership Academy program at the National Defense University. DLA provides the Army, Navy, Air Force, Marine Corps and other federal agencies with a variety of logistics, acquisition and technical services in peace and war. These services include logistics information, materiel management, procurement, warehousing and distribution of spare parts, food, clothing, medical supplies and fuel, reutilization of surplus military materiel, and document automation and production.



Office of the Under Secretary of Defense (Comptroller)  
Office of the Deputy Chief Financial Officer



# *Impact of the Proposed Lease Standard on Department of Defense*

Alaleh Jenkins

Assistant Deputy Chief Financial Officer

April 26, 2017

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# Issue 1: Definition of a Lease



## The Exposure Draft (ED) definition is too broad and all-encompassing

- DoD enters into agreements that are *vast* in quantity and variety
  - Examples: air space corridors, infeasible rights of use, charters, utility easements, soil sample rights of way
  - Most agreements are individually negotiated and will require individual review
- No specific guidance for how to distinguish a service contract from a lease



## Risk

- Lack of precision in definition will lead to inconsistent interpretations and implementation
- Impedes auditability within prescribed timeline
- Wait for TR/implementation guide will produce long period of indecision

# Issue 2: Asset/Liability Criteria



## Recording an Asset

- “Right to use” should be replaced with “control”
- What constitutes “Control” should be defined in the context of a lease. Should include rights substantially similar to owning an asset.
  - Examples: the right to sublet, use the asset for alternative purposes, and alter the asset during the agreement period without permission

## Recording a Liability

- The ED requires recording a liability for an event that has not yet occurred
  - Generally a liability is not recorded until the asset or service has been received
  - DoD’s agreements allow it to unilaterally terminate an agreement. This happens due to funding constraints and mission changes
  - Future liabilities can be disclosed in a footnote
- Different accounting than a similar transaction for acquiring services, or a commitment to acquire 1,000 widgets over the next 5 years

## Risk

- Current criteria will distort DoD’s financial position
- Requires treatment that conflicts with existing standards



# Issue 3: Benefits and Costs to Taxpayers

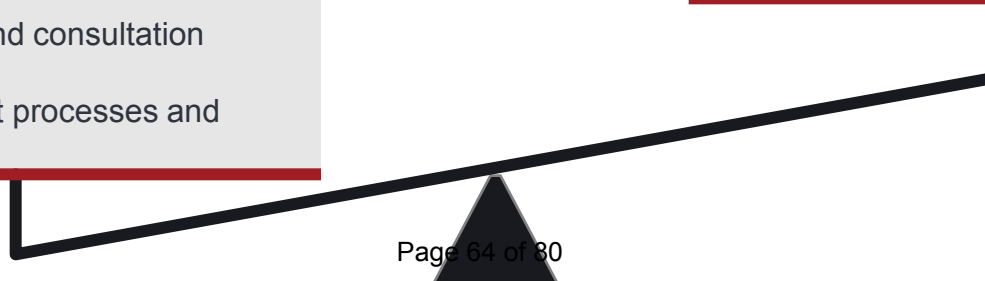


## Cost Outweighs the Benefit

- The ED provides little useful information to management, taxpayers, or congress
  - Taxpayers can obtain an understanding of DoD's obligations through its budget exhibits
- DoD's agreements can often be cancelled at zero or low cost, reducing any benefit of reporting future lease/rental payments

| Costs   |
|---|
| <ul style="list-style-type: none"><li>• Existence and completeness of identified leases</li><li>• Reviews of all agreements</li><li>• ID lease payments</li><li>• Unbundling lease and service costs</li><li>• Calculation and recording of lease assets and liabilities</li><li>• Estimating the rate implicit in the lease</li><li>• Legal reviews and consultation</li><li>• Training</li><li>• Updating current processes and systems</li></ul> |

| Benefits   |
|--|
| <p>Provide financial information for federal financial statement users</p> |



# Issue 4: Effective Date



**The ED effective date does not provide enough time to prepare systems and allow preparers to identify all agreements**

- A more realistic timeframe is 4 years
- Recommend prospective implementation versus retrospective

## **Risks**

- Major resource distraction in drive towards auditability



## Additional Recommendations:

- Limit to tangible assets
- Exclude all intangibles such as easements, land rights, air rights, water rights, software licenses, etc.
- Must be for a specific identified item of Property, Plant, and Equipment with no right of substitution
  - Define “identified item” and “right of substitution”
- Agreement must convey the right to control and to operate an asset in a manner determined by the lessee
- Exclude service arrangements and expand service definition
- The lessee has the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use
  - Examples: the right retain revenue, right to sublet, use the asset for alternative purposes, and alter the asset during the agreement period without permission

## **General Services Administration**

### **Robert Smalskas**

Robert Smalskas is the current Division Director of Accounting and Financial Reporting for GSA. He has been with GSA for 1 1/2 years, and has been with the U.S. Government for 8 years. His previous experience with the federal government has been with DoD (DLA, U.S. Air Force and the Department of Navy) primarily working on audit readiness activities. Prior to the federal government, he has worked in general accounting and financial reporting capacities for large and medium sized corporations. He has managed the real estate accounting activities of a large retailer, and provided financial support to a global facilities organization of a large automotive components corporation. He is a CPA and is working towards his CFE certification.



U.S. General Services Administration

# FASAB Leasing ED - Analysis & Discussion on Impact to GSA

April 26, 2017

GSA Office of the Chief Financial Officer



# Presentation Contents

## 1. Issues

- a. Stakeholder Benefits? (Cost v. Benefit considerations)
- b. Control (Concepts terminology) v. Right-to-Use (ED terminology) over Assets
- c. Lease Definition (too broad)
- d. Effective Date

## 2. Analysis and Discussion

## 3. Concluding Remarks





## **a. Stakeholder Benefits**

- The proposed Leasing ED would not provide information that is actionable, or information from which better business decisions could be made.
- Costs to implement and sustain the requirements of the Leasing ED would far exceed any incremental benefits realized from the implementation of this ED.
- GSA received no inquiries or notices that our current lease reporting is deficient...and further believes that our current reporting (through footnote disclosure) is sufficient.





# Issues (continued)

## a. Control v. Right-to-Use over Assets

- Control and ownership should be considered when recording assets, and related liabilities. A lessee (right-to-use) does not receive all the rights and benefits of asset ownership...for example, in some cases structural changes to a building that is leased requires lessor approval. As a lessee your “rights” to the property are abridged...to include duration.
- SFFAC 5 defines as an asset that is “controlled”, whereas the ED defines an asset where the federal entity has a “right-to-use”. The SFFAC and the ED seem to be using contradictory terms around the same concepts...which can and will lead to some confusing if the language is not cleaned up or clarified.
- *It seems that “control” is an essential element of the SFFAC 5 definition of an asset. Without “control”, the underlying item referenced in a lease should not be considered an asset and should not be recorded as such.*



# Issues (continued)

## a. Lease Definition

- The ED definition of a lease is too broad.
  - “... a lease as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.”
- Under this definition...GSA would be capitalizing AND depreciating land as a consequence of ground leases.
- *GSA suggests that FASAB consider a narrower “lease” definition, and any refined definition should speak to SCAs and service agreements...rather than remaining silent.*



# Issues (continued)

## a. **Effective Date is too soon for successful implementation**

- More time and resources would be needed to ensure a successful transition and implementation (system changes, system testing, data validation, personnel training, risk assessment, lease documentation reviews, et al).
- *GSA suggests a more realistic timetable to ensure a successful transition (NLT 2022).*



# Analysis and Discussion

- **Implementation of the ED would have a significant impact on our Balance Sheet, and throughout GSA**
  - > ~\$20B increase in asset value (and related lease liabilities)
  - 7,000+ leases to be reviewed, and would be subject to the provisions of the ED
  - Significant costs (around system changes/enhancements, data validation, lease reviews/data scrubbing, interface testing, personnel training, risk assessments, audit compliance, et al) would be incurred to implement the ED
  - Costs to implement/sustain would far outstrip any perceived or known benefits
  - Additional discovery may be necessary to validate our population of leasing activity (personal and real property)



# Concluding Remarks

- No significant benefit to GSA or any other stakeholder has been identified related to this ED (no financial analysts are analyzing our financials for possible investment)
- Significant costs to implement and sustain (which outstrip any identified benefits)
- No actionable information will be provided to any stakeholders that can or could inform any decision making activities as a consequence of adopting this ED
- There are incongruencies between FASAB Concepts and the Leasing ED, specifically around the concept of asset “control” and “right-of-use” referenced in the ED...”control” appears to be an essential element to the definition of an asset, yet “right-of-use” is an abridgement of rights identified within a lease...these terms appear to be incongruent

## Leases ED Clarification Discussion – General Agency Questions

1. Is your agency able to separately identify future lease commitments for which obligations have been made versus those which require future appropriations?
2. Do you believe the current lease reporting requirements in Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of The Federal Government*, and SFFAS 6, *Accounting for Property, Plant, and Equipment*, should be revised and, if so, how? Would your suggested change in the current lease reporting requirements increase your agency's reporting burden and, if so, how and to what extent? Do you believe the benefits of the increased burden would prove useful to the readers of your financial statements and, if so, why?
3. How would the proposed requirements in the *Leases* exposure draft (ED) increase your agency's reporting burden? How much of the increased burden do you believe would be worthwhile? If you believe the increased burden would not be beneficial, how would you change the ED to minimize the increase in the reporting burden?
4. What are your agency's expectations as to the cost and/or difficulty of implementing the proposed standards? Specifically, what issues have you identified that the Board should explore further or revisit?
5. Should the scope of the *Leases* proposal be more narrowly defined? If so, what items should be excluded and why?

6. Is the proposed definition of a lease clear? Can you effectively apply the proposed definition? Do you believe it would be helpful to include how “control” relates to the right to use a leased asset, meaning “the right to control the use of a leased asset”, to the proposed definition? Are there any other proposed definitions in the ED (for example, intragovernmental lease, lease option periods, initial direct costs, or short-term leases) or other critical terms that you believe are not adequately defined?
7. Do you believe assessing whether it is probable (that is, more likely than not) that the agency will exercise a lease option would be burdensome to your agency and, if so, why?
8. What are your thoughts on using the lessor’s implicit interest rate to calculate the lease liability? What are your thoughts on using the lessor implicit rate versus the lessee incremental borrowing rate to calculate the lease liability? What difficulties does your agency expect in calculating the lease liability and lease asset?
9. Do you believe the proposed remeasurement requirements are burdensome? If so, how would you change those requirements?
10. Should the maximum lease term for short-term leases differ from the proposed 24 months? If so, what maximum lease term would you suggest for short-term leases? What would be your justification for the greater or lesser lease term other than recording fewer or more leases?
11. What type of implementation guidance would be most helpful to your agency to effectively and efficiently apply the proposed Leases standards? For example, would flow charts, decision trees, illustrations, examples, etc., be helpful?



12. Approximately how many non-intragovernmental lease contracts/agreements does your agency currently have? What portion of those leases qualifies as capital leases now?
13. What benefit do you see in reporting the long-term obligation and related interest expense associated with your agency's non-intragovernmental leases?
14. What value do you see in requiring federal entities to disclose in their financial report the terms of any lease-related cancellation penalties? Would that information be difficult to gather for disclosure?

## Leases ED Clarification Discussion – Specific Agency Questions

### USDA

In reference to your response to ED Q1, can you further explain to the Board the types of contracts or agreements that you are uncertain would meet the proposed definition of a lease?

In reference to your response to ED Q4, how do the average noncancelable periods of your non-intragovernmental leases compare to the actual lease terms of those leases?

### ENERGY

In reference to your response to ED Q5, what other options would you suggest be used by the lessee to measure the future lease payments?

In reference to your response to ED Q6, are the liability remeasurement triggers in paragraph 25 common to your agency's leases?

### INTERIOR

In reference to your response to ED Q1, can you elaborate on your easements, land rights, licenses, and concession agreements? How are these agreements currently recognized? Do you believe they would be included or excluded from the scope of the proposal based on the current proposed lease definition?

In reference to your response to ED Q2, can you elaborate on what you refer to as a “firm term” versus a “lease term”?

## DOD

In reference to your response to ED Q1, can you elaborate on your land rights, rights of way, easements, air rights, mineral rights, and indefeasible rights of use? How are these agreements currently recognized? Do you believe they would be included or excluded from the scope of the proposal based on the current proposed lease definition?

In reference to your response to ED Q2, do you believe lease transactions are more analogous to entitlements as opposed to the purchase of goods or services?

## GSA

In reference to your response to ED Q2, is it typical for GSA not to include renewal options in its non-intragovernmental leases, but instead wait until a few months prior to the existing lease's expiration to extend the lease for an additional period of time?

In reference to your response to ED Q2, is it normal practice for GSA not to include "fiscal funding clauses" in its non-intragovernmental lease agreements? If not, is a similar appropriation-related clause included in those contracts/agreements?

**Comment Letters of Presenter Agencies**

*(Listed in order of appearance at the April 26, 2017 Leases ED Clarification Discussion)*

|   |           |
|---|-----------|
| <b>Department of Agriculture .....</b>      | <b>1</b>  |
| <b>Department of Energy.....</b>            | <b>9</b>  |
| <b>Department of the Interior .....</b>     | <b>16</b> |
| <b>Department of Defense.....</b>           | <b>28</b> |
| <b>General Services Administration.....</b> | <b>40</b> |

**FASAB Exposure Draft: Questions for Respondents due January 6, 2017**

***Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment***

**Please select the type(s) of organization responding to this exposure draft. If you are not responding on behalf of an organization, please select "individual."**

|                                   |                                     |  |
|-----------------------------------|-------------------------------------|--|
| Accounting Firm                   | <input type="checkbox"/>            |  |
| Federal Entity (user)             | <input type="checkbox"/>            |  |
| Federal Entity (preparer)         | <input checked="" type="checkbox"/> |  |
| Federal Entity (auditor)          | <input type="checkbox"/>            |  |
| Federal Entity (other)            | <input type="checkbox"/>            | If other, please specify: <input type="text"/> |
| Association/Industry Organization | <input type="checkbox"/>            |  |
| Nonprofit organization/Foundation | <input type="checkbox"/>            |  |
| Other                             | <input type="checkbox"/>            | If other, please specify: <input type="text"/> |
| Individual                        | <input type="checkbox"/>            |  |

**Please provide your name.**

Name:

**Please identify your organization, if applicable.**

Organization:

**Q1.** The Board is proposing to define a **lease** as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. The current lease standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, do not specifically define a lease. SFFAS 5 and SFFAS 6 only define a capital lease as a "lease that transfers substantially all the benefits and risks of ownership to the lessee." The Board believes that the more concise definition being proposed is broad enough to capture the diversity of federal leasing activities. The proposed lease definition is presented in paragraph 9 and further explained in paragraph A15.

**Do you agree or disagree with the proposed definition of lease presented in paragraph 9 and further explained in paragraph A15? Please provide the rationale for your answer.**

I believe that the definition is a bit broad and generic, and needs to be enhanced. In our organization we have various groups and staffs that participate in the leasing activities; leasing and contracting officers, property staff and the accounting team, and we all have to be on the same page. Possibly providing examples of the types of contracts and agreements in the appendix would be helpful. I thought that the

**FASAB Exposure Draft: Questions for Respondents due January 6, 2017**

*Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment*

issuance of Technical Release 16: Implementation Guidance for Internal Use Software, was nicely done, and provided us with information and examples that we could share with our Information Technology (IT) staff to get them on point so we could better communicate. I think we need to do something similar, in terms of spelling out we are interested in, with this lease pronouncement.

- Q2.** The Board is proposing that the **lease term** be determined as the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period) plus each option period if it is probable, based on all relevant factors, that the lessee will exercise that option to extend the lease. The lease term proposal also provides guidance on the noncancelable period and on how specific provisions (such as fiscal funding/cancellation clauses and month-to-month lease holdovers) should be applied. The proposed lease term requirements are presented in paragraphs 14 – 18 and further explained in paragraphs A16 – A18.

**Do you agree or disagree with the proposed guidance on determining the lease term as presented in paragraphs 14 - 18 and further explained in A16 – A18? Please provide the rationale for your answer.**

I understand the rationale for the proposed guidance for determining the lease term. I like the use of “probable”, per paragraph A18, when evaluating the lease renewal options that are five or ten years out. It is a challenge for the Real Property Leasing Officer (RPLO), Contracting Officer and/or the accountant to readily determine whether an individual lease will be renewed because the actual tenant/user (State / Program representative) needs to provide input as to whether the property meets his/her needs when determining whether to renew or terminate the lease when approaching the effective renewal date. During my 5+ years of working with real property leases, our agency has opted to renew a higher percentage of leases than it terminates. So the rule of thumb, and the more conservative approach, has been to include the option renewal period(s) as stated in the lease agreement when performing our lease determination analysis (operating or capital lease).

- Q3.** The Board is proposing that at the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases. The proposed lease recognition requirements are presented in paragraph 19.

**FASAB Exposure Draft: Questions for Respondents due January 6, 2017**

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**Do you agree or disagree with the proposed lessee recognition of a lease at the beginning of the lease term as presented in paragraph 19? Please provide the rationale for your answer.**

I disagree with the proposal that leases with non-federal entities should be recognized as capital leases because I do not believe that this treatment provides more meaningful and relevant data for federal financial statement users, i.e., the general public.

A summary of the agency's future lease payments is prepared and provided in the notes to the financial statements. The effort and cost to provide the existing summary info is far less than it would be compared to running our lease transactions through the accounting and inventory systems in an effort to report these non-federal leases as capital leases.

Secondly, our agency has approximately 600 leases for office space with non-federal entities, and I am fairly certain that our agency and our parent agency do not have statutory or budget authority to freely purchase any of these buildings. Given that the agency mission is totally unrelated to property and/or property leases, Lease Expense and not Property Plant and Equipment is the correct functional description. Attempting to treat the lease transactions as a financing for a potential purchase, and to account for the payments (NPV) as "government assets" instead of as operating expenses does not make the financial presentation "more meaningful" for the general public. Per paragraph A26, the goal should be to take a 'simplified approach for leases which would be pragmatic and cost efficient'.

For agencies where property is a significant and material part of their activities, such as GSA, then maybe it makes sense to capitalize the non-federal leases. But for other agencies where property leases are a tool needed to perform tasks for the mission, the accounting should be simple and cost efficient as previously stated. The agencies can continue to use their money for their mission and programs, and not have to spend it to enhance accounting and inventory systems, and to hire accountants.



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Thirdly, most if not all leases have a short period (2 to 4 months) where the lessee can terminate the lease. I believe the best presentation remains as an ongoing operating cost and not a capital cost. To have an asset and liability based on 10 to 20 years worth of rent payments is not an accurate presentation at lease inception because the lessee can terminate the lease within the first year.

I feel that the current disclosures in the notes to the financial statements for leases (future payments) provide a good overview for the readers of the financial statements, without having to run the lease-level asset and liability transactions through the general ledger.

- Q4.** The Board is proposing that a lessee should measure the **lease liability** initially at the present value of payments to be made for the lease term. In addition, the measurement of the lease liability should include the several types of payments that might be required by a lease. The proposed lease liability measurement and recognition requirements are presented in paragraphs 21– 29 and further explained in paragraphs A20 – A21.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease liability as presented in paragraphs 21 - 29 and further explained in paragraphs A20 – A21? Please provide the rationale for your answer.**

Valuing the lease liability at the Net Present Value (NPV) of the cash flows for the duration of the lease term potentially overstates the debt for an agreement that can be terminated when the shorter noncancelable period has expired. This requirement is also inconsistent with valuing the asset at the lesser of fair market value (FMV) or NPV.

Another unaddressed question is whether the agency will need to establish an obligation (budgetary resources) to cover the lease liability at lease inception. Some or most agencies will need to have access to additional “no year funding” as the duration of the funding is supposed to match or exceed the lease period.

- Q5.** The Board is proposing that the future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the lessee’s incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used. The specific proposed requirement is presented in paragraph 23.

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- a. Do you agree or disagree that the rate the lessor charges the lessee, which may be the interest rate implicit in the lease, should be used to measure the future lease payments as presented in paragraph 23? Please provide the rationale for your answers.
- b. Do you agree or disagree that the lessee's incremental borrowing rate should be used to measure the future lease payments when the lessor rate cannot be reasonably estimated by the lessee as presented in paragraph 23? Please provide the rationale for your answers.

I agree that either the implied rate or the published Treasury rate should be used.

**Q6.** The Board is proposing that the lessee should remeasure the lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability. The Board is also proposing that the lease asset should generally be adjusted by the same amount when the corresponding lease liability is remeasured based on those changes. Additionally, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain. The proposed lessee requirements for remeasurement are presented in paragraphs 25 – 29, 33, and further explained in paragraph A19.

- a. Do you agree or disagree with the circumstances when the lessee must remeasure the lease liability as presented in paragraph 25? Please provide the rationale for your answer.

The circumstances requiring re-measurement appear reasonable.

- b. Would the requirements triggering remeasurement cause undue costs? Please provide the rationale for your answer.

Based on the info provided, I cannot determine whether there would be undue costs for the re-measurement processes. However, I believe that there will be undue costs for the agencies to enhance their accounting systems and lease inventory systems in order to account for all non-federal leases as capital leases, and to add staff to the accounting teams.

- c. Do you agree or disagree with the effect of the remeasurement on the carrying value of the lease asset as presented in paragraph 33 and further explained in paragraph A19? Please provide the rationale for your answer.

Generally the re-measurement of an intangible property asset is achieved through: (1) systemic amortization based on the expected / estimated life of the asset; and (2) adjustments for changes to the

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residual value, changes to the annual rental cost, etc. The amortization and adjustment amounts provide an audit trail from the historical cost to the current valuation (net book value). I am not convinced that the re-pricing of the liability should drive the asset balance.

- Q7.** The Board is proposing that a lessee should measure the lease asset initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service. The proposed lessee lease asset measurement and recognition requirements are presented in paragraphs 30 – 34 and further explained in paragraph A22.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease asset as presented in paragraphs 30 - 34 and further explained in paragraph A22? Please provide the rationale for your answer.**

I disagree as I see the cost of a lease as a period cost, and not an asset; i.e., pay as you go. Accounting for the leases with non-federal entities as an asset overly complicates a fairly simple transaction. I do not believe this approach is meaningful for anyone other than accountants.

The original valuation for capitalized leased property was the lesser of the NPV or FMV. It appears that this concept has been thrown out the window in favor of the calculated lease liability amount.

- Q8.** The Board is proposing that at the beginning of the lease term, a lessor should recognize a lease receivable and deferred revenue, except for intragovernmental and short-term leases. The proposed requirements for the measurement and recognition of the lessor lease receivable and deferred revenue are presented in paragraphs 36 – 48 and further explained in paragraphs A23 - A24.

**Do you agree or disagree with the proposed lessor measurement and recognition of the lease receivable and deferred revenue as presented in paragraphs 36 - 48 and further explained in paragraphs A23 - A24? Please provide the rationale for your answer.**

I disagree based on the similar reasons stated in Q3.

- Q9.** The Board is proposing to define a short-term lease as a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. The

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proposed requirements for the measurement and recognition of a short-term lease are presented in paragraphs 59 – 61 and further explained in paragraph A25.

**Do you agree or disagree with the proposed definition and measurement and recognition of a short-term lease as presented in paragraphs 59 - 61 and further explained in paragraph A25? Please provide the rationale for your answer.**

Our agency capitalizes assets that meet a certain dollar threshold that have a useful life of 2 or more years. So I am fine with short term defined as 24 months or less.

- Q10.** The Board is proposing to establish distinct standards for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, Reporting Entity. The proposed requirements for the measurement, recognition, and disclosure of intragovernmental leases are presented in paragraphs 75 – 95 and further explained in paragraphs A26 - A29.

**Do you agree or disagree with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases as presented in paragraphs 75 - 95 and further explained in paragraphs A26 - A29? Please provide the rationale for your answer.**

I concur with most of the info for the intragovernmental leases, which is to treat the rents as operating expenses for the current period. The exception is the proposed treatment of lease incentives and concessions as reductions to expense (for lessee) and income (lessor) over the lease term. I am not aware that our agency receives or gives any incentives or concessions, but if so, I believe that they are immaterial to the total dollars spent for rents, and to the financial statements as a whole.

- Q11.** The Board is proposing that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. The proposed implementation requirements are presented in paragraphs 99 -100.

**Do you agree or disagree with the proposed prospective implementation approach as presented in paragraphs 99 - 100? Please provide the rationale for your answer.**

I cannot offer an opinion at this time as I have some unanswered questions; specifically, (1) will the liability for the leases with non-federal entities need to be funded (obligated); (2) do we undo the

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existing accounting that is currently done for the existing capital leases that have been recorded; and (3) would the unused funds from the existing capital leases be available to use to fund the liability in the new world of lease accounting.

- Q12.** The Board is proposing that the requirements of this Statement be effective for reporting periods beginning after September 30, 2018. The proposed effective date is presented in paragraph 101.

**Do you agree or disagree with the proposed effective date as presented in paragraph 101? Please provide the rationale for your answer.**

The federal agencies have used SFFAS 5 and 6, and FASB 13 for any years so I think there is some flexibility with the implementation of any successor accounting pronouncements for leases.


If this exposure draft is implemented as is, which I am not in favor of, I am not in a position to project whether our agency would be ready for the changes to our accounting and lease inventory systems by September 30, 2018.

I would suggest asking the CFOs and IT teams for their thoughts and projections for an implementation date.

**Department of Energy**

Washington, DC 20585

January 5, 2017

**MEMORANDUM FOR THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD****FROM:**Tom Park   
Director, Office of Finance and Accounting**SUBJECT:**

Comments on the Federal Accounting Standards Advisory Board's Exposure Draft Leases: *An Amendment of Statement of Federal Financial Accounting Standards (SFFAS) 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment.*

The Department of Energy (Department) appreciates the opportunity to comment on Exposure Draft Leases: *An Amendment of Statement of Federal Financial Accounting Standards (SFFAS) 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment.* Generally, the Department found that many of the proposed changes correlate with the Financial Accounting Standards Board (FASB) and other accounting governing bodies.

Our responses to the questions in the exposure draft are as follows:

**Q1. The Board is proposing to define a lease as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. The current lease standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment, do not specifically define a lease. SFFAS 5 and SFFAS 6 only define a capital lease as a "lease that transfers substantially all the benefits and risks of ownership to the lessee." The Board believes that the more concise definition being proposed is broad enough to capture the diversity of federal leasing activities. The proposed lease definition is presented in paragraph 9 and further explained in paragraph A15.**

**Do you agree or disagree with the proposed definition of lease presented in paragraph 9 and further explained in paragraph A15? Please provide the rationale for your answer.**

Generally, the Department agrees with the Board's definition of a lease.

**Q2. The Board is proposing that the lease term be determined as the period during which a lessee has a non-cancelable right to use an underlying asset (referred to as the non-cancelable period) plus each option period if it is probable, based on all relevant factors, that the lessee will exercise that option to extend the lease. The lease term proposal also provides guidance on the non-cancelable period and on how specific**

provisions (such as fiscal funding/cancellation clauses and month-to-month lease holdovers) should be applied. The proposed lease term requirements are presented in paragraphs 14 – 18 and further explained in paragraphs A16 - A18.

**Do you agree or disagree with the proposed guidance on determining the lease term as presented in paragraphs 14 - 18 and further explained in A16 - A18? Please provide the rationale for your answer.**

The Department agrees with the Board's proposed determination of a lease term.

**Q3. The Board is proposing that at the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases. The proposed lease recognition requirements are presented in paragraph 19.**

**Do you agree or disagree with the proposed lessee recognition of a lease at the beginning of the lease term as presented in paragraph 19? Please provide the rationale for your answer.**

The Department agrees with the proposed guidance for lease recognition. The guidance complements OMB Circular A-11 Appendix B scoring rules on leases. We would just request that any new standard be implemented in conjunction with the roll out of new SGL accounts and guidance on the transaction/posting models.

**Q4. The Board is proposing that a lessee should measure the lease liability initially at the present value of payments to be made for the lease term. In addition, the measurement of the lease liability should include the several types of payments that might be required by a lease. The proposed lease liability measurement and recognition requirements are presented in paragraphs 21 – 29 and further explained in paragraphs A20 - A21.**

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease liability as presented in paragraphs 21 - 29 and further explained in paragraphs A20 - A21? Please provide the rationale for your answer.**

The Department partially agrees with the proposed lessee measurement and recognition of lease liability presented paragraphs 21 - 29. We think an additional "required" lease payment type should be added in addition to the outlined criteria listed under paragraph 21 a-g as follows:

“Payments required to be made by the lessee under non-routine or unique circumstances (such as triple net leasing arrangements).”

**Q5. The Board is proposing that the future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the lessee's incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used. The specific proposed requirement is presented in paragraph 23.**



**a. Do you agree or disagree that the rate the lessor charges the lessee, which may be the interest rate implicit in the lease, should be used to measure the future lease payments as presented in paragraph 23? Please provide the rationale for your answers.**

The Department agrees the rate the lessor charges the lessee should be used to measure future lease payments.

**b. Do you agree or disagree that the lessee's incremental borrowing rate should be used to measure the future lease payments when the lessor rate cannot be reasonably estimated by the lessee as presented in paragraph 23? Please provide the rationale for your answers.**

The Department agrees with the proposed guidance for discounting lease payments and the lessee's use of its incremental borrowing rates when the lessor's borrowing rate cannot be readily estimated. However, we would like for FASAB to consider providing guidance on situations in which the lessor's incremental borrowing rate cannot be reasonably estimated, and the lessee's borrowing rate on the lease is less than Treasury's borrowing rate for securities of similar maturity to the term of the lease.

**Q6. The Board is proposing that the lessee should re-measure the lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability. The Board is also proposing that the lease asset should generally be adjusted by the same amount when the corresponding lease liability is re-measured based on those changes. Additionally, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain. The proposed lessee requirements for re-measurement are presented in paragraphs 25 – 29, 33, and further explained in paragraph A19.**

**a. Do you agree or disagree with the circumstances when the lessee must re-measure the lease liability as presented in paragraph 25? Please provide the rationale for your answer.**

The Department partially agrees with the circumstances provided in which the lessee must re-measure the lease liability. We would like to know how FASAB is interpreting the distinction between "significantly affect" and "material".

The term "significantly affect", is not defined in the current version of the FASAB Handbook of Federal Accounting Standards (June 2016). Also, we are concerned the term "significantly affect", as it is discussed at paragraph 25, is subject to misinterpretation or misapplication in context with the re-measurement of lease liabilities.

**b. Would the requirements triggering re-measurement cause undue costs? Please provide the rationale for your answer.**

The requirements triggering re-measurement would cause undue costs if the change is not "material" to the agency's financial statements. Also, for agencies that have entered into leases

with "variable" interest rates, the re-measurement process may be burdensome because of the continuous change in interest rates.

**c. Do you agree or disagree with the effect of the re-measurement on the carrying value of the lease asset as presented in paragraph 33 and further explained in paragraph A19? Please provide the rationale for your answer.**

The Department would like for the Board to consider further explaining its position on the effects of re-measurement on the carrying value of the leased assets, as discussed in paragraph 33.

Paragraph 33 states, *"The lease asset generally should be adjusted by the same amount when the corresponding lease liability is re-measured based on paragraphs 25–29. However, if this change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain."*

Specifically, the Department would like for FASAB to address under which circumstances a leased asset can have any "carrying value" left over to be reported as a "gain", if the associated lease liability has been reduced to zero?

**Q7. The Board is proposing that a lessee should measure the lease asset initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service. The proposed lessee lease asset measurement and recognition requirements are presented in paragraphs 30 – 34 and further explained in paragraph A22.**

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease asset as presented in paragraphs 30 - 34 and further explained in paragraph A22? Please provide the rationale for your answer.**

The Department agrees with the proposed lease measurement and recognition of the leased asset.

**Q8. The Board is proposing that at the beginning of the lease term, a lessor should recognize a lease receivable and deferred revenue, except for intragovernmental and short-term leases. The proposed requirements for the measurement and recognition of the lessor lease receivable and deferred revenue are presented in paragraphs 36 – 48 and further explained in paragraphs A23 - A24.**

**Do you agree or disagree with the proposed lessor measurement and recognition of the lease receivable and deferred revenue as presented in paragraphs 36 - 48 and further explained in paragraphs A23 - A24? Please provide the rationale for your answer.**

The Department agrees with the proposed lessor measurement and recognition of the lease receivable and deferred revenue.

**Q9. The Board is proposing to define a short-term lease as a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. The proposed requirements for the measurement and recognition of a short-term lease are presented in paragraphs 59 – 61 and further explained in paragraph A25.**

**Do you agree or disagree with the proposed definition and measurement and recognition of a short-term lease as presented in paragraphs 59 - 61 and further explained in paragraph A25? Please provide the rationale for your answer.**

Generally, the Department agrees with the proposed definition, measurement, and recognition of a short term lease. However, we are concerned there is a possible misinterpretation between paragraphs 14 and 59 on the determination of a lease. We would like for the Board to clarify whether it is the Board's intent for Paragraph 14 to be the final qualifier for defining a lease term.

Paragraph 14 states, *"The lease term is the period during which a lessee has a non-cancelable right to use an underlying asset (referred to as the non-cancelable period), plus each option period if it is **probable**, based on all relevant factors, that the lessee will exercise that option to extend the lease."*

Paragraph 59 states, *"A short-term lease is a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. For a lease that is cancelable by either the lessee or the lessor, such as a month-to-month lease or a year-to-year lease, the maximum possible term is the non-cancelable period, including any notice periods. For a lease that is cancellable only by the lessee, the maximum possible term should be evaluated under the requirements of the lease term as defined in paragraph 14."*

Please consider the following examples:

- 1) The Department enters into a lease contract [as a lessee] that is 16 months with an option period of 9 months. If the Department has the option to cancel the 9 month option period of its lease, then the maximum lease term to be evaluated would be 16 months (the non-cancellable portion of the lease) under paragraphs 14 and 59.
- 2) The Department enters into a lease contract [as a lessee] for 16 months, with the probable exercise of a 9 month lease option period. Based on the Department's interpretation of paragraph 14, this lease contract will not qualify as a short term lease because the lease term is for 25 months. Therefore, this lease will have to be tracked and recorded as a capital lease.

**Q10. The Board is proposing to establish distinct standards for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, Reporting Entity. The proposed requirements for the**

measurement, recognition, and disclosure of intragovernmental leases are presented in paragraphs 75 – 95 and further explained in paragraphs A26 - A29.

**Do you agree or disagree with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases as presented in paragraphs 75 - 95 and further explained in paragraphs A26 - A29? Please provide the rationale for your answer.**

The Department partially agrees with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases.

At Paragraphs 90 and 91, we would like FASAB to clarify why the distinction was made between a "lease incentive" and "lease concession", when both terms as applied to intragovernmental leases, appear to be synonymous?

A "lease incentive" and a "lease concession" is a form of payment given by the lessor to entice the lessee to sign the lease. They both result in reduced rental income received by the lessor and paid by the lessee. Even the basis for conclusions at paragraph A29, which states *"lease incentives and concessions should be recognized by the lessee/lessor as reductions of lease rental expense/lease rental income"*, supports the analogous interpretation of these two terms.

**Q11. The Board is proposing that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. The proposed implementation requirements are presented in paragraphs 99-100.**

**Do you agree or disagree with the proposed prospective implementation approach as presented in paragraphs 99 - 100? Please provide the rationale for your answer.**

The Department agrees with the proposed prospective implementation approach as presented in paragraphs 99 - 100.

**Q12. The Board is proposing that the requirements of this Statement be effective for reporting periods beginning after September 30, 2018. The proposed effective date is presented in paragraph 101.**

**Do you agree or disagree with the proposed effective date as presented in paragraph 101? Please provide the rationale for your answer.**

The Department agrees with the proposed effective date.

Other Matters

Although an update to SFFAS 10 (Accounting for Internal Use Software) is not specifically a topic for discussion under this exposure draft, for future FASAB activities, we thought it may be helpful for us to provide you with our questions pertaining to the treatment of software under the new lease standards.

Question #1: SFFAS 10 already classifies internal use software as PP & E. What other software besides internal use software is expected to be treated as a lease?

Question #2: Is internal use software included as a right-to-use asset? What assets would this definition include—only plant and equipment assets and internal use software? For example, would agreements for “software as a service” (SaAS) or cloud applications or data storage fall under this guidance, or are these items considered services and therefore exempt?

Question #3: Since SaAS applications are not controlled by the lessee in the same manner as a more customized Enterprise Resource Planning (i.e., Oracle) system, does that warrant different accounting treatment?

Question #4: Are annual payments for software licenses considered leases? If yes, are the annual renewals considered short term leases?

Question #5: Can the Board clarify or define “if and when” to include software licenses or maintenance licenses as a “lease” if the license is for a period longer than 2 years? For example:

- One-time perpetual leases with annual maintenance agreements.
- Non-perpetual licenses “lease” software for use for a specified period of time. Users are required to remove the software from their computer if they cease paying for the license fee.
- Some license agreements allow the user to purchase “maintenance” or “software assurance” along with the original license fee, which entitles the user to receive new versions of the software until the maintenance agreement expires.

Question #6: How are umbrella software agreements accounted for?

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**Please select the type(s) of organization responding to this exposure draft. If you are not responding on behalf of an organization, please select "individual."**

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| Accounting Firm                   | <input type="checkbox"/>            |  |
| Federal Entity (user)             | <input type="checkbox"/>            |  |
| Federal Entity (preparer)         | <input checked="" type="checkbox"/> |  |
| Federal Entity (auditor)          | <input type="checkbox"/>            |  |
| Federal Entity (other)            | <input type="checkbox"/>            | If other, please specify: <input type="text"/> |
| Association/Industry Organization | <input type="checkbox"/>            |  |
| Nonprofit organization/Foundation | <input type="checkbox"/>            |  |
| Other                             | <input type="checkbox"/>            | If other, please specify: <input type="text"/> |
| Individual                        | <input type="checkbox"/>            |  |

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Organization:

**Q1.** The Board is proposing to define a **lease** as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. The current lease standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, do not specifically define a lease. SFFAS 5 and SFFAS 6 only define a capital lease as a "lease that transfers substantially all the benefits and risks of ownership to the lessee." The Board believes that the more concise definition being proposed is broad enough to capture the diversity of federal leasing activities. The proposed lease definition is presented in paragraph 9 and further explained in paragraph A15.

**Do you agree or disagree with the proposed definition of lease presented in paragraph 9 and further explained in paragraph A15? Please provide the rationale for your answer.**

**PFM:** Agree. The definition is concise enough to capture federal leasing activities and yet not too restrictive. Specifically, the inclusion of "agreement" in the definition provides flexibility for the inclusion of leasing activities that may not be legally enforceable but have financial impacts on the reporting entity.

**BIO:** Agree. It is left open enough to provide flexibility. If you look in a dictionary, the definition of lease is a contract by which one party conveys land, property, services, etc., to another for a specified time, usually in return for a periodic payment. So, I think the proposed definition provides clarity with flexibility.

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**BOEM/BSEE:** Agree.

**BOR: Disagree.** Suggest clarifying where easements and land rights, licenses, concession agreements, etc. fall under this definition.

**DO:** Agree with the definition.

**IA:** Agree.

**OSM:** Agree. This provides a clearer understanding of what a lease is.

- Q2.** The Board is proposing that the **lease term** be determined as the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period) plus each option period if it is probable, based on all relevant factors, that the lessee will exercise that option to extend the lease. The lease term proposal also provides guidance on the noncancelable period and on how specific provisions (such as fiscal funding/cancellation clauses and month-to-month lease holdovers) should be applied. The proposed lease term requirements are presented in paragraphs 14 – 18 and further explained in paragraphs A16 – A18.

**Do you agree or disagree with the proposed guidance on determining the lease term as presented in paragraphs 14 - 18 and further explained in A16 – A18? Please provide the rationale for your answer.**

**PFM:** Disagree with the definition. Lease Term is defined as “the period during which a lessee has a noncancelable right to use an underlying asset, plus each option period if it is probable...”. Disagree with the use of the phrase “**noncancelable right**” as it seems to imply that the lease term is the period during which the lessee’s right to use the underlying asset cannot be canceled by the lessor. Suggest rephrasing to something such as “the period during which either the lessor or lessee cannot terminate the contract or agreement without penalty”. Also suggest rephrasing “option period” to “option renewal period” to be clear.

In addition, Paragraph 15 is confusing. 15a and 15b seem to be the same, and only 15c defines “noncancelable period”. Agree with paragraphs 16 - 18.

**BIO:** I disagree with the definition. When a lease is negotiated, the lease is identified by a term (10 years for example) with a firm term (5 years) for example. The firm term is the timeframe that the Lessor amortizes the tenant improvements over in order to get his investment back. If the tenant cancels the lease during this firm term period, then the tenant will owe the unamortized tenant improvements to the Lessor in a lump sum payment. The term after the firm term and before the expiration date of the lease is still part of the lease term and is not considered option years. Option years are called renewal periods in the leasing world. These are negotiated for after the lease term (10 years). So, for example a lease could be a 10 year lease, 5 year firm, with 4 one-year renewal periods. So, this lease could technically be 14 years long.

**BOEM/BSEE:** Agree.

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**BOR:** Agree.

**DO:** Agree with the proposed guidance.

**IA:** Agrees (in part). IA believes that determining probabilities of extensions will pose problems.

**OSM:** Agree, it makes sense that we should account for the lease for the amount of time the lessee has a right to use the asset.

- Q3.** The Board is proposing that at the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases. The proposed lease recognition requirements are presented in paragraph 19.

**Do you agree or disagree with the proposed lessee recognition of a lease at the beginning of the lease term as presented in paragraph 19? Please provide the rationale for your answer.**

**PFM:** Agree. This is consistent with the asset and liability definitions in SFFAC 5.

**BIO:** I agree.

**BOEM/BSEE:** Clarification and/or confirmation of interpretation of the subleases section of the ED needed. Our interpretation of subleases: when GSA is the original lessee with a non-intragovernmental lessor and then leases that non-intragovernmental lease to another government entity, the other government entity is the new lessee and should apply the "intragovernmental" general lessee guidance for this lease. Is this the correct interpretation? There is no definition of what 'general lessee guidance' is in the ED. 'General lessee guidance', specifically, is only used under the Subleases section, but 'general guidance' is used only under the 'intragovernmental' section of the ED.

**BOR:** Agree.

**DO:** Disagree with the proposed lessee recognition of a liability and asset at the beginning of a lease term. It appears that in this case FASAB is creating guidance to mirror private sector guidance. However, Federal accounting standards do not always need to mimic private sector standards as government missions are often distinctly different than a private company's mission and the information stakeholders might need or want differs as well. According FASB's Amendment of the FASB Accounting Standards Codification No. 2016-02, Leases (Topic 842), "Previous leases accounting was criticized for failing to meet the needs of users of financial statements because it did not always provide a faithful representation of leasing transactions." The users of private sector financial statement differ from the users of Federal government users.

When a private company enters into a lease agreement, they may very well need to record a liability as stakeholders certainly have a need to know of the future liabilities of a



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company. However, recording a liability for the Federal government for leases in certain instances, such as noted in Paragraph 16c, "A fiscal funding or cancellation clause should be considered in determining the lease term only when it is probable that the clause will be exercised," I do not believe is accurate. In the case of the Federal government, a change in administration or an abrupt end to a specific project may result in the cancellation of a lease with no future obligation. If the purpose of the financial statements of the Federal government is to paint a true picture of its financial position, I would argue that certain lease liabilities are not true liabilities for the actual going concern of the Federal government. Additionally, by recording a liability and an associated asset, there is no impact on the net position of the Federal government, only an inflation of balance sheet figures. I believe that the current OMB Circular A-136 guidance regarding the disclosure of leases within the footnotes of agencies' financial reports is adequate for reporting the financial position of the Federal government. Requiring the recording of liabilities and assets for leases adds a burden to agencies where the benefit does not outweigh the cost.

**IA:** Need clarification. GSA Operating agreements shall not be capitalized and no liability shall be reported? When there's a purchase option on a newly signed lease contract- will the asset purchase be recorded at that time or will a lease asset/liability still be recorded until the time of purchase and then the Asset purchase will be recorded? Paragraph 21E seems to confuse this issue.

**OSM:** Yes, if we have lease we need to recognize we should have a liability/PPE right to use lease asset on one side and a Receivable/Deferred revenue on the other.

- Q4.** The Board is proposing that a lessee should measure the **lease liability** initially at the present value of payments to be made for the lease term. In addition, the measurement of the lease liability should include the several types of payments that might be required by a lease. The proposed lease liability measurement and recognition requirements are presented in paragraphs 21– 29 and further explained in paragraphs A20 – A21.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease liability as presented in paragraphs 21 - 29 and further explained in paragraphs A20 – A21? Please provide the rationale for your answer.**

**PFM:** Partially agree. 21f, payments for penalties for terminating the lease, should not be considered in measuring the initial lease liability but should be considered in remeasurement of the liability when considering terminating the lease during the noncancelable period.

**BIO:** I agree with the majority of the paragraphs. I have concern about 21d and 21f. 21d is very vague. Measurement of lease liability includes "Amounts that are probable of being required to be paid by the lessee under residual value guarantees". In my mind, tax adjustments would be included in this purview. Tax adjustments are probable of being required, however, it is unknown what those adjustments would be until the Lessor provided the tax receipts from the previous year. So, how could those be included in a liability determination? As for 21f, measurement of lease liability includes payments for penalties for lease termination. If a lessee terminates the lease early (during the firm term

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of the lease), the Leasing Contracting Officer and the Lessor negotiate the terms of that penalty. It starts with the unamortized portion of the tenant improvements that have left to be paid and can be negotiated from there. If the Landlord has a tenant looking to move into that space right away, he may waive a good portion of that penalty to get the lessee out sooner. What I'm pointing out is that this amount is not firm and is negotiable, so how do you determine the amount to apply to the lease liability?

**BOEM/BSEE:** Undecided, see clarification and/or confirmation of interpretation is needed. See Q3 response.

**BOR:** Partially Agree. A lease does not really contain interest. Have concerns regarding the cost benefit. Do not see the value of discounting the lease and reporting the interest.

**DO:** Disagree with the proposed lessee measurement and recognition of the lease liability. Requiring the measurement of lease liabilities at the present value of payments could place an enormous burden on agencies to individually track each and every lease and adjust them every month for GTAS (Governmentwide Treasury Account Symbol Adjusted Trial Balance System) reporting. The current requirement of an annual footnote disclosure within agencies' annual financial reports seems adequate for Federal government reporting purposes. See Q3 response.

**IA:** Agree with the present value and other items to calculate the Liability. However- For A21- the full obligation would occur at the inception of the contract for the liability amount? What about ISA vs DLA leases- with DLA obligation s/b annual.

**OSM:** Agree-We should only have to recognized what is the current value of the lease when we enter into the lease and then adjust as needed.

**Q5.** The Board is proposing that the future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the lessee's incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used. The specific proposed requirement is presented in paragraph 23.

- a. **Do you agree or disagree that the rate the lessor charges the lessee, which may be the interest rate implicit in the lease, should be used to measure the future lease payments as presented in paragraph 23? Please provide the rationale for your answers.**

**PFM:** Agree as it's the actual rate charged.

**BIO:** For private sector leases, this is acceptable. However, for Government leases, this is harder to determine. A Leasing Contracting Officer must get the interest rate the Lessor. This can prove to be difficult. In addition, that rate does not necessarily provide an accurate account for the escalation of the rents on the lease. In most cases, the operating expenses are the only portions of the rent that are escalated and they are

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escalated per the CPI Index rates. So, these rates could be significantly different depending on the time.

**BOEM/BSEE:** Undecided, if the lease is through GSA for a non-intragovernmental lease, what is spelled out in the occupancy agreement for rates/charges is what is billed, why would the future lease payments need to be discounted?

**BOR:** Partially Agree. See response to question 4.

**DO:** Disagree with discounting future lease payments. See Q3 and Q4 responses.

**IA:** Agree - this is the rate actually charged

**OSM:** Agree-we will leave this up the FASAB to determine

- b. **Do you agree or disagree that the lessee's incremental borrowing rate should be used to measure the future lease payments when the lessor rate cannot be reasonably estimated by the lessee as presented in paragraph 23? Please provide the rationale for your answers.**

**PFM:** Agree but not sure how to determine lessee's incremental borrowing rate.

**BIO:** For private sector leases, this is acceptable. However, if this is a Government lease, there is no incremental borrowing rate for Government tenants. The Lessor's rate would need to be used and I disagree with using that per my answer above.

**BOEM/BSEE:** Undecided, where would a bureau get their incremental borrowing rate from?

**BOR:** Partially Agree. See response to question 4.

**DO:** Disagree with discounting future lease payments. See Q3 and Q4 responses.

**IA:** Agree - Lessor's rate should be the first consideration.

**OSM:** Agree-We will leave this up to FASAB to determine

- Q6.** The Board is proposing that the lessee should remeasure the lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability. The Board is also proposing that the lease asset should generally be adjusted by the same amount when the corresponding lease liability is remeasured based on those changes. Additionally, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain. The proposed lessee requirements for remeasurement are presented in paragraphs 25 – 29, 33, and further explained in paragraph A19.

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- a. **Do you agree or disagree with the circumstances when the lessee must remeasure the lease liability as presented in paragraph 25? Please provide the rationale for your answer.**

**PFM:** Agree as the circumstances will affect the liability.

**BIO:** I agree. If significant changes are negotiated to a lease that affect the rates, square footage, or payments, then the lease liability should also change as well.

**BOEM/BSEE:** Might not be cost effective.

**BOR:** Agree. The change in the lease should trigger the remeasurement. Periodic remeasurements should not be required.

**DO:** Agree with the remeasure proposal.

**IA:** Agree - logical to re-measure in these circumstances.

**OSM:** Agree - We should always remeasure amounts we have on the financial statements whenever we prepare them to ensure they are accurate and reflect the current situation.

- b. **Would the requirements triggering remeasurement cause undue costs? Please provide the rationale for your answer.**

**PFM:** No, as only significant changes are considered for remeasurement.

**BIO:** I don't believe so.

**BOEM/BSEE:** Might not be cost effective.

**BOR:** Reevaluating the future liability would be necessary if the circumstances of the lease changed. If the requirement is to remeasure all leases periodically, this would cause undue costs.

**DO:** As stated in responses to previous questions, I believe the entire process of measuring and recording lease liabilities and assets creates an undue cost to the Federal government.

**IA:** Unsure at this point- certainly a possibility.

**OSM:** No I don't think so since it would be part of the normal process of doing business with a lease agreement.

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- c. **Do you agree or disagree with the effect of the remeasurement on the carrying value of the lease asset as presented in paragraph 33 and further explained in paragraph A19? Please provide the rationale for your answer.**

**PFM:** Agree, as the position of the entity has not been changed due to the remeasurement (net effect 0 to the balance sheet).

**BIO:** I disagree. If the lease asset value is carried at the initial amount of lease liability, that is the total rent paid over the lease term. So, if that liability will be the asset value, how do you depreciate the lease asset? A leased asset is something you do not own. Therefore, how do you handle the accounting of that depreciation of that asset value?

**BOEM/BSEE:** Might not be cost effective.

**BOR:** Agree. If the carrying value of the leased asset is reduced to zero a gain should be reflected on the statement of cash flows.

**DO:** Agree.

**IA:** Need to elaborate as to why a gain would result.

**OSM:** Yes - assets and liabilities should always match between the lessor and the lessee.

- Q7.** The Board is proposing that a lessee should measure the lease asset initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service. The proposed lessee lease asset measurement and recognition requirements are presented in paragraphs 30 – 34 and further explained in paragraph A22.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease asset as presented in paragraphs 30 - 34 and further explained in paragraph A22? Please provide the rationale for your answer.**

**PFM:** Agree. The benefits derived from the lease should be the same for each period in the lease term. Including these costs and amortizing over the lease term on a straight-line basis will match the costs to the benefits.

**BIO:** I disagree. See my answer in Q6c.

**BOEM/BSEE:** Undecided, see clarification and/or confirmation of interpretation is needed. See Q3 response.

**BOR:** Agree. Entities must include all costs associated with the leased asset.

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**DO:** If the Board is going to require a liability be recorded for leases, then I believe the asset should be recorded in the amount of the liability only. To require agencies to record other costs as an asset and then amortize the amounts creates a burden where the costs do not outweigh the benefits.

**IA:** Agree - inclusions/exclusions are logical.

**OSM:** Yes - gain whatever the lessor measurement and recognition standards are, the lessee should mirror it.

- Q8.** The Board is proposing that at the beginning of the lease term, a lessor should recognize a lease receivable and deferred revenue, except for intragovernmental and short-term leases. The proposed requirements for the measurement and recognition of the lessor lease receivable and deferred revenue are presented in paragraphs 36 – 48 and further explained in paragraphs A23 - A24.

**Do you agree or disagree with the proposed lessor measurement and recognition of the lease receivable and deferred revenue as presented in paragraphs 36 - 48 and further explained in paragraphs A23 - A24? Please provide the rationale for your answer.**

**PFM:** Agree. This is consistent with the definitions of asset and liability in SFFAC 5.

**O (Tami Skinner):** I agree. However, this applies to private sector leasing, not Government leases.

**BOEM/BSEE:** Undecided, see clarification and/or confirmation of interpretation is needed. See Q3 response.

**BOR:** Agree.

**DO:** If the Board is going to implement the proposed lessee requirements, then I agree with the lessor measurement and recognition.

**IA:** Agree - this is consistent with the lessee accounting treatment (as the other party).

**OSM:** Yes, if we have lease we need to recognize we should have a liability/PPE right to use lease asset on one side and a Receivable/Deferred revenue on the other.

- Q9.** The Board is proposing to define a short-term lease as a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. The proposed requirements for the measurement and recognition of a short-term lease are presented in paragraphs 59 – 61 and further explained in paragraph A25.

**Do you agree or disagree with the proposed definition and measurement and recognition of a short-term lease as presented in paragraphs 59 - 61 and further explained in paragraph A25? Please provide the rationale for your answer.**



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**PFM:** Agree, as recognizing an asset and liability for leases less than 24 months is not cost-effective.

**BIO:** I agree. It is good to have a specific definition and two years is a reasonable timeframe.

**BOEM/BSEE:** Agree.

**BOR:** Agree.

**DO:** Agree with the proposal.

**IA:** Agree. Costs outweigh benefits to implement the standards for leases 2 years or less and this is also consistent w/ the useful life determination for PP&E.

**OSM:** Agree - We will leave this up to FASAB to determine. One issue we might want to consider is maybe considering a short term lease to be one year or less since that is what we normally consider when classifying liabilities into current vs noncurrent. Maybe keeping the same time line would help the statements be more consistent.

**Q10.** The Board is proposing to establish distinct standards for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, Reporting Entity. The proposed requirements for the measurement, recognition, and disclosure of intragovernmental leases are presented in paragraphs 75 – 95 and further explained in paragraphs A26 - A29.

**Do you agree or disagree with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases as presented in paragraphs 75 - 95 and further explained in paragraphs A26 - A29? Please provide the rationale for your answer.**

**PFM:** Agree. This will avoid double-counting assets and liabilities at the government-wide level, and it will avoid issues with intragovernmental reconciliations

**BIO:** I agree. No further comment.

**BOEM/BSEE:** Agree - see Q3 for clarification and/or confirmation of interpretation is needed. Also, for lease incentives and concessions, the guidance states these should be recognized as reductions of lease rental expense by the lessee on a straight-line basis over the lease term. If the expenses the lessee recognizes for these intragovernmental leases is different than what GSA has for revenue, this will potentially cause issues with intragovernmental eliminations, unless GSA is compensating or billing the lessee using the straight-line basis.

**BOR:** Agree. By not recording a lease asset, this resolves issues with eliminations and/or double recording of the asset at the department and government-wide level.

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**DO:** Agree with the proposal.

**IA:** Needs clarification. Paragraph #86- Currently, we expense TI if GSA has built it into the total cost and bills on a monthly basis. We would capitalize and amortize only if an RSA exists exceeding our threshold. Is this paragraph consistent with that approach? For paragraph #87- is this an expansion of our FMLP note for Federal leases?

**OSM:** Agree-we will leave this up to FASAB to determine.

- Q11.** The Board is proposing that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. The proposed implementation requirements are presented in paragraphs 99 -100.

**Do you agree or disagree with the proposed prospective implementation approach as presented in paragraphs 99 - 100? Please provide the rationale for your answer.**

**PFM:** Agree as this is a new requirement and not a correction of prior year errors.

**BIO:** I disagree. This makes no sense at all. The lease liability and lease asset should initially be measured based on the remaining lease term (this part makes sense because that is what is left in the liability) and associated lease payments as of the beginning of the period of implementation (this makes no sense to me). These amounts would not match and therefore, cause a difference in accounting.

**BOEM/BSEE:** Agree.

**BOR:** Agree.

**DO:** Agree with the proposal.

**IA:** Agree - treating this prospectively will avoid additional costs during implementation.

**OSM:** Agree - if there is new reporting standard then it should be applicable to all leases involved.

- Q12.** The Board is proposing that the requirements of this Statement be effective for reporting periods beginning after September 30, 2018. The proposed effective date is presented in paragraph 101.

**Do you agree or disagree with the proposed effective date as presented in paragraph 101? Please provide the rationale for your answer.**

**PFM:** Agree as agencies need time to implement the new requirement.

**BIO:** I agree. Agencies will need at least a year and a half, if not longer, to be able to implement these changes.



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**BOEM/BSEE:** Undecided, refer to response on Q10. Does GSA need to change their methodology for billing?

**BOR:** Agree.

**DO:** Agree with the proposal.

**IA:** Agree - treating this prospectively will avoid additional costs during implementation.

**OSM:** Agree- Giving reporting entities a year to implement is a good time frame.



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COMPTROLLER

JAN 05 2017

Wendy M. Payne, Executive Director  
Federal Accounting Standards Advisory Board  
Mailstop 6H19  
441 G Street, NW, Suite 6814  
Washington, DC 20548

Dear Ms. Payne:

The Department of Defense (DoD) is pleased to submit the attached comments to the Federal Accounting Standards Advisory Board (FASAB) on the Exposure Draft (ED), *Accounting for Leases*. Our response to FASAB's request for comments is organized into two Sections: (1) Responses to the ED questions; and, (2) Comments on other matters contained in the ED.

The DoD understands that the Board undertook this effort in response to questions raised during the development of the Financial Accounting Standards Board's guidance in Accounting Standards Codification 842, *Leases*. However, the DoD notes that there is a divergence between that standard and FASAB's proposal, as discussed in detail in the appendix to this letter.

The DoD does not believe that FASAB has made a compelling case that the information available to a financial statement user under the proposed accounting model represents a significant improvement over the current accounting model, or that it necessarily achieves the goal of comprehensive view of an entity's total obligations that will result in cash outflows in future periods. For these reasons, the DoD does not support the codification of this ED as a FASAB standard.

Thank you for considering the Department's responses and comments. If you have any questions concerning our comments, please contact me.

Sincerely,

Alaleh A. Jenkins  
Assistant Deputy Chief Financial Officer

Attachments:  
As stated



**SECTION 1 – RESPONSES TO EXPOSURE DRAFT QUESTIONS**

**Q1.** The Board is proposing to define a lease as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. The current lease standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, do not specifically define a lease. SFFAS 5 and SFFAS 6 only define a capital lease as a “lease that transfers substantially all the benefits and risks of ownership to the lessee.” The Board believes that the more concise definition being proposed is broad enough to capture the diversity of federal leasing activities. The proposed lease definition is presented in paragraph 9 and further explained in paragraph A15.

**Do you agree or disagree with the proposed definition of lease presented in paragraph 9 and further explained in paragraph A15? Please provide the rationale for your answer.**

**DoD Response:**

DoD does not agree with the proposed definition. The definition is too broad and all-encompassing. The DoD believes that the definition of a lease should specifically exclude agreements such as those excluded from the recently issued Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) on Leases (Topic 842). ASC 842, as enumerated in ASC 842-10-15-1 specifically excludes leases of intangible assets; leases to explore for or use minerals, oil, natural gas, and similar nonregenerative resources; leases of biological assets, including timber; leases of inventory; and assets under construction. In addition the DoD proposes to exclude other intangible assets such as (but not limited to) land rights and rights of way, various types of easements (e.g., utility easements), air rights, mineral rights, and indefeasible rights of use. ASC 842 defines leases more specifically and states [in part], “A contract...that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration”. Because of the breadth and complexity of the DoD, the DoD enters into many different types of complex agreements that, under the proposed FASAB standard, would be difficult to categorize as a lease instead of a service arrangement. Therefore, the DoD suggests that the Board provide specific guidance in distinguishing service arrangements from leases, and suggests that the Board expand the guidance currently in paragraph A11 of the ED, and specifically define Service Concession Arrangements (SCAs) as service agreements.

In addition, the DoD believes that FASAB should consider narrowing the definition to specifically state that a lease (1) conveys the “right to control” and (2) that a lease covers “identified property, plant, or equipment (an identified asset)”. The DoD believes that the Exposure Draft should address the concept of “control” as discussed in Statement of Federal Financial Accounting Concepts (SFFAC) 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*, and the current language referring to “right to use” is too broad a term and may result in inconsistent and incorrect application of the definition of a lease. For example, service agreements may convey a right to use an asset when control is effectively retained by the supplier. Similarly, the DoD believes that the term “nonfinancial asset” is too broadly defined in footnote 16 of paragraph A11, and should not include internal use software, intangible assets, and the types of assets excluded by ASC 842.

The DoD suggests that the Board consider including a flowchart depicting a prescribed decision process to follow in identifying whether a contract is a lease or a service arrangement, and conform the ED to the concepts in the flowchart in ASC 842-10-55-1, including (but not limited to) the concept of substantive substitution rights of the supplier. The DoD enters into many contracts that involve use of assets of a supplier that may not qualify as leases when considering the guidance in ASC 842.

The DoD believes that the proposed definition, as written, will:

- 1) Create a large administrative burden on agencies on an ongoing basis. Including the term "agreement" in the definition adds ambiguity and confusion as to what should or should not be considered as a lease. At a minimum, the DoD suggests that for an "agreement" to be considered a lease for accounting purposes, an agreement should be required to be in writing and executed by each of the parties to the transaction, by individuals who are duly authorized to enter into such an agreement.
- 2) Will not prove to be cost-beneficial to federal government agencies. As federal government agencies are dependent upon ongoing appropriations, the related fulfillment of an agency's future obligations that will result in cash outflows in future periods is entirely dependent on these ongoing appropriations. The DoD believes that this is inconsistent with the concept of Budgetary Integrity in paragraph 13 of SFFAC 1: *Objectives of Federal Financial Reporting*, where "Federal financial reporting should assist in fulfilling the government's duty to be publicly accountable for monies raised through taxes and other means and for their expenditure in accordance with the appropriations laws that establish the government's budget for a particular fiscal year and related laws and regulations".
- 3) We believe that this is different from a commercial entity where these obligations are important to the portrayal of a commercial entity's financial health and viability, because unilateral rights (i.e., to make alterations at any time to the contract requirements) are not found in commercial relationships as they are with the government.
- 4) Potentially mislead the users of federal agencies' balance sheets by recording assets that have different characteristics than the other assets recorded on the balance sheet. Typically lessees do not have many of the rights in using the leased asset as they would as the owner. Often the owner/lessor retains the right to require lessees to obtain lessor approval to make changes to the leased asset that the lessee desires in order to have the asset in a condition suitable for lessee use. As a result, it does not appear proper to record an asset on the lessee's financial statements unless the terms of the lease provide the lessee with unconditional control of the asset.
- 5) Cause the rights of the parties to the arrangement to all be treated the same, and arrangements that are structured as capital leases (with specific rights of ownership under the current construct) would be accounted for the same as those arrangements that do not contain the same rights.

**Q2. The Board is proposing that the lease term be determined as the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period) plus each option period if it is probable, based on all relevant factors, that the lessee will exercise that option to extend the lease. The lease term proposal also provides guidance on the noncancelable period and on how specific provisions (such as fiscal funding/cancellation clauses and month-to-month lease holdovers) should be applied. The proposed lease term requirements are presented in paragraphs 14 – 18 and further explained in paragraphs A16 – A18.**

**Do you agree or disagree with the proposed guidance on determining the lease term as presented in paragraphs 14 - 18 and further explained in A16 – A18? Please provide the rationale for your answer.**

DoD Response:

The DoD does not agree with the proposed guidance. The DoD believes that for the lessee, fiscal funding

clauses should be considered in determining the noncancelable period, without regard to probability of exercising the fiscal funding clause. Specifically, not considering a fiscal funding/cancellation clause (unless it's probable of being exercised) as a reason to exclude future periods from the noncancelable period will:

- 1) Result in reflecting liabilities on the balance sheet that are analogous to liabilities that are contingent on future events rather than liabilities reflecting events that have already occurred.
- 2) Include liabilities on the balance sheet which are not liabilities based on current laws or regulations, which is contrary to most, if not all, other liabilities recorded on the balance sheet. The DoD, like many federal government agencies, is subject to mandates from Congress such as sequestration, and the annual budget process, which can affect DoD's ability to satisfy obligations such as lease liabilities. At any given time, recording these liabilities would not be an accurate depiction of the DoD's obligations because Congressional mandates could (like sequestration) render certain contracts (like lease contracts) short-term in nature (i.e., they can be cancelled subject to these mandates). Since the federal government lessee can unilaterally terminate the contract at any time, the probability of whether or not this will occur should not be a factor. Fiscal funding clauses in lease contracts should be considered since this reflects both the legal form and economic substance of the lease transaction. Recognizing the legal enforceability and substance of the fiscal funding clause in a lease contract, a maximum of one fiscal year would be the lessee's minimum lease term, thereby qualifying the lease as a short-term lease. These unilateral contractual rights of a federal government lessee are not found in leases where a commercial entity is the lessee. Leases with commercial entity lessees legally commit the commercial entity lessee to a minimum lease term that cannot be unilaterally altered. For leases greater than one year, commercial leases are not similar to government leases, which typically have annual option periods in which the government lessee can unilaterally exercise or terminate the remainder of the lease term without any further liability. This annual opportunity to "opt out" of the remainder of the lease is not included in commercial leases. This major difference of the terms in the lease between commercial entities and federal entities should be considered and respected in how the lease is accounted for since it represents a fundamental difference in the legal liability the entity is committed to. This is supported by the American Institute of Certified Public Accountants' Audit and Accounting Guide, *Federal Government Contractors*, which acknowledges that government contractors are subject to a degree of risk different from their commercial counterparts because of the unilateral contractual right of the government to terminate a contract.
- 3) Cause the accounting for leases to be inconsistent with the accounting for other types of liabilities, such as entitlement programs, as they are reflective of the current legal obligations of the federal government and would only be changed based on changes in law. Recording a liability for a non-finance or non-sales type lease is recording a liability for a future event that may not occur (e.g., the occupancy of a building or office space in the future). This is inconsistent with the definition of a liability as discussed in paragraphs 42 and 46 of SFFAC 5.
- 4) Include as liabilities amounts which are not real liabilities since the federal government can contractually reduce them to zero through a non-appropriation. Including these amounts as liabilities does not provide the user of the financial statements with an accurate depiction of the agency's financial condition, and can be misleading to the users of the financial statements. Instead, this information (significant lease terms) could be included in the notes to the financial statements to achieve the same objective of reporting future use of resources in satisfaction of the respective leases.
- 5) Result in unfunded lease liabilities recorded in the balance sheet and no corresponding obligation in

the Statement of Budgetary Resources (SBR), creating a difference between the obligation in the SBR and the liability on the balance sheet.

- 6) Impose undue hardship on agency financial statement preparers to analyze, prepare, record, and retain information for numerous lease transactions that otherwise would not be needed.
- 7) Be inconsistent with Office of Management and Budget (OMB) budget requirements, which state in OMB A-11:

“For operating leases, budget authority is required to be obligated up front in the amount necessary to cover the Government's legal obligations, consistent with the requirements of the Antideficiency Act. This will include the estimated total payments expected to arise under the full term of the contract or, if the contract includes a cancellation clause, an amount sufficient to cover the lease payments for the first year plus an amount sufficient to cover the costs associated with cancellation of the contract. For each subsequent year, sufficient budget authority is required to be obligated to cover the annual lease payment for that year plus any additional cancellation costs. For operating leases funded by the General Services Administration's Federal Buildings Fund (which is self-insuring under existing authority), only the amount of budget authority needed to cover the annual lease payment is required to be obligated.”

“For operating leases, budget authority will be scored against the legislation in the year in which the budget authority is first made available in the amount necessary to cover the Government's legal obligations. The amount scored will include the estimated total payments expected to arise under the full term of a lease contract or, if the contract will include a cancellation clause, an amount sufficient to cover the lease payments for the first fiscal year during which the contract is in effect, plus an amount sufficient to cover the costs associated with cancellation of the contract. For funds that are self-insuring under existing authority, only budget authority to cover the annual lease payment is required to be scored.”

**Q3. The Board is proposing that at the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases. The proposed lease recognition requirements are presented in paragraph 19.**

**Do you agree or disagree with the proposed lessee recognition of a lease at the beginning of the lease term as presented in paragraph 19? Please provide the rationale for your answer.**

DoD Response:

Please see the response to Q2 above.

In addition, the DoD agrees that intragovernmental and short-term leases should be exempted from the requirement to recognize a lease liability and a right-to-use lease asset. However, the DoD does not agree with the proposed recognition at the beginning of the lease term (for leases other than intragovernmental and short-term) for the following reasons.

- 1) The government does not always have the benefits of an asset and often has limited control over the use of the asset being leased.
- 2) Lessees typically do not have many of the rights in using the leased asset as they would as the owner. Often the owner/lessor retains the right to require lessees to obtain their approval to make

changes to the leased asset that the lessee desires in order to have the asset in a condition suitable for the lessee's use. As a result, it does not appear proper to record an asset in the lessee's financial statements unless the terms of the lease provide the lessee with right to obtain substantially all of the economic benefits from control of the asset throughout the period of use (for example, by having exclusive use of the asset throughout that period) and unconditional use of the asset.

- 3) The government has no title to or control of these assets under contracts that would potentially be considered leases. The government obtains the right to use an asset owned by others, but has no right to pledge, assign, or encumber these assets; or claims to these assets, and therefore recording a right to use asset in the government's financial statements does not seem to be appropriate accounting. Additionally, because the lessor (as owner) would record the asset on its balance sheet, the lessee's recording of a right to use asset would result in double counting of the asset.

**Q4. The Board is proposing that a lessee should measure the lease liability initially at the present value of payments to be made for the lease term. In addition, the measurement of the lease liability should include the several types of payments that might be required by a lease. The proposed lease liability measurement and recognition requirements are presented in paragraphs 21– 29 and further explained in paragraphs A20 – A21.**

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease liability as presented in paragraphs 21 - 29 and further explained in paragraphs A20 – A21? Please provide the rationale for your answer.**

DoD Response:

The DoD agrees with the requirement in principle, if in fact there was a liability to be recognized. However, the DoD does not agree with the proposed requirement to measure and recognize a lease liability when there is the presence of a fiscal funding clause as discussed in Q2 above.

**Q5. The Board is proposing that the future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the lessee's incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used. The specific proposed requirement is presented in paragraph 23.**

- a. **Do you agree or disagree that the rate the lessor charges the lessee, which may be the interest rate implicit in the lease, should be used to measure the future lease payments as presented in paragraph 23? Please provide the rationale for your answers.**

DoD Response:

The DoD does not agree. The "interest rate implicit in the lease" is not defined in the ED. ASC 842 defines the interest rate implicit in the lease as "The rate of interest that, at a given date, causes the aggregate present value of (a) the lease payments and (b) the amount that a lessor expects to derive from the underlying asset following the end of the lease term to equal the sum of (1) the fair value of the underlying asset minus any related investment tax credit retained and expected to be realized by the lessor and (2) any deferred initial direct costs of the lessor". If there was a requirement to apply the definition in ASC 842, it would cause significant judgment on the part of lessees that may lead to assumptions that are not accurate. In addition, Appendix B of OMB Circular A-11 requires the use of the treasury borrowing rate to calculate the present value of the minimum lease payments and using an interest rate implicit in the lease would depart from this requirement.



- b. Do you agree or disagree that the lessee's incremental borrowing rate should be used to measure the future lease payments when the lessor rate cannot be reasonably estimated by the lessee as presented in paragraph 23? Please provide the rationale for your answers.

DoD Response:

The DoD agrees that the rate used to discount future lease payments should be the lessee's incremental borrowing rate, not the lessor's rate implicit in the lease. The DoD believes that the incremental borrowing rate is more appropriate because it is less subjective and would lessen the burden of determining future lease payments by the lessee, and at the same time be reflective of the rate the lessee would have incurred to borrow, over a similar term, the funds necessary to purchase the leased asset. A Treasury bill rate using a term commensurate with the term of the lease would result in a more objective measure of the future lease payments and result in consistency in application between federal government agencies. This would also be consistent with the concepts embodied in OMB Circular A-11.

**Q6. The Board is proposing that the lessee should remeasure the lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability. The Board is also proposing that the lease asset should generally be adjusted by the same amount when the corresponding lease liability is remeasured based on those changes. Additionally, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain. The proposed lessee requirements for remeasurement are presented in paragraphs 25 – 29, 33, and further explained in paragraph A19.**

- a. Do you agree or disagree with the circumstances when the lessee must remeasure the lease liability as presented in paragraph 25? Please provide the rationale for your answer.

DoD Response:

The DoD believes that it would be appropriate to remeasure the lease liability due to the circumstances in paragraph 25, however, the DoD believes that clarity may be needed to define "certain changes". For practical reasons, it would be necessary to adjust the liability in these circumstances. The remeasurement should take place upon the actual occurrence (versus the likelihood) taking place based on conclusive evidence, since the terms and conditions of the signed lease contract or agreement still exist and the lessee has a non-cancellable right to use the asset.

- b. Would the requirements triggering remeasurement cause undue costs? Please provide the rationale for your answer.

DoD Response:

The DoD believes that the requirements triggering remeasurement will significantly increase the costs of accounting for a lease. The DoD believes that federal government entities would have to change existing processes, and design and implement systems and controls to account for these changes. Current systems are not configured to handle the complexities of accounting for lease remeasurements.

- c. Do you agree or disagree with the effect of the remeasurement on the carrying value of the lease asset as presented in paragraph 33 and further explained in paragraph A19? Please provide the rationale for your answer.



DoD Response:

The DoD believes that it would be appropriate to remeasure the lease asset as presented in paragraph 33 and further explained in paragraph A19. For practical reasons, it would be necessary to adjust the lease asset in the same manner as the lease liability.

**Q7. The Board is proposing that a lessee should measure the lease asset initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service. The proposed lessee lease asset measurement and recognition requirements are presented in paragraphs 30 – 34 and further explained in paragraph A22.**

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease asset as presented in paragraphs 30 - 34 and further explained in paragraph A22? Please provide the rationale for your answer.**

DoD Response:

Regarding initial direct costs, the DoD believes that initial direct costs that are ancillary charges necessary to place the lease asset into service (i.e., commissions and/or payments made to an existing tenant to incentivize that tenant to terminate its lease) should be excluded from the determination of the lease asset as those costs are expected to be minimal (as they are with most commercial leases) and to include these costs as part of the lease asset would cause undue costs of identifying, assessing, and accounting for these costs that would outweigh the benefit of presenting these costs as an asset. ASC 842-10-30-10 specifically states that costs to negotiate or arrange a lease that would have been incurred regardless of whether the lease was obtained, such as fixed employee salaries, are not initial direct costs. The following items are examples of costs that the DoD believes should be excluded from the measurement of the lease liability that are not considered initial direct costs (as enumerated in ASC 842-10-30-10(a) through 30-10(c):

- General overheads, including, for example, depreciation, occupancy and equipment costs, unsuccessful origination efforts, and idle time;
- Costs related to activities performed by the lessor for advertising, soliciting potential lessees, servicing existing leases, or other ancillary activities;
- Costs related to activities that occur before the lease is obtained, such as costs of obtaining tax or legal advice, negotiating lease terms and conditions, or evaluating a prospective lessee's financial condition.

The DoD believes that a simpler and better accounting for these costs would be to include them as period expenses.

The DoD further recommends adding illustrative examples of the concepts embodied in paragraphs 33 and 34 of the ED.

**Q8. The Board is proposing that at the beginning of the lease term, a lessor should recognize a lease receivable and deferred revenue, except for intragovernmental and short-term leases. The proposed requirements for the measurement and recognition of the lessor lease receivable and deferred revenue are presented in paragraphs 36 – 48 and further explained in paragraphs A23 -**

A24.

**Do you agree or disagree with the proposed lessor measurement and recognition of the lease receivable and deferred revenue as presented in paragraphs 36 - 48 and further explained in paragraphs A23 - A24? Please provide the rationale for your answer.**

DoD Response:

Other than Enhanced Use Leases (EULs), the DoD is generally not a lessor. EUL is a method for funding construction or renovations on federal property by allowing a private developer to lease underutilized property, subject to several provisions, with rent paid by the developer in the form of cash or in-kind services. Because of the structure of these arrangements, the long terms of EULs, and the complexities related to the compliance with requirements of Section 2667 of Title 10, U.S. Code, EULs are would prove difficult to account for under the proposed standard. Therefore, the DoD recommends adding illustrative examples of the concepts embodied in paragraphs 36 – 48 and revising the ED to address EULs.

**Q9. The Board is proposing to define a short-term lease as a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. The proposed requirements for the measurement and recognition of a short-term lease are presented in paragraphs 59 – 61 and further explained in paragraph A25.**

**Do you agree or disagree with the proposed definition and measurement and recognition of a short-term lease as presented in paragraphs 59 - 61 and further explained in paragraph A25? Please provide the rationale for your answer.**

DoD Response:

The DoD agrees with the definition of a short-term lease as “a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less”. However, the DoD does not agree that options to extend should be included without regard to their probability of being exercised. The DoD believes that options to extend would be excluded until those options are probable of being exercised. The DoD believes that this treatment is appropriate because of the unilateral rights afforded to the government related to termination of contracts.

**Q10. The Board is proposing to establish distinct standards for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, Reporting Entity. The proposed requirements for the measurement, recognition, and disclosure of intragovernmental leases are presented in paragraphs 75 – 95 and further explained in paragraphs A26 - A29.**

**Do you agree or disagree with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases as presented in paragraphs 75 - 95 and further explained in paragraphs A26 - A29? Please provide the rationale for your answer.**

DoD Response:

The DoD agrees with the proposed definition, measurement, recognition, and disclosures of

intragovernmental leases as presented in paragraphs 75 – 95 and further explained in paragraphs A26 – A29. More specifically, the DoD believes that leases between federal government agencies that consolidate to the overall U.S. Government financial statements, and non-government entities that are required to be consolidated in a federal government agency's financial statements in accordance with SFFAS 47, *Reporting Entity*, would qualify as intragovernmental.

The DoD does not agree with the disclosure requirements for intragovernmental leases embodied in paragraphs 87 and 95 of the ED. The preparation of these disclosures would require systems and processes to track and account for these leases, which would contradict the purpose of the intragovernmental "exception" to recording lease assets and liabilities, and add complexity and cost.

**Q11. The Board is proposing that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. The proposed implementation requirements are presented in paragraphs 99 -100.**

**Do you agree or disagree with the proposed prospective implementation approach as presented in paragraphs 99 - 100? Please provide the rationale for your answer.**

DoD Response:

The DoD disagrees with the proposed guidance. The DoD believes that the proposed standard should apply only to leases entered into after the effective date of the proposed standard. The DoD believes that federal government entities will need time to develop processes, and implement systems and controls to be able to apply the proposed standard. Requiring the determination of the lease term assuming that the lease term began as of the beginning of the period of implementation, and requiring that the lease liability and lease asset be initially measured based on the remaining lease term and associated lease payments as of the beginning of the period of implementation would cause undue cost.

The reason for the undue cost is that there is no consistent methodology or policy that has been followed to record monthly or periodic payments that are made on leasing arrangements. These payments could be recorded in various general ledger accounts, and searching for them and identifying them will be very labor intensive. Determining the population of leases subject to the accounting requirements in the ED will require identification, review and analysis of an enormous number of payment transactions. The DoD suggests that the proposed standard be applied only to leases entered into after the effective date of the proposed standard to reduce difficulties related to identifying and assessing current leases to allow for proper implementation of the proposed standard.

**Q12. The Board is proposing that the requirements of this Statement be effective for reporting periods beginning after September 30, 2018. The proposed effective date is presented in paragraph 101.**

**Do you agree or disagree with the proposed effective date as presented in paragraph 101? Please provide the rationale for your answer.**

DoD Response:

The DoD disagrees with the proposed effective date as presented in Paragraph 101. The DoD proposes that the effective date be approximately four years after the issuance date of the proposed standard. This amount of time is needed for federal government entities to develop processes, and design controls and develop systems in order to account for these lease transactions. As a point of reference, the FASB lease

standard issued in February 2016, is effective for fiscal years beginning after December 15, 2019 (approximately 46 months).

## **SECTION 2 – COMMENTS ON OTHER MATTERS CONTAINED IN THE EXPOSURE DRAFT**

- 1) Purpose (Paragraphs 1 – 3) — Federal agency financial statements, and the users of those financial statements, are different than the financial statements of commercial entities and/or state and local government financial statements and their users. For this reason, the DoD requests that the Board consider the following reasons for not following the recent direction of the FASB and GASB in changing lease accounting.
  - The FASB revised lease accounting for commercial entities primarily due to a concern that the amount of off balance sheet debt related to leases was a large amount.
  - Based on a study of 2014 public company filings, FASB technicians found more than \$1 trillion in undiscounted lease obligations are reported in footnotes and not on the balance sheet.
  - FASB found that credit rating agencies, industry focused analysts, and sophisticated investors, were estimating lease obligations and adding them to the company's balance sheet for their analyses.
  - State and municipal financial statements are often used to evaluate their worthiness for industrial revenue bonds, tax-exempt securities, municipal bonds, etc.
  - The amount of debt carried by a commercial entity, or state or local entity usually impacts a user's analysis of the credit worthiness of the entity. More often than not, a user of the financial statements of a federal government entity would not consider credit worthiness of said entity as all federal government entities are fully backed by the full faith and credit of the Federal Government itself.
- 2) Scope exceptions (Paragraph 6) — ASC 842 excludes from its scope leases in which the customer does not have a right to use an identified asset if the supplier has the substantive right to substitute the asset throughout the period of use in certain circumstances. The Board should consider a similar scope exception for both lessees and lessors. While many government contracts would appear to be leases on the basis of the definition in the ED, they may, in substance, be providing the customer with access to certain assets to provide a service (e.g., use of airport runways and taxiways by airlines).
- 3) Intragovernmental leases (Paragraph 75) — In the Basis for Conclusions, paragraph A26, the ED references an educational session provided by the General Services Administration (GSA) to the FASAB. Based on the information received, the DoD believes that the Board should further define intragovernmental leases, and more specifically, whether leases with the GSA (as assignor to other federal government agencies) qualify as intragovernmental under the ED. It is unclear whether the GSA would be considered to be an agent for the federal government or the primary lessee and sublessor.
- 4) In the final version of the proposed standard, the DoD suggests providing illustrative examples (similar to those in ASC 842) of how to apply this proposed standard.
- 5) Impact on DoD Audit Efforts — Each military service and other components within the DoD are currently focused on financial improvement and audit readiness efforts. Most of these entities are preparing for their initial financial statement audit and a large amount of resources are being utilized

in this undertaking. Having to transition to the accounting as set forth in this ED would be a significant task for the following reasons:

- a) There is a finite amount of resources that DoD has to work on audit readiness. These resources are both internal (e.g. government employees) and outside contractors. In the current environment, it is virtually impossible to obtain additional funding for audit readiness efforts. As a result, having to transition to the accounting as set forth in this ED would divert some of the audit resources to work on implementing this proposed standard.
  - b) The effort for the implementation to this proposed standard and the required steps for transition and ongoing accounting go beyond accounting for leases. Currently, lease payments can be recorded to any one of hundreds of general ledger accounts since there is no written policy providing guidance. Each of the DoD entities most likely records lease payments using different general ledger accounts so there is not an efficient way to review all lease payments made. In addition, there is no way to identify a payment transaction in the general ledger is related to a lease versus other types of payments that are routinely made. As a result, in order to identify the population of lease payments made for analysis of what type of lease exists, would be an immense undertaking. Also, to properly account for leases on an ongoing basis, changes to policies, procedures, and systems would be needed so that lease payments are recorded in accordance with the proposed standard.
- 6) The ED proposes standards for classifying leases that are different than the scoring criteria in OMB A-11. Creating this difference between financial statement accounting and OMB lease classification will cause unnecessary additional confusion and complications between budgetary accounting and proprietary accounting.
  - 7) Paragraph 6 of the ED states, "This definition does not include contracts or agreements for services unless...". We suggest that this paragraph be expanded to define what is intended to be included in "services".
  - 8) The DoD suggests that the proposed standard specifically provide concepts related to capitalization thresholds similar to that provided in paragraph 13 of SFFAS 6, addressing situations where the dollar amounts of lease payments for the minimum lease term are less than the entity's capitalization threshold.
  - 9) Footnote 7 on page 13 of the ED states "The lease asset should be classified as PP&E unless the underlying asset is not PP&E. In those instances, such assets should be classified with the underlying asset." The DoD believes based on the principles underlying the proposed accounting treatment, since both the legacy operating leases and capitalized leases are now both categorized as operating leases, and since this is based on the right to use, that the asset reported on the balance sheet should be reported as an intangible asset, and not PP&E. These assets resulting from the lease are more akin to patents, copyrights, and trademarks than to hard tangible assets that are typical of the underlying assets reported as PP&E on the balance sheet.

**Please select the type(s) of organization responding to this exposure draft. If you are not responding on behalf of an organization, please select “individual.”**

|                                   |   |                                 |
|-----------------------------------|---|---------------------------------|
| Accounting Firm                   |   |                                 |
| Federal Entity (user)             |   |                                 |
| Federal Entity (preparer)         | X |                                 |
| Federal Entity (auditor)          |   |                                 |
| Federal Entity (other)            |   | If other, please specify: _____ |
| Association/Industry Organization |   |                                 |
| Nonprofit organization/Foundation |   |                                 |
| Other                             |   | If other, please specify: _____ |
| Individual                        |   |                                 |

**Please provide your name.**

Name: Edward Gramp, Jared Leicht, April Pratt

**Please identify your organization, if applicable.**

Organization: General Services Administration

**Q1.** The Board is proposing to define a **lease** as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. The current lease standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, do not specifically define a lease. SFFAS 5 and SFFAS 6 only define a capital lease as a “lease that transfers substantially all the benefits and risks of ownership to the lessee.” The Board believes that the more concise definition being proposed is broad enough to capture the diversity of federal leasing activities. The proposed lease definition is presented in paragraph 9 and further explained in paragraph A15.

**Do you agree or disagree with the proposed definition of lease presented in paragraph 9 and further explained in paragraph A15? Please provide the rationale for your answer.**

**GSA offers the following for the Boards’ consideration:**

We agree with the definitions that a lease is a contract and in the case of intragovernmental transactions, an agreement, that give the right to use a non-financial asset for a period of time, and provides consideration or something of value in exchange for the use of the asset.

It will be helpful if in the final standard, discussion to clarify applicability to various types of real property, such as airport terminals, land lease only, outdoor parking lots/spaces, ground easements, air right easement, etc., that have required unique accounting treatment in the past. Without further guidance we would assume the Board would expect all real estate leases to be treated similar.

**Q2.** The Board is proposing that the **lease term** be determined as the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period) plus each option period if it is probable, based on all relevant factors, that the lessee will exercise that option to extend the lease. The lease term proposal also provides guidance on the noncancelable period and on how specific provisions (such as fiscal funding/cancellation clauses and month-to-month lease holdovers) should be applied. The proposed lease term requirements are presented in paragraphs 14 – 18 and further explained in paragraphs A16 – A18.

**Do you agree or disagree with the proposed guidance on determining the lease term as presented in paragraphs 14 - 18 and further explained in A16 – A18? Please provide the rationale for your answer.**

#### **GSA's Response:**

View #1

We concur that the lease term should include the noncancelable right to use the underlying asset and should include options, that have likelihood (>50% probability) of being exercised. For entities such as GSA with a high number of real estate leases in its PBS portfolio (8,000+), assessing the probability of a lease option being exercised is an extreme workload at an individual lease. We ask for consideration from the Board to approve a high level approach to assessing the likelihood of options being exercised from a historical global perspective, for specific entities such as PBS. As defined in paragraph 17 *“At the beginning of a lease, lessors and lessees should assess all factors relevant to the likelihood that the lessee will exercise options, whether these factors are contract/agreement based, underlying asset based, market based, or federal specific. The assessment often will require the consideration of a combination of these interrelated factors. Examples of factors to consider include, but are not limited to, the following ...c. The lessee’s history of exercising renewal or termination options)”*.

How would the Board consider an extension? Typically we may extend a lease for a 5 year or less period, and such language would not typically be found in the original lease award. Rather GSA would seek an amendment with the lessor, a few months prior to the lease expiration to extend the lease term for a period of time, typically 5 years or less. Would the Board consider this an option period, per definition of paragraph 11. lease option period? We understand and agree with paragraph 16 d. the month-to-month holdovers and agree this would be considered a cancelable period and agree these would be excluded from the lessee's lease liability.

Paragraphs 14-16 are difficult to understand the Board's intent. Upon initial reading it appears paragraph 16a to be in contrast to paragraph 14. We provide the following example for the Board's consideration to show the confusion of these paragraphs;

Example: 7 year initial lease term, with a 5 year firm term, and (one) 8 year renewal option. No purchase options. GSA would assess greater than 50% probability of exercising the option to renew, and less than 50% probability to terminate the lease at the end of the firm term. Application per paragraphs 14-16 we would assume the following; noncancelable period= 5 years firm, option period = 8 year, Under which paragraph would the Board include year 6 and year 7 in the lease term?

Please elaborate on paragraph 16.c. GSA does not typically use such clause in real estate leases and would not find this relevant. *A fiscal funding or cancellation clause (a clause that allows federal lessees to cancel a lease agreement, typically on an annual basis, if funds for the lease payments are not appropriated) should be considered in determining the lease term only when it is probable that the clause will be exercised.*

## **View #2**

We do see benefits of the proposed approach of defining the lease term to consider inclusion of option periods to provide a more comprehensive picture of the expected financial impact of lease agreements. Especially with real property leases that GSA has extensive history with, the base or firm term of leases are rarely the total period of time that a lease will cover, with execution of options periods, lease renewals and extensions being commonplace in our operating environment.

However, there is also concern with the ED's use of the "probable" (>50% chance) as the gauge for inclusion of options in lease terms. It is requested that the Board further consider using the alternative terminology of "reasonably certain," with its higher likelihood of outcome, for this purpose, as it is used in the FASB 842 topic. Using the lower bar of the "probable" criterion would risk creating significant financial statement impacts when there is not reliable evidence that options will be exercised. Given the



proposed accounting treatment, the immediate recognition of long-term liabilities, combined with recognition of charges for interest in the payment stream, based on the total recognized liability, would leave readers with the implication of greater extension of debt-like financing than management is really binding itself to, and represent unnecessary risk of balance sheet overstatement. With the greater risk of overstatement, we would expect greater volatility and volume of downward financial adjustments being required due to changes in estimates of the likelihood of options being exercised. Since using the assessment of “probable” rather than “reasonably certain” will lead to earlier recognition of the associated lease assets and liabilities, this balance sheet and financing impact will be further distanced, and sometime much further in advance, of managements’ actual determinations and decision-making over commitment to extending leases. Use of “reasonably certain” both reduces this risk of balance sheet overstatement, and would help move the recognition closer to actual management decision-making when options are exercised. Further discussion of the impacts of using the “probable” likelihood for including options in lease terms is discussed with responses to question 4. While paragraph A-18 indicates that the FASAB agreed to not introduce a new definition of probable, we would refer them to example of SFFAS 12 as an example of where an alternative definition currently exists for circumstances related to legal contingencies.

An additional concern within the definition of lease term is the unique definition of “noncancellable period” that the ED creates. We recommend the Board consider the alternative definitions for lease term as cited in FASB 842. The term “noncancellable” and its normal language usage implies that the lessee/lessor cannot reasonably exit the lease without significant penalty. In paragraphs 15a and 15b, the ED changes this traditional meaning, to include periods that are cancellable, as long as earlier termination is not probable. Take an example of a lease with a base 7-year term, with the option to terminate after the 5<sup>th</sup> year - with a low probability of being exercised. The paragraph 15 definition of noncancellable period, would result in the 7-year term as being the noncancellable period to use with the para. 14 definition of lease term. This result is computed by taking the base 7-year term in accordance with para. 15a, with no adjustment needed for para. 15b since early termination is not probable. For practical purposes, the technical noncancellable period is 5 years, with 2 cancellable years to make up the base 7-year lease term. The FASB terminology results in the same computation of a 7-year lease term, but leaves the traditional language of non-cancellable period being the 5-year period, and then adds the 2-year reasonably certain period after the noncancellable period to compute the lease term. The FASB wording does not change the definition of a noncancellable period to include cancellable periods that are not reasonably certain. Accordingly, we recommend the ED be adjusted to use the more traditional meaning of a non-cancellable period, to exclude cancellable periods,

regardless of the probability of being exercised. Such a change would require rewording of paragraph 14's definition of lease term, to go beyond the true noncancellable term, based on the additional conditions such as likelihood of options, comparable to the definitions FASB used.

**Q3.** The Board is proposing that at the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases. The proposed lease recognition requirements are presented in paragraph 19.

**Do you agree or disagree with the proposed lessee recognition of a lease at the beginning of the lease term as presented in paragraph 19? Please provide the rationale for your answer.**

**GSA's Response:**

We agree with the asset and liability accounts per this paragraph. For instances of bargain purchase options or ownership transfers, we agree that a lessee should record PP&E asset per SFFAS 6, par. 26.

We suggest additional clarification for 'beginning of lease term'. Numerous GSA leases are awarded that require significant build-out. In these instances availability of the use of asset is delayed upwards of 18-24 months during the construction period. We suggest clarification 'beginning of lease term', should be the date when the lessee establishes beneficial occupancy and has the right to begin using the lease asset.

**Q4.** The Board is proposing that a lessee should measure the **lease liability** initially at the present value of payments to be made for the lease term. In addition, the measurement of the lease liability should include the several types of payments that might be required by a lease. The proposed lease liability measurement and recognition requirements are presented in paragraphs 21– 29 and further explained in paragraphs A20 – A21.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease liability as presented in paragraphs 21 - 29 and further explained in paragraphs A20 – A21? Please provide the rationale for your answer.**

**GSA's Response:**

We agree that the lease liability should be recognized and measured as the present value of payments to be made by the lessee over the lease term. However, we suggest further clarification is needed specifically for 21 a, and 21 b.

Please clarify the term lease incentives used in 21 a. *Fixed payments, less any lease incentives (such as a cash payment or reimbursement of moving costs) receivable from the lessor.* Lease incentive is defined only in the section for Guidance for specific Intragovernmental Leases with paragraphs 82 as lessee and lessor in paragraph 90. Is this term not relevant to lessees with non-intragovernmental leases? If yes, then please provide further detailed guidance.

Our initial reading of 21 b, we assumed the Board intended for federal agencies to include operating costs and taxes -since variable payments dependent on CPI, - in the lease liability and associated right -to-use- lease asset. This seemed conflicting as these are period costs that are always expensed in the period incurred. It was not until we read further down the ED in paragraphs 51-56 that we realized the Board considers these as non-lease components are to be handled as separate contract from the lease component. We suggest clarification in 21 b. that operating costs are to be excluded from the lease liability or reference to paragraphs 51-56 in 21. *b. Variable lease payments that depend on an index or a rate (such as the Consumer Price Index or a market interest rate), initially measured using the index or rate as of the beginning of the lease.*

### **Additional views**

While we generally agree with the proposed measurement of lease liability stated in paragraphs 21-29 and discussed in A20 and A21, we suggest the Board revisit and reconsider requirements in multiple areas.

- We strongly believe paragraph 21 must acknowledge the excludable components of lease payments and directly reference the limitations as presented in paragraphs 51-58. Since leases regularly contain operating cost components in addition to the asset rental cost component as elements of a lease payment stream, we consider it imperative that the current narrative in paragraph 21 be amended to address the significant exclusions.

This proper understanding of major elements of lease payments that are includable and excludable under the proposed lease accounting requirements is so vital, we suggest it is preferable to have initial discussion of lease payments components in the Definitions section of the standard. It is critical for readers to have such awareness in order to understand the subsequent requirements for Recognition and Measurement for lessees and lessors, and for both asset and liability recognition, such as those prescribed in paragraph 21. As we understand the exposure draft and impacts of paragraphs 51-58, a Definitions narrative should clarify that elements in lease payments for period costs such as operating activities are excluded from the payment amounts used to determine asset and liability values. As an example, building lease payments often contain elements for

operating activities such as utilities, cleaning, maintenance, security, and other period costs like taxes. As we understand the ED, only elements of lease payments attributable to the cost of an asset should be included in calculations for asset and liability recognition.

- Regarding the discussions in paragraphs A20 and A21, there is concern that inclusion of option periods, based on an assigned probability of occurrence, is stretching the definition of liabilities to instances where there has been no management decision or legal commitment to bind an agency to long-term obligations of option periods. Resulting financial statements, even with proposed disclosures, could be a cause for confusion to readers. Application of a lease term limited to noncancellable periods would appear more consistent with elements of being bound to future payments. Inclusion of option periods in asset and liability calculations at inception of a lease does not appear consistent with the discussions in paragraph A20, regarding having an obligation at a determined date, since management must make further decisions at later dates to extend a commitment or not, into option periods. While the discussion in paragraph 21 likens leases to financing transactions, due to the inclusion of option periods, there would be little comparability between existing debt financing arrangements vs the lease liabilities that would be created in accordance with the proposed standard. As a comparison to debt financing, recognizing lease liabilities based on having options, would seem akin to recognizing liabilities at the date management might arrange a line of credit, where it is probable that the credit line will be used. For the FASAB to include option periods in lease liability calculations, further discussion is requested to provide readers a better understanding of consistency with FASAB SFFAC definitions of liabilities. The recognition of option periods is exacerbated by the proposed use of the likelihood of “probable” vs “reasonably certain” when determining inclusion of option periods, etc., and appears to create more concerns in relating the resulting lease liabilities to SFFAC liability definitions.

- It is also important to recognize the Federal acquisition process contains some bias towards longer-term contracting arrangements, such as using option periods in leases, to obtain better/reduced pricing and cost, and simplify the acquisition process by reducing the volume and amount of work that shorter, fixed terms would require. While the historical use of the option periods may lead to determinations that execution of options is probable, recognizing the potential cost of option periods as liabilities at the time of initial lease award is generally not matched with actual acquisition decisions and commitment to longer-term arrangements. By definition, having option periods allows management the discretion to change course due to future events, without penalty or incursion of cost.

- Paragraph 21a. indicates that lease incentives are to be excluded from the fixed payments amounts of a lease. We request that the Board consider clarifying the types of incentives that may apply under this exclusion. While items listed, such as cash payments or reimbursement for moving cost are understandable exclusions as they do not directly relate to the asset cost, there are also incentives where a lessor offers to make asset improvements at a lessee's request. With building leases, incentives may cover costs such as build-out finishes, customized elements such as labs or computer data centers,

furnishings, etc., likened to leasehold improvements, to improve useable space to higher levels of quality or meet requirements to meet a lessee's specific needs. While cost for such improvements may be imbedded in a lease payment stream as an incentive, we would suggest that incentives should not be excluded from the fixed payments stream when the incentive is applied to cover costs to bring an asset to specific condition required by a lessee to use the asset. We note that there is additional discussion of lease incentives and accounting treatment for them, applicable to intragovernmental leasing, in paragraphs 82, 83 and 90. Similar requirements are needed in the non-intragovernmental leases section, where we would expect such incentives to be much more prevalent.

· Also missing from paragraphs 21 through 29 is any discussion of lease concessions or leasehold improvements related to non-intragovernmental leases, comparable to discussions in paragraphs 82 through 86 and 91 through 93 for intragovernmental leases. Inclusion of such topics, as requirements for non-Fed leases is imperative, as they are regular conditions in those leases. Regarding leasehold improvements, additional discussion is needed related to subleases where improvements may be made to an asset that are for the intended use and benefit of (and generally funded by) a Federal sub-lessee, rather than for the benefit and use of the prime lessee. We would expect that a prime lessee would only record leasehold improvements for improvements intended for its own use, and sub-lessees would capitalize the cost of improvements made specifically for their benefit to eliminate duplicate asset recognition across Federal agencies. In instances where a Federal sublessee has such improvements to capitalize, we would recommend the Federal lessor (prime lessee) would expense and recognize revenues for any associated costs incurred through the underlying lease or other contracts, as cost are incurred and reimbursements earned in the period improvements are provided.

Paragraph 21.g poses similar concerns as discussed previously regarding to inclusion of option periods based on a "probable" likelihood. It is recommended that the higher level of reasonable certainty be applied for inclusion of such other payments anticipated by 21.g. in the liability calculation. The wording of 21.g needs further clarification, as the wording is overly vague and general. From the existing language, one might concluded "in the assessment of relevant factors" that additional payments will likely result from future negotiations to extend a lease, and though not yet negotiated in lease terms, could be estimated. We would strongly believe such subjective estimates would be excluded from lease liability calculations.

**Q5.** The Board is proposing that the future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the lessee's incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used. The specific proposed requirement is presented in paragraph 23.

- a. **Do you agree or disagree that the rate the lessor charges the lessee, which may be the interest rate implicit in the lease, should be used to measure the future lease payments as presented in paragraph 23? Please provide the rationale for your answers.**

**GSA's Response:**

We do not agree with using the rate implicit in the lease due to the difficulty of practical application. For the approximate 8000 real estate leases that may potentially be impacted by this standard, GSA would have difficulty assessing and tracking the rate charged from the lessor per lease. Since it would not be readily available, or identifiable to us, to do this calculation, we would need to know the fair value of each asset and from a global perspective we have no such database that houses 8000 lease asset's fair value.

- b. **Do you agree or disagree that the lessee's incremental borrowing rate should be used to measure the future lease payments when the lessor rate cannot be reasonably estimated by the lessee as presented in paragraph 23? Please provide the rationale for your answers.**

**GSA's Response:**

We agree to use the lessee's incremental borrowing rate, and GSA would assume that use of OMB historical rates in Circular A-94 would be appropriate.

**Additional Views**

There are multiple concerns and considerations we would want the Board to consider related to the discount rate determinations specified for use in paragraph 23. Selecting appropriate discount rates heavily depends on multiple factors for the Board to prioritize. For instance, one priority may be to ensure computed asset and liability values for balance sheet recognition are reasonably comparable with costs to directly build or acquire a similar asset. We recommend this element of comparability be key to the Board's decisions regarding the use of discount rates. Alternatively the Board may conclude that the lease asset and liability accounting is to be a more basic valuing of rights (to-use) conveyed by a lease, with reflection of the likely cash flows, and the present value of payment streams, without regard to whether the resulting value of rights has comparability to the cost of ownership or comparability of liabilities to traditional financing arrangements. It is requested that such issues be discussed in the standard, to allow readers to understand the basis for the Board's determination.

1. Q5 a. - While we generally agree that a lessor's rate or implicit rate is preferable to determine the true cost of an asset's acquisition, we find its use not reasonable when

option periods are included in the lease term for purposes of discounting future payments. When including option periods, the resulting asset values are likely to diverge significantly from comparable acquisition costs. In addition, inclusion of multiple option periods in a lease term gives the implication that a lessor is arranging long-term financing based on the longer option period basis and including such costs in its lease pricing. For large leasing actions, we regularly see lessors' financing arrangements to be more correlated to the base period of leases rather than the full option periods.

2. Q5 b. – For purposes of valuing assets and liabilities at comparable cost of a direct acquisition, the use of discount rates based on the lessee's incremental borrowing rate is not considered appropriate where the Federal government is the lessee. Due to the significantly lower cost of financing that the government enjoys compared to commercial rates, use of Federal financing borrowing rates in present value calculations will greatly overstate asset and liability values, compared to direct asset acquisition costs. Due to the significant disparity between interest rates available to commercial vs the Federal sector, if a lessor's financing rate or implicit rate are unknown, we would suggest the Board consider the use of a commercial equivalent, such as published average market rates for highly-rated (such as AAA) bonds of a comparable length. Use of such a commercially-based rate would be a better reflection of the interest financing being charged in a lease than the Federal incremental borrowing rate would provide.

**Further comments regarding Q5 are as follows:**

- If the primary purpose of the recognition is to value cash flows created by the rights-to-use, it may be preferable to use discount rates that would be reflective of the cost applicable to the Federal government's cash flows. Most lease vs own decisions are heavily influenced by budget limitations and the amount of up-front investment funding provided by Congress in appropriation acts. The use of the Federal incremental borrowing rate may be a better choice to simply reflect the value of cash flow streams rather than implying a commitment to long-term financing at lessor's rates.
- Inclusion of probable option periods in calculations will create significant disparity in comparability of assets values of leased vs owned assets when options periods substantially extend the base lease term. From the perspective of present value calculations, the alternative consideration of using a likelihood of "reasonably certain" instead of "probable" for determining the inclusion of options would somewhat reduce the risk of non-comparability.

Even use of the lessor's stated interest rate or the implicit interest rate, when all probable option periods are considered in calculations, will likely lead to frequent occurrences where the present value of the total lease payments is higher than an asset's market value. In long-term leases of real property, it is not unusual for lessors to recover substantial amounts of their capital investment in the base term of a lease. In many large leases, we see examples where the present value (PV) of lease payments is

over 80% of the fair market value (FMV) of the asset, using only the base term of the lease. In such instances, adding the PV of all probable option periods could create computed values well exceeding the asset's FMV. This condition would be further exacerbated if the Federal incremental borrowing rate is used, since the Federal rate is generally well below lessor borrowing rates, resulting in much higher PV calculations.

- For the Board's consideration, it is also important to be aware of significant complexities in determining lessors' interest rates and implicit rates. Generally such interest rate terms are not identified in lease agreements, and for many leases, there is not a readily determinable way to identify a comparable acquisition cost of an asset, for use in computing an implicit rate. Particularly with real property leasing, where the leased asset may only be a portion of a building, we request guidance be included in the standard to provide a basis to be used in determining estimates of the FMV component of implicit rate calculations.

- Such complexities raise particular concern when trying to interpret the first sentence of paragraph 23. With the wording in that first sentence "...which may be the interest rate implicit in the lease," it is not clear whether the Board is directing preferred use of a stated rate identified in a lease by a lessor, followed by a second choice of using an implicit rate where a stated rate is not known, or whether this quoted section is simply a comment that a stated rate may match the implicit rate. If the quoted section is simply a comment, then the requirement of the paragraph appears to assign discount rate prioritization to be 1) a lessor's stated rate in the lease, or if not known 2) the Federal incremental borrowing rate; with no requirement to calculate or use an implicit rate. If computations of implicit rates are expected, much greater detailed guidance would be needed in the standard. Since implicit rate calculations require determinations of a principle amount (such as FMV), the payment terms and payment amounts, guidance would be needed to prescribe the basis for determining FMV and which lease terms are applicable for computing future payments (such as all payments discussed in paragraph 21) and what lease term would be used for computing the implicit rate (apply paragraphs 14 and 15, or possibly limit to the base-term, or non-cancellable term, etc.). Using implicit rates will, by definition, ensure the PV of the future payments equals the FMV of the asset. Accordingly, if the definition of "future payments" for computing implicit rates match the requirements given for liability recognition, the calculated implicit rates would likely be exceptionally high, though the use of implicit rates would ensure the asset and liability values match the estimated FMV of the underlying asset. The potential for such calculated high implicit rates could very well create anomalies in the presentation interest expense recognition, as interest expense would calculate to be very large balances for entities with large amounts of leases, containing option periods.

Due to the requirements to include probable option periods in calculating liability balances, the requirements of paragraph 24 to recognize interest expense on the outstanding liability value will greatly increase costs being recognized, and in much earlier periods than is recognized in financial statements today. Taking an example of a



20-year base-term lease for a building, with a termination clause after year 15, and with two 10-year option periods that are considered probable of being exercised, the requirements of the ED would result in recognition of lease asset and liability for the PV of the full 40-year payment stream, even though the government is only committed to the first 15 years of the lease. The recognition of interest costs, beginning at the outset of such a long-term leasing arrangement seems to create a misimpression that the government is paying interest on the whole long-term liability value, and as if costs were being incurred on that value throughout the whole life of the lease.

**Q6.** The Board is proposing that the lessee should remeasure the lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability. The Board is also proposing that the lease asset should generally be adjusted by the same amount when the corresponding lease liability is remeasured based on those changes. Additionally, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain. The proposed lessee requirements for remeasurement are presented in paragraphs 25 – 29, 33, and further explained in paragraph A19.

- a. **Do you agree or disagree with the circumstances when the lessee must remeasure the lease liability as presented in paragraph 25? Please provide the rationale for your answer.**

**GSA's Response:**

We are unclear in paragraph 25a. what event(s) would meet the definition of modification referenced further down in par. 66 that would cause the lessee to remeasure the lease liability amount, and potentially cause recognition of a gain. As well as further definition and clarification is needed for the difference between modification in par. 66 vs partial termination in par. 64. Full termination is understood, but it seems as if reducing sq. footage, releasing one floor of a multi-floor building, could either be a modification or partial termination, either would provide the same accounting entry recognition. Expansion or increase of sq. footage of the leased space would provide for modification, so that may be the only difference in those two paragraphs 64-partial termination vs 66-modification. We suggest examples be provided or further clarification of the Board's intent of these paragraphs, all of 25, 64 & 66

We are unclear as to the remeasurement provision of the exposure draft outlined in paragraphs 25-29, as it relates to 25d. Initial reading we assumed paragraph 25 d., like 21 b. would include operating costs and taxes, that are adjusted annually for CPI. If we read paragraph 25 d we assume that annually the Board would expect us to remeasure the liability balance for CPI changes, however paragraph 26 would preclude us from doing such, if re-measurement is based solely on CPI adjustments;

*25. The lessee should remeasure the lease liability at subsequent financial reporting dates if any of the following changes have occurred and are expected to significantly affect the amount of the lease liability:*

- a. There is a change in the lease term due to a reassessment (see par. 18), a modification (see par. 66), or a termination (see par. 64).*
- b. An assessment of all relevant factors indicates that the likelihood of a residual value guarantee being paid has changed from probable to not probable, or vice versa.*
- c. An assessment of all relevant factors indicates that the likelihood of a purchase option being exercised has changed from probable to not probable, or vice versa.*
- d. There is a change in the estimated amounts for payments already included in the liability.*
- e. There is a change in the interest rate the lessor charges the lessee, if used as the initial discount rate.*

*26. If a lease liability is remeasured for any of the changes in paragraph 25, the liability also should be remeasured for any change in an index or rate used to determine variable lease payments if that change in the index or rate is expected to significantly affect the amount of the liability. A lease liability is not required to be remeasured solely for a change in an index or rate used to determine variable lease payments.*

It is not until you read contract/agreement with multiple component sections, starting on paragraph 51-54 do you realize that non-lease components such as operating cost and taxes would be excluded from the lease liability in par. 21 b & 25 d. We suggest in par. 21 b and 25 d, a reference to exclude such non-lease component as utility costs or taxes, as found in par 54.

**b. Would the requirements triggering remeasurement cause undue costs? Please provide the rationale for your answer.**

**GSA's Response:**

Yes these remeasurement requirements will be costly in IT system dollars needed to enhance current systems and added workload for our agency's CFO associates. GSA will have to write requirements and enhance our systems or build new to implement this standard, not only GSA's accounting system but additionally our Program office's feeder system(s). What becomes extremely problematic is the capturing of data from a specific

event(s) that is to trigger such remeasurement. During the course of an individual life of a lease we will need a sophisticated system to identify critical dates to automate the recording of accounting entries. Although the initial recording of a right - to-use - lease asset and the associated liability could be programmed to record the proper accounting entries and correct amounts at the implementation date, we are concerned with the accuracy and timeliness needed for the re-measurement requirements. With 8000 potential real estate leases impacted by this accounting standard, the dates for possible remeasurement will be potentially every business day. The remeasurement of the lease asset and liability amounts and potential gain or loss recognition, could be an area of control failure for federal agencies, if the data is input into the feeder systems incorrectly, or untimely.

- c. Do you agree or disagree with the effect of the remeasurement on the carrying value of the lease asset as presented in paragraph 33 and further explained in paragraph A19? Please provide the rationale for your answer.**

**GSA's Response:**

We are concerned that the remeasurement of the liability also requires the asset value to change and match the adjusted liability, which would alter methodology of recording assets at historical cost. This would also alter the amortization of the right-to-use-lease asset for depreciation purposes, several times potentially over the lease term. Are agencies to identify that such instances occur in their footnote section of the annual report that discloses such unique accounting methodologies for recording asset values?

**Additional Views**

While the factors identified to guide remeasurement of lease assets and liabilities appear conceptual appropriate, the practical application of remeasurement would appear to create a daunting challenge.

1. Q6.a. – The factors in paragraph 25. a. through c. are appropriate for consideration, as they are the major elements that would give rise to significant changes in estimated remaining liabilities for assets. The requirement of 25.d. would appear to capture virtually all other changes that would give rise to changes in the estimate vs actual lease payments, necessitating remeasurement in very high volumes for real property leasing, many of which would be inconsequential per instance. The requirement of 25.e might appear to be one that would occur very infrequently, however, for instances where the lessor's rate is an imputed rate, the calculated rate would change every time the payment stream changes, which would likely be a common occurrence.

2. Q6.b. Given the previous comment, we would expect a very high cost associated with remeasurement due to the anticipated volume. In many anticipated instances of minor changes, the associated cost would likely not support the resulting benefit.

However, performing the calculations would be required to know the actual impact to determine materiality of the change in various factors.

3. Q6.c. Our perspectives on the requirements of paragraph 33 depend on whether the original asset value was intended to be comparable to the underlying assets' FMV, or if it was simply a calculated PV of the cash flow, as discussed in responses to question 4 above. Where the valuation of the original leased asset was the FMV of the asset, we would not concur with adjusting the asset value due to liability remeasurement changes, other than for changes that substantially change the lease term or the FMV of the asset under lease. Other changes in the lease payment stream or discount rate would not appear to have an impact on valuing the underlying asset to warrant a change in the asset value.

If however, the originally recognized asset and liability were based on simple discounting of cash flows (especially if the lessee's incremental borrowing rate is used), disassociated from comparable asset acquisition costs, than a practice of carrying matching assets and liabilities is preferable, and requirements of paragraph 33 would ensure that matching occurs and eliminates unnecessary recognition of gains or losses.

**Q7.** The Board is proposing that a lessee should measure the lease asset initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service. The proposed lessee lease asset measurement and recognition requirements are presented in paragraphs 30 – 34 and further explained in paragraph A22.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease asset as presented in paragraphs 30 - 34 and further explained in paragraph A22? Please provide the rationale for your answer.**

**GSA's Response:**

We agree that the lease asset should be measured initially for the amount of the initial lease liability. The present value of the cash flows under the lease agreement is the best method of approximating the value of the lease contract.

Please provide examples of such initial direct costs as described in paragraph 30 c.

*30. A lessee should initially measure the lease asset as the sum of the following:*

*a. The amount of the initial measurement of the lease liability (see par. 21)*

*b. Lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor*

*c. Initial direct costs that are ancillary charges necessary to place the lease asset into service*

Paragraph 32 describes bargain purchase option in a lease contract, without congressional approval GSA would not be able to purchase such asset, bargain or not. We assume that such constraints would not meet the definition of probable. We would appreciate any further guidance on this issue from the Board.

*32. The presence of a bargain purchase option in a lease contract/agreement is not equivalent to a provision that transfers ownership of the underlying asset; therefore a bargain purchase option should be treated as any other purchase option included in a lease. If the lease contains a purchase option that the lessee has determined is probable of being exercised, the lease asset should be amortized over the useful life of the underlying asset. In this circumstance, if the underlying asset is non-depreciable, such as land, then the lease asset should not be amortized.*

### **Additional Views**

We agree that initial measurement of lease assets and liabilities should be consistent, generally matching as proposed in paragraphs 30-34. However, the same concerns exist with asset valuation as is discussed above for liabilities, for questions 4 and 5, where inclusion of probable option periods in the lease term and calculations of PV's of payments could cause significant issues with non-comparability of the asset values computed in accordance with this ED vs the FMV of underlying assets being leased. Carrying asset values for leased assets where exercising options is probable but not reasonably certain, would seem somewhat contradictory to the discussion in paragraph A-22. Given the A-22 discussion of SFFAC 5 and definitions including the ability to control an asset, it again (as with liabilities) appears mis-timed, for the ED to effectively combine the right to exercise an option with the right to actually use an asset, based on a simple probable (>50%) basis. Until management makes any determinations to exert the future control over an asset, via at least expressing the intent to exercise options, it does not seem appropriate and of likely confusion to readers, that assets may be recognized prior to that decision-making having occurred.

We also request that the final standard be further clarified regarding amortization of the asset, to identify whether amortization is to be netted directly against the asset, reducing the asset's carrying value over time (which is assumed), or recorded in conjunction with a contra-asset, similar to PP&E presentation.

**Q8.** The Board is proposing that at the beginning of the lease term, a lessor should recognize a lease receivable and deferred revenue, except for intragovernmental and short-term leases. The proposed requirements for the measurement and recognition of the lessor lease receivable and deferred revenue are presented in paragraphs 36 – 48 and further explained in paragraphs A23 - A24.

**Do you agree or disagree with the proposed lessor measurement and recognition of the lease receivable and deferred revenue as presented in paragraphs 36 - 48 and further explained in paragraphs A23 - A24? Please provide the rationale for your answer.**

**GSA's Response:**

In general, we agree with the lessor's accounting treatment indicated in paragraphs 36-48, however, we suggest the Board reconsider the lease term applicable to the lessor's calculations of receivables and deferred revenues. For purposes of conservatism, it is suggested that a higher level of confidence be required for lessors to include option periods in their lease recognition calculations, to ensure a higher degree of confidence, such as a "reasonably certain", rather than the lower "probable" (>50%) likelihood indicated in paragraph 14. In general, we believe it will be difficult for a lessor to judge probability that a lessee will exercise option periods. It would seem reasonable to liken the exercising of lessee' options to contingent rentals, which would not qualify for receivable recognition by lessors.

Regarding paragraph 46, the last sentence requires rewording to indicate that deferred revenue is to be amortized and recognized as earned revenue in a systematic and rational manner over the term of the lease. The existing language makes an incorrect statement about when deferred revenue is to be recognized (which should be at the same time as receivable recognition in accordance with paragraph 36), rather than addressing when revenue is subsequently earned.

**Q9.** The Board is proposing to define a short-term lease as a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. The proposed requirements for the measurement and recognition of a short-term lease are presented in paragraphs 59 – 61 and further explained in paragraph A25.

**Do you agree or disagree with the proposed definition and measurement and recognition of a short-term lease as presented in paragraphs 59 - 61 and further explained in paragraph A25? Please provide the rationale for your answer.**

**GSA's Response:**

We disagree. GSA would like for the Board to consider the volume of real estate leases in our portfolio that would be impacted by this standard, about 8000. We are pleased the Board considers exclusion for those under 24 months, but would propose the Board consider redefining short term leases as those with base terms 5 years or less. If at a minimum the implementation guidance required only leases with terms greater than 5 years. This would tremendously help reduce the volume of leases that we would be required to track with implementation of this standard. Such as with the Census', when they require space, and is intended for a very short term period, we would not want to recognize such asset and liabilities.

In paragraph 59 related to short-term leases, what is meant by a 'notice period?' 59. *A short-term lease is a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. For a lease that is cancelable by either the lessee or the lessor, such as a month-to-month lease or a year-to-year lease, the maximum possible term is the noncancelable period, including any notice periods. For a lease that is cancellable only by the lessee, the maximum possible term should be evaluated under the requirements of the lease term as defined in paragraph 14*

### **Additional Views**

We believe the proposed definition and measurement of short-term leases should be expanded to lessen the burden of the alternative lease accounting requirements. The following are suggestions for consideration to reduce the volume of leases requiring recognition as right-to-use assets, yet capture material transactions:

- It is suggested that short-term leases include those with base periods of 5 years or less.
- We would suggest consideration of the term of the lease, as compared to the useful life of the underlying asset, be included in determining the short-term nature. For instance, lease periods (base period) in excess of 50 percent of an asset's remaining life maybe useful as a determiner, whereby a period in excess of 50% of the remaining life indicates use for a period that might indicate a need for comparisons of costs of leasing vs ownership.
- We suggest the likelihood of option periods being exercised should be included when calculating the maximum possible period, for determining short-term leases. Using the existing wording of the maximum possible period to include options regardless of likelihood of being exercised will create the additional workload of right-to-use asset and liability recognition for many leases expected to very short in nature. Accordingly, it is suggested that the wording of the maximum possible period be replaced with the period that is reasonably certain. As an example, an IT equipment lease could be written with a base year and 4 annual option periods, for equipment expected to be replaced within 2

years, but with an expected useful life of 3 years before becoming technically obsolete and an economic life of 5 years. While it is not probable that the lease will last more than two years, full asset and liability recognition would be required by the standard in accordance with the short-term definitions, with a probable lease term of only 2 years. This appears to create unnecessary additions to the volume of assets requiring the more complex accounting treatment.

It is unclear whether the use of the term “noncancellable period” in paragraph 59 is the same as that term is as defined by paragraph 15. The last sentence of paragraph 59, with reference to paragraph 14 (which would appear to require application of the definition of paragraph 15) made interpretation difficult. Greater definition of requirements is requested to clarify the last sentence of the paragraph and its language that seemingly supersedes the “maximum possible” terminology of the first sentence of the paragraph, for instances where only the lessee has options to extend lease periods.

**Q10.** The Board is proposing to establish distinct standards for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, Reporting Entity. The proposed requirements for the measurement, recognition, and disclosure of intragovernmental leases are presented in paragraphs 75 – 95 and further explained in paragraphs A26 - A29.

**Do you agree or disagree with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases as presented in paragraphs 75 - 95 and further explained in paragraphs A26 - A29? Please provide the rationale for your answer.**

**GSA's Response:**

We agree with the general concepts proposed for intragovernmental leasing, particularly that such leases would predominantly be treated as operating leases. Specific issues with certain requirements are as follows:

- Regarding paragraph 78 we recommend clarity regarding the recognition of expenses being based on “specifics of the lease provisions.” It is unclear whether that language effectively means entities should record cost to match cash flows (payment provisions) or some other provisions of the lease. We would suggest that costs should be recognized evenly over the lease term, or in relationship to levels of asset rental services provided over the lease term (variations may exist in services provided from period-to-period or the quantity of assets being supplied may be adjusted, such as for changes in assigned



square footage in buildings). We would suggest that a cash flow based approach may not properly match costs to services and assets being provided.

· In paragraph 86 we recommend clarity regarding recognition of capitalized leasehold improvements. The financing of such improvements can take various forms, such as 1) upfront funding being provided by lessees either in advance of, or at the time of acceptance of the improvements; 2) amortization of the leasehold improvement over the entire base period of a lease; or 3) amortized over a term shorter than the entire lease term. Each of these conditions would appear to require unique recognition treatment. In the first instance, the proposed language for the standard would appear to apply. For the second instance, there may be no unique treatment warranted, as costs would already be spread evenly over the lease term based on the lease provisions. In the third instance, there would appear to be a need to separately recognize costs and liability for the future payments related to the improvements, with amortization over the lease period.

With leasehold improvements, we request further clarity to determine if the definition includes costs for items like building construction and build-out costs necessary to develop an asset to a basic level of usability (such as “plain vanilla” office space). Alternatively, leasehold improvements may be limited to only those improvements made to bring an asset to a higher level of suitability for a lessee’s specific needs. Such clarity in definitions would be used to differentiate between certain payments and costs that may qualify as prepaid expenses (discussed in paragraph 78) related to the development of a basic asset for lease, vs the additional costs for improvements that take an asset to higher levels than a basic operating asset. We would suggest that costs incurred to bring an asset to basic operating condition should be consider costs of the asset being leased, with amortization of such costs as prepayments when payment is required other than amortization with the cost over the lease term. We also suggest that leasehold improvements only include costs above and beyond those incurred to bring an asset to basic operating condition.

· Similarly to the leasehold improvement discussion, clarity for lessors, as discussed in paragraph 93 is requested to ensure proper understanding of the requirements. We recommend that improvement's only be capitalized by lessors when improvements are to enhance or extend the life of assets that are general in nature to the asset, and not specific to a particular lessee’s needs. We would recommend that capital improvements to a lessor’s owned assets not be capitalized for improvements made to meet a specific lessee request, particularly when directly funded by the lessee. In subleasing arrangements where a Federal entity is subleasing an asset it leases from a non-federal entity, we further recommend that capitalization of leasehold improvements should only be applicable to entities receiving the benefit of the improvements. Accordingly, when improvements are funded on a pass-through basis from the actual Federal tenant/sublessee to the non-Fed lessor, improvements would only benefit the tenant/sublessee, making the costs capitalizable in the sublessee’s records. Such costs

capitalized by subleases would be expensed by the prime federal lessee (landlord to the sublease tenant), who derives no direct benefit from those improvements.

- Similar to discussions above related to paragraph 78, we recommend that requirements be further defined to clarify the income recognition of “based primarily on the provisions of the lease.” As suggested for expenses, we recommend similar concepts be applied have income earned evenly over the term of the lease, with considerations for variations in service delivery that may occur over the lease term. We would have concerns if the Board intends that the “provisions in the lease” are equated to the timing and amount of payments that may not reflect the substance of services and rights being provided.
- For intergovernmental leasing, please add clarity regarding the definition of “lease term” to confirm whether or not the definitions in paragraph 14, 15 and 16 apply to intragovernmental leases, especially conditions related to probability of lease options. An example of why this clarification of definition is needed relates to paragraph 95 and the disclosure of future lease rental income over the lease term. This lease term would require definition for entities to determine when conditions require inclusion of cancellable terms vs non-cancellable terms (with current disclosure requirements only covering non-cancellable terms).
- There are also conditions in some intragovernmental leases, that transfer the asset to the lessee, at the end of the agreement term. Comparable to the requirements of paragraphs 20 and 37, we recommend that such agreements be treated as a purchase and sale between the Federal lessee and lessor, respectively, rather than following operating lease treatment.

**Q11.** The Board is proposing that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. The proposed implementation requirements are presented in paragraphs 99 -100.

**Do you agree or disagree with the proposed prospective implementation approach as presented in paragraphs 99 - 100? Please provide the rationale for your answer.**

**GSA’s Response:**

We believe the implementation requirements of the ED will be unnecessarily difficult to accomplish for existing leases. We recommend the Board consider alternatives such as discussed related to question 9, and consider extending the periods reportable as short-term leases with base periods remaining of at least a five year period from the date of implementation. In addition, much further clarity would be required to provide guidance related to determination of discount rates

to be applied when recognizing leased assets and liabilities, particularly to compute imputed rate for remaining lease periods. Please refer to additional discussions addressed in question 5, for issues requiring further details being needed to support computation of imputed discount rates. We have significant concerns regarding existing leases as posing tremendous challenge to collect and capture necessary data for many old leasing records to enable the agency to calculate lease asset and liability balances. Particularly information related to future option periods is not captured today in any form that can be used for computations for financial recordkeeping, requiring manual review, analysis and data collection from all leases. The resources expected for such a task may very well be cost prohibitive.

**Q12.** The Board is proposing that the requirements of this Statement be effective for reporting periods beginning after September 30, 2018. The proposed effective date is presented in paragraph 101.

**Do you agree or disagree with the proposed effective date as presented in paragraph 101? Please provide the rationale for your answer.**

**GSA Response:**

We disagree with the proposed effective date presented in paragraph 101 as it appears unreasonable for the implementation of this standard. For agencies and departments with large volumes of leasing activity, significant new automation will be required to handle the large volume of ongoing lease activity and changes that will now require accounting recognition. The staffing resources anticipated to manage the implementation requirements for existing leases is expected to be quite significant in size and cost (see related issues noted in question 11 above). The long-term operating environment to manage lease data and lease accounting requirements will demand increases for associated staffing resources as well.

Timeframes for development of automated systems functionality is particularly problematic. For large systems modifications and new systems development that is envisioned to meet the requirements of this proposed standard, the Federal budget cycle is a key driver to consider. At the earliest, agencies and departments would need to submit proposals in their FY 2019 budget requests due for submission in August of 2017. To have funding requests included in the 2019 submission, agency financial experts would need to work very quickly with IT experts to develop rough-order-of-magnitude estimates, to address requirements based on this FASAB ED (since a final standard is not expected until well after submission of budget requests). Such budget submissions, if successfully approved, would likely provide funding to start system development activities sometime early in FY 2019. Given the size and complexity of

envisioned systems changes, it could easily take more than one year after receiving budgetary funding to complete systems development. We can already anticipate the need for significant new systems functionality in just the business systems that capture lease contact data where GSA is a lessee and systems that capture agreement data where GSA is a lessor. Additional requirements and implementation schedules would need to be arranged with the Federal community's COTS vendors who provide core accounting systems. While these vendors are not directly limited by the Federal budget cycle to update the baseline functionality of their systems, implementation and systems configuration to meet specific agency circumstances does generally depend on funding that Federal agencies must reimburse to vendors. Even when COTS vendors add functionality to their systems, there are often delays in agency implementation of new versions of software, in order to accommodate the extensive lead time for testing and configuration. Accordingly, if all implementation activities proceed smoothly and funding is provided in a timely manner (following the budget cycle) and the FASAB desires implementation at the start of a fiscal year, we suggest implementation should not be required prior to FY 2021.

Lastly, of particular risk to Federal entities is a current environment that continues to pursue cost cutting in overhead functions, such as CFO activities and IT costs, making expansion of activities and new systems face stringent oversight. With the upcoming change in Executive Branch administrations, any appetite for funding such initiatives is unknown.

**Additional comments for the Board's consideration not related to specific questions 1-12;**

**Paragraph 63.** We disagree that expansion of sq. footage to add an additional room or floor to an already existing lease, should create a separate lease. GSA leasing practices would amend an existing lease to include the expansion space and adjust the new annual rent, typically within the existing lease term. GSA would not have negotiated a new lease with the lessor, but amended the existing lease, to require our business practices to change due to this accounting standard is not reasonable.

**Paragraph 66.** Provide clarifying guidance between the difference of lease modification found in par. 66 that results in potential gain, and par. 63 that requires lessee to create a separate lease. ....LEASE MODIFICATIONS / LESSEE TREATMENT OF LEASE MODIFICATIONS

*66. A lessee should account for a lease modification by remeasuring the lease liability. The lease asset should be adjusted by the difference between the remeasured liability and the liability immediately before the lease modification. However, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain.*

**GUIDANCE FOR RECOGNITION OF SPECIFIC INTRAGOVERNMENTAL LEASE TOPICS, Paragraph 79-86, as well as 90-94.** This includes such topics as lease incentives and lease concessions,.. why is this not in a general section? are these topics only relevant to intragovernmental leases? Please clarify.

We are concerned about the reduction for lease incentives received from the lessor. As defined in paragraph 82. *Lease Incentives – Lease incentives include lessor payments made to or on behalf of the lessee to entice the lessee to sign a lease. Lease incentives may include up-front cash payments to the lessee; for example, moving costs, termination fees to lessee's prior lessor, or lessor's assumption of the lessee's lease obligation under a different lease with another lessor.* Would such items as a warm lit shell credit provided by the lessor converted into tenant improvements, meet such definition? These tenant improvements are amortized in the annual rent typically over the noncancellable term of the lease. What are the journal entries to record such lease incentives, (par 83)? In instances that the lease meets the definition of right- to -use lease asset how would the Board expect recording of the lease incentives, in guidance paragraph 83 it states to recognize as reductions of lease rental expense by the lessee on a straight-line basis over the lease term, but there would not be a lease rental expense as the accounting treatment would have us recognize an asset and liability where monthly payments to the lessor are reduction of principal liability and recognition of interest expense accrued on the unliquidated liability.

We are also concerned with the accounting treatment of lease concessions. As described in paragraph 85. lease concessions should be recognized as reductions of lease rental expense by the lessee on a straight-line basis over the lease term. As noted for lease incentives, how would the Board expect recording of lease concessions for leases that meet the definition of right-to -use lease asset, as there would not be a lease rental expense as the accounting treatment would have us recognize an asset and liability, where monthly payments to the lessor are reduction of principal liability and recognition of interest expense accrued on the unliquidated liability.



Wendy M. Payne, Executive Director  
Federal Accounting Standards Advisory Board  
Mailstop 6H19  
441 G Street NW, Suite 6814  
Washington, D.C. 20548

Dear Ms. Payne:

GSA appreciates the opportunity to provide perspective on the Federal Accounting Standards Advisory Board (FASAB) Exposure Draft (ED), *Accounting for Leases*. Our assessment questions whether the effort poses more operational burdens than added value to our organization. In our statements below, we raise concerns about the context of the change and cost-benefit of implementation in our organization.

The purpose of private industry financial reporting and federal government financial reporting differ in some aspects for our stakeholders. In the federal space, we see our role as demonstrating stewardship and accountability of taxpayer dollars within applicable laws. This role is paramount because we understand that taxpayers assess our operations against our ability to meet mission, while private sector financial reporting is an indicator of an entity's financial prospects and future viability. We believe these differences in stakeholders and purpose of financial reporting must be considered when proposing accounting changes.

GSA anticipates significant effort and cost to comply with the standard, with little increase in value. Implementation would require a full inventory evaluation, reclassification of assets, value assessments, computation of financial impacts, and extensive financial system modification. Beyond initial assessments and changes, upholding the standard would require us to modify our business processes and audit compliance; increasing operational costs in a declining budgetary environment. Inversely, GSA sees no net gain to our financial statements by implementing the standard, seeing reporting changes as potentially misleading and not providing greater insight or better information to our stakeholders. As an aside, GSA already presents future minimum rental payment projections in footnotes to the financial statements, meeting the transparency intent of the proposed standard.

In summary, based on limited benefits and significant costs to implement the proposed standard, GSA recommends reevaluation of the Exposure Draft. We believe our accounting and reporting around leases meets the needs of our stakeholders.

GSA additionally endorses the Department of Defense's responses to FASAB's Leasing Exposure Draft, attached letter dated 05 January 2017.

Thank you for considering the Agency's comments. If you have any questions, please contact Bob Smalskas, Accounting and Financial Reporting Director on 202 357-9518.

Sincerely,



Kathy Hammer  
Director, Office of Financial Management

Enclosure



**Federal Accounting Standards Advisory Board**

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## **LEASES:**

AN AMENDMENT OF STATEMENT OF FEDERAL FINANCIAL ACCOUNTING STANDARDS  
(SFFAS) 5, ACCOUNTING FOR LIABILITIES OF THE FEDERAL GOVERNMENT AND  
SFFAS 6, ACCOUNTING FOR PROPERTY, PLANT, AND EQUIPMENT

### **Statement of Federal Financial Accounting Standards**

#### **Exposure Draft**

Written comments are requested by January 6, 2017

September 26, 2016

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## THE FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD

The Secretary of the Treasury, the Director of the Office of Management and Budget (OMB), and the Comptroller General of the United States, established the Federal Accounting Standards Advisory Board (FASAB or "the Board") in October 1990. FASAB is responsible for promulgating accounting standards for the United States government. These standards are recognized as generally accepted accounting principles (GAAP) for the federal government.

An accounting standard is typically formulated initially as a proposal after considering the financial and budgetary information needs of citizens (including the news media, state and local legislators, analysts from private firms, academe, and elsewhere), Congress, federal executives, federal program managers, and other users of federal financial information. The proposed standards are published in an exposure draft for public comment. In some cases, a discussion memorandum, invitation for comment, or preliminary views document may be published before an exposure draft is published on a specific topic. A public hearing is sometimes held to receive oral comments in addition to written comments. The Board considers comments and decides whether to adopt the proposed standard with or without modification. After review by the three officials who sponsor FASAB, the Board publishes adopted standards in a Statement of Federal Financial Accounting Standards. The Board follows a similar process for Statements of Federal Financial Accounting Concepts, which guide the Board in developing accounting standards and formulating the framework for federal accounting and reporting.

Additional background information is available from FASAB or its website:

- ["Memorandum of Understanding among the Government Accountability Office, the Department of the Treasury, and the Office of Management and Budget, on Federal Government Accounting Standards and a Federal Accounting Standards Advisory Board."](#)
- ["Mission Statement: Federal Accounting Standards Advisory Board"](#), [exposure drafts](#), [Statements of Federal Financial Accounting Standards and Concepts](#), [FASAB newsletters](#), and other items of interest are posted on FASAB's website at: [www.fasab.gov](http://www.fasab.gov) .

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## Federal Accounting Standards Advisory Board

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September 26, 2016

TO: ALL WHO USE, PREPARE, AND AUDIT FEDERAL FINANCIAL INFORMATION

Your comments on the exposure draft of a proposed Statement of Federal Financial Accounting Standards, entitled *Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment*, are requested. Specific questions for your consideration appear on page 6 but you are welcome to comment on any aspect of this proposal. If you do not agree with the proposed approach, your response would be more helpful to the Board if you explain the reasons for your position and any alternative you propose. Responses are requested by January 6, 2017.

All comments received by FASAB are considered public information. Those comments may be posted to FASAB's website and will be included in the project's public record.

Mail delivery is delayed by screening procedures. Therefore, please provide your comments in electronic form by e-mail to [fasab@fasab.gov](mailto:fasab@fasab.gov). If you are unable to e-mail your responses, we encourage you to fax the comments to (202) 512-7366. Alternatively, you may mail your comments to:

Wendy M. Payne, Executive Director  
Federal Accounting Standards Advisory Board  
Mailstop 6H19  
441 G Street, NW, Suite 6814  
Washington, DC 20548

We will confirm receipt of your comments. If you do not receive confirmation, please contact our office at 202.512.7350 to determine if your comments were received.

The Board's rules of procedure provide that one or more public hearings may be held on any exposure draft. No hearing has yet been scheduled for this exposure draft. Notice of the date and location of any public hearing on this document will be published in the Federal Register and in FASAB's newsletter.

Sincerely,

D. Scott Showalter  
Chairman

## EXECUTIVE SUMMARY

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### WHAT IS THE BOARD PROPOSING?

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The Board is proposing revisions to the existing federal lease accounting standards. The proposal would provide a comprehensive set of lease accounting standards to recognize federal lease activities in the reporting entity's general purpose federal financial reports and include appropriate disclosures.

The Board is proposing that federal lessees recognize a lease liability and a leased asset at the beginning of the lease, unless it is an intragovernmental lease or a short-term lease. A federal lessor would recognize a lease receivable and deferred revenue, unless it is an intragovernmental lease or a short-term lease.

### HOW WOULD THIS PROPOSAL IMPROVE FEDERAL FINANCIAL REPORTING AND CONTRIBUTE TO MEETING THE FEDERAL FINANCIAL REPORTING OBJECTIVES?

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The Board first addressed lease accounting during the development of Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of The Federal Government*, and SFFAS 6, *Accounting for Property, Plant, and Equipment*. At that time, the Board decided to use the high-level language on lease accounting from Financial Accounting Standards Board's (FASB) Statement of Financial Accounting Standards (SFAS) 13, *Accounting for Leases*. The Board chose to use this language as a placeholder until it was prepared to add lease accounting to its agenda as a separate project. Consequently the standards in SFFAS 5 and SFFAS 6 are minimal and only address the definition of a capital lease, the criteria for capital leases, and the measurement of a capital lease asset and liability.

The current lease accounting standards have been criticized for not making meaningful distinctions between types of leases and not providing sufficient guidance to the federal community. Additionally, the current federal standards are based on FASB's lease accounting standards which have since been revised.

This lease proposal would improve the existing lease accounting standards in SFFAS 5 and SFFAS 6 by

- providing relevant and meaningful financial information needed by federal financial statement users and
- providing comprehensive lease standards that appropriately address the various lease transactions/activities of the federal community.

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## QUESTIONS FOR RESPONDENTS

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The Board encourages you to become familiar with all proposals in the Statement before responding to the questions in this section. In addition to the questions below, the Board also would welcome your comments on other aspects of the proposed Statement. Because the proposals may be modified before a final Statement is issued, it is important that you comment on proposals that you favor as well as any that you do not favor. Comments that include the reasons for your views will be especially appreciated.

The Board believes that this proposal would improve federal financial reporting and contribute to meeting the Federal financial reporting objectives. The Board has considered the perceived costs associated with this proposal. In responding, please consider the expected benefits and perceived costs and communicate any concerns that you may have in regard to implementing this proposal.

The questions in this section are available in a Word file for your use at [www.fasab.gov/documents-for-comment/](http://www.fasab.gov/documents-for-comment/). Your responses should be sent by e-mail to [fasab@fasab.gov](mailto:fasab@fasab.gov). If you are unable to respond by e-mail, please fax your responses to (202) 512-7366. Alternatively, you may mail your responses to:

Wendy M. Payne, Executive Director  
Federal Accounting Standards Advisory Board  
Mailstop 6H19  
441 G Street, NW, Suite 6814  
Washington, DC 20548

All responses are requested by **January 6, 2017**.

- Q1. The Board is proposing to define a **lease** as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. The current lease standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, do not specifically define a lease. SFFAS 5 and SFFAS 6 only define a capital lease as a “lease that transfers substantially all the benefits and risks of ownership to the lessee.” The Board believes that the more concise definition being proposed is broad enough to capture the diversity of federal leasing activities. The proposed lease definition is presented in paragraph 9 and further explained in paragraph A15.

**Do you agree or disagree with the proposed definition of lease presented in paragraph 9 and further explained in paragraph A15? Please provide the rationale for your answer.**

- Q2. The Board is proposing that the **lease term** be determined as the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period) plus each option period if it is probable, based on all

relevant factors, that the lessee will exercise that option to extend the lease. The lease term proposal also provides guidance on the noncancelable period and on how specific provisions (such as fiscal funding/cancellation clauses and month-to-month lease holdovers) should be applied. The proposed lease term requirements are presented in paragraphs 14 – 18 and further explained in paragraphs A16 - A18.

**Do you agree or disagree with the proposed guidance on determining the lease term as presented in paragraphs 14 - 18 and further explained in A16 - A18? Please provide the rationale for your answer.**

- Q3. The Board is proposing that at the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment right-to-use lease asset (the lease asset), except for intragovernmental and short-term leases. The proposed lease recognition requirements are presented in paragraph 19.

**Do you agree or disagree with the proposed lessee recognition of a lease at the beginning of the lease term as presented in paragraph 19? Please provide the rationale for your answer.**

- Q4. The Board is proposing that a lessee should measure the **lease liability** initially at the present value of payments to be made for the lease term. In addition, the measurement of the lease liability should include the several types of payments that might be required by a lease. The proposed lease liability measurement and recognition requirements are presented in paragraphs 21 – 29 and further explained in paragraphs A20 - A21.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease liability as presented in paragraphs 21 - 29 and further explained in paragraphs A20 - A21? Please provide the rationale for your answer.**

- Q5. The Board is proposing that the future lease payments should be discounted using **the rate the lessor charges the lessee**, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the **lessee's incremental borrowing rate**<sup>1</sup> (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used. The specific proposed requirement is presented in paragraph 23.

a. **Do you agree or disagree that the rate the lessor charges the lessee, which may be the interest rate implicit in the lease, should be used to measure the future lease payments as presented in paragraph 23? Please provide the rationale for your answers.**

b. **Do you agree or disagree that the lessee's incremental borrowing rate should be used to measure the future lease payments when the lessor rate cannot be reasonably estimated by the lessee as presented in paragraph 23? Please provide the rationale for your answers.**

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<sup>1</sup> A federal lessee's incremental borrowing rate would be the Department of the Treasury borrowing rate for securities of similar maturity to the term of the lease unless the entity has its own borrowing authority.

Q6. The Board is proposing that the lessee should remeasure the lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability. The Board is also proposing that the lease asset should generally be adjusted by the same amount when the corresponding lease liability is remeasured based on those changes. Additionally, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain. The proposed lessee requirements for remeasurement are presented in paragraphs 25 – 29, 33, and further explained in paragraph A19.

- a. **Do you agree or disagree with the circumstances when the lessee must remeasure the lease liability as presented in paragraph 25? Please provide the rationale for your answer.**
- b. **Would the requirements triggering remeasurement cause undue costs? Please provide the rationale for your answer.**
- c. **Do you agree or disagree with the effect of the remeasurement on the carrying value of the lease asset as presented in paragraph 33 and further explained in paragraph A19? Please provide the rationale for your answer.**

Q7. The Board is proposing that a lessee should measure the **lease asset** initially as the sum of (1) the amount of the initial measurement of the lease liability, (2) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (3) initial direct costs that are ancillary charges necessary to place the lease asset into service. The proposed lessee lease asset measurement and recognition requirements are presented in paragraphs 30 – 34 and further explained in paragraph A22.

**Do you agree or disagree with the proposed lessee measurement and recognition of the lease asset as presented in paragraphs 30 - 34 and further explained in paragraph A22? Please provide the rationale for your answer.**

Q8. The Board is proposing that at the beginning of the lease term, a lessor should recognize a **lease receivable and deferred revenue**, except for intragovernmental and short-term leases. The proposed requirements for the measurement and recognition of the lessor lease receivable and deferred revenue are presented in paragraphs 36 – 48 and further explained in paragraphs A23 - A24.

**Do you agree or disagree with the proposed lessor measurement and recognition of the lease receivable and deferred revenue as presented in paragraphs 36 - 48 and further explained in paragraphs A23 - A24? Please provide the rationale for your answer.**

Q9. The Board is proposing to define a **short-term lease** as a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. The proposed requirements for the measurement and recognition of a short-term lease are presented in paragraphs 59 – 61 and further explained in paragraph A25.



**Do you agree or disagree with the proposed definition and measurement and recognition of a short-term lease as presented in paragraphs 59 - 61 and further explained in paragraph A25? Please provide the rationale for your answer.**

- Q10. The Board is proposing to establish distinct standards for **intragovernmental leases**. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, *Reporting Entity*. The proposed requirements for the measurement, recognition, and disclosure of intragovernmental leases are presented in paragraphs 75 – 95 and further explained in paragraphs A26 - A29.

**Do you agree or disagree with the proposed definition, measurement, recognition, and disclosures of intragovernmental leases as presented in paragraphs 75 - 95 and further explained in paragraphs A26 - A29? Please provide the rationale for your answer.**

- Q11. The Board is proposing that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. The proposed implementation requirements are presented in paragraphs 99-100.

**Do you agree or disagree with the proposed prospective implementation approach as presented in paragraphs 99 - 100? Please provide the rationale for your answer.**

- Q12. The Board is proposing that the requirements of this Statement be effective for reporting periods beginning after September 30, 2018. The proposed effective date is presented in paragraph 101.

**Do you agree or disagree with the proposed effective date as presented in paragraph 101? Please provide the rationale for your answer.**



## INTRODUCTION

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### PURPOSE

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1. The Federal Accounting Standards Advisory Board (FASAB or “the Board”) undertook this project primarily because
  - a. the current lease accounting standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, have been criticized as ineffective because they do not make meaningful distinctions between capital and operating leases based on the substance of lease transactions, and
  - b. the lease accounting standards in SFFAS 5 and SFFAS 6 are based on lease accounting standards from Financial Accounting Standards Board (FASB) which have since been amended. In addition, existing FASAB standards are not comprehensive and do not provide meaningful information on federal leasing activities.
2. SFFAC 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*, defines both an asset and liability. In that concepts statement an asset is defined as “a resource that embodies economic benefits or services that the federal government controls.” A liability is defined as “a present obligation of the federal government to provide assets or service to another entity at a determinable date, when a specific event occurs, or on demand.” The SFFAC 5 definitions only address whether the asset or liability exists and not how it should be measured or whether or when it should be recognized. The current leasing activities/transactions of federal entities should be evaluated against these definitions to ensure proper measurement and recognition. This proposal seeks to adopt the most current concepts so that the accounting principles for leases provide comprehensive guidance for consistent reporting.
3. This Statement is intended to improve federal financial reporting for leases by requiring concise, meaningful, and transparent information about the cost and related asset and liability to improve users’ understanding of the operating performance of the federal government and component entities.

### MATERIALITY

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4. The provisions of this Statement need not be applied to immaterial items. The determination of whether an item is material depends on the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement.

## PROPOSED STANDARDS

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### SCOPE

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5. This Statement applies to federal entities that present general purpose federal financial reports, including the consolidated financial report of the U.S. Government (CFR), in conformance with generally accepted accounting principles, as defined by paragraphs 5 through 8 of Statement of Federal Financial Accounting Standards (SFFAS) 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.
6. For purposes of applying this Statement, a **lease**<sup>2</sup> is defined as a contract or agreement that conveys the right to use a nonfinancial asset<sup>3</sup> (the underlying asset) for a period of time in an exchange transaction. Leases include contracts or agreements that, although not explicitly identified as leases, meet the definition of a lease. This definition does not include contracts or agreements for services unless that contract or agreement also conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.
7. This Statement amends the lease accounting standards in SFFAS 5, *Accounting for Liabilities of the Federal Government*, and SFFAS 6, *Accounting for Property, Plant, and Equipment*. This Statement also establishes distinct standards for **intragovernmental leases**.
8. This Statement does not apply to leases of federal natural resources as defined in Technical Bulletin (TB) 2011-1, *Accounting for Federal Natural Resources Other than Oil* and leases of federal oil and gas resources as defined in SFFAS 38, *Accounting for Federal Oil and Gas Resources*.

### DEFINITIONS

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9. **Lease** – A lease is a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.
10. **Intragovernmental Lease** – An intragovernmental lease is a lease occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, *Reporting Entity*.<sup>4</sup>
11. **Lease Option Periods** – Lease option periods are additional lease periods beyond the initial lease term. The options may be included in the initial lease or may be agreed to later in the lease term.

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<sup>2</sup> Terms defined in the Glossary are shown in bold-face the first time they appear.

<sup>3</sup> Examples of nonfinancial assets include land, buildings, vehicles, equipment, internal use software, and intangible assets. Examples of financial assets include cash, investments, and receivables.

<sup>4</sup> See SFFAS 47, *Reporting Entity*, par. 38-42.

12. **Initial Direct Costs** – Initial direct costs are costs that are directly attributable to negotiating and arranging a lease or portfolio of leases and would not have been incurred without entering into the lease.
13. **Short-Term Lease** – A short-term lease is a lease that, at the beginning of the lease, has a maximum possible term under the contract or arrangement of 24 months or less, including any options to extend, regardless of their probability of being exercised.

## STANDARDS FOR NON-INTRAGOVERNMENTAL LEASES

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### LEASE TERM

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14. The lease term is the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period), plus each option period if it is **probable**, based on all relevant factors, that the lessee will exercise that option to extend the lease.
15. The noncancelable period is the shorter of
- a. the initial lease period, before considering renewal options for additional periods;
  - b. the period of the lease preceding an option for the lessee to terminate the lease if it is probable, based on all relevant factors, that the lessee will exercise that option to terminate; or
  - c. the period of the lease preceding a point at which either the lessor only or both the lessee and the lessor have an option to terminate the lease, regardless of the probability of termination.<sup>5</sup>
16. In determining the lease term, the following specific provisions should be applied:
- a. When the noncancelable period is less than the initial lease term (due to options to terminate discussed in par. 15b and 15c) there should be no option periods added to the noncancelable period in calculating the lease term.
  - b. Provisions that allow for termination of a lease due to (a) purchase of the underlying asset, (b) payment of all sums due, or (c) default on payments are not considered options to terminate.
  - c. A fiscal funding or cancellation clause (a clause that allows federal lessees to cancel a lease agreement, typically on an annual basis, if funds for the lease payments are not appropriated) should be considered in determining the lease term only when it is probable that the clause will be exercised.

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<sup>5</sup> Periods for which either the lessor only or both the lessee and the lessor have an option to terminate the lease are cancelable periods and are excluded from the lease term.

- d. Month-to-month lease holdovers, also referred to as rolling lease extensions, or any lease that continues into a holdover period until a new contract or agreement is signed should be considered cancelable because either the lessee or lessor could cancel the lease at any time. These holdover periods should be excluded from the lessee's lease liability and the lessor's lease receivable.<sup>6</sup>
17. At the beginning of a lease, lessors and lessees should assess all factors relevant to the likelihood that the lessee will exercise options, whether these factors are contract/agreement based, underlying asset based, market based, or federal specific. The assessment often will require the consideration of a combination of these interrelated factors. Examples of factors to consider include, but are not limited to, the following:
- a. A significant economic incentive, such as contractual terms and conditions for the option periods that are favorable compared with current market rates
  - b. A significant economic disincentive, such as costs to terminate the lease and sign a new lease (for example, negotiation costs, relocation costs, abandonment of significant leasehold improvements, costs of identifying another suitable underlying asset, costs associated with returning the underlying asset in a contractually specified condition or to a contractually specified location, or a substantial cancellation penalty)
  - c. The lessee's history of exercising renewal or termination options
  - d. The extent to which the lease asset is considered mission critical to the federal entity
18. Lessors and lessees should reassess the lease term only if the lessee does either of the following:
- a. Elects to exercise an option even though the lessor or lessee had previously determined that it was not probable that the lessee would exercise that option
  - b. Does not elect to exercise an option even though the lessor or lessee had previously determined that it was probable that the lessee would exercise that option

## RECOGNITION AND MEASUREMENT FOR LESSEES

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19. At the beginning of the lease term, a lessee should recognize a lease liability and a property, plant, and equipment (PP&E)<sup>7</sup> right-to-use lease asset (hereinafter referred to as the lease asset), except as provided in paragraph 20 and paragraphs 59-61 (short-term leases).

<sup>6</sup> SFFAS 1, *Accounting for Selected Assets and Liabilities*, applies to any related accounts payable or accounts receivable amounts.

<sup>7</sup> The lease asset should be classified as PP&E unless the underlying asset is not PP&E. In those instances, such assets should be classified with the underlying asset.

## LEASES THAT TRANSFER OWNERSHIP

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20. A lease contract/agreement that transfers ownership of the underlying asset to the lessee at or before the end of the lease, and does not contain termination options (see par. 14 - 15), should be reported as a purchase of that asset.<sup>8</sup>

## LEASE LIABILITY

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21. A lessee should measure the lease liability initially at the present value of payments to be made for the lease term. Measurement of the lease liability should include the following types of payments that might be required by a lease:
- a. Fixed payments, less any lease incentives (such as a cash payment or reimbursement of moving costs) receivable from the lessor
  - b. Variable lease payments that depend on an index or a rate (such as the Consumer Price Index or a market interest rate), initially measured using the index or rate as of the beginning of the lease
  - c. Variable lease payments that are fixed in-substance as described in paragraph 22
  - d. Amounts that are probable of being required to be paid by the lessee under residual value guarantees
  - e. The exercise price of a purchase option if it is probable that the lessee will exercise that option
  - f. Payments for penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease or a fiscal funding or cancellation clause
  - g. Any other payments that are probable of being required based on an assessment of all relevant factors
22. Variable payments based on future performance of the lessee or usage of the underlying asset should not be included. Rather, these variable payments should be recognized as an expense in the statement of net cost in the period in which those payments are incurred. However, any component of these variable payments that is fixed in-substance should be included in the lease liability. An example is a lease payment based on a percentage of sales or usage but with a required minimum amount to be paid. That required minimum payment is fixed in-substance.
23. The future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the rate cannot be reasonably estimated by the lessee, the **lessee's incremental borrowing rate**<sup>9</sup> (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used.

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<sup>8</sup> See SFFAS 6, *Accounting for Property, Plant, and Equipment*, par. 26.

<sup>9</sup> A federal lessee's incremental borrowing rate would be the Treasury borrowing rate for securities of similar maturity to the term of the lease unless the entity has its own borrowing authority.

24. At subsequent financial reporting dates, the lessee should calculate the amortization of the discount on the lease liability and recognize that amount as interest expense for the period. Any payments made should be allocated first to the accrued interest liability and then to the lease liability.
25. The lessee should remeasure the lease liability at subsequent financial reporting dates if any of the following changes have occurred and are expected to significantly affect the amount of the lease liability:
- a. There is a change in the lease term due to a reassessment (see par. 18), a modification (see par. 66), or a termination (see par. 64).
  - b. An assessment of all relevant factors indicates that the likelihood of a residual value guarantee being paid has changed from probable to not probable, or vice versa.
  - c. An assessment of all relevant factors indicates that the likelihood of a purchase option being exercised has changed from probable to not probable, or vice versa.
  - d. There is a change in the estimated amounts for payments already included in the liability.
  - e. There is a change in the interest rate the lessor charges the lessee, if used as the initial **discount rate**.
26. If a lease liability is remeasured for any of the changes in paragraph 25, the liability also should be remeasured for any change in an index or rate used to determine variable lease payments if that change in the index or rate is expected to significantly affect the amount of the liability. A lease liability is not required to be remeasured solely for a change in an index or rate used to determine variable lease payments.
27. The lessee also should update the discount rate as part of the remeasurement if any of the following changes have occurred and are expected to significantly affect the amount of the lease liability:
- a. There is a change in the lease term due to a reassessment (see par. 18), a modification (see par. 66), or a termination (see par. 64).
  - b. An assessment of all relevant factors indicates that the likelihood of a purchase option being exercised has changed from probable to not probable, or vice versa.
28. A lease liability is not required to be remeasured, nor is the discount rate required to be reassessed solely for a change in the lessee's incremental borrowing rate.
29. If the discount rate is required to be updated based on the provisions in paragraph 27, the discount rate should be based on the revised rate the lessor charges the lessee at the time the discount rate is updated. If that rate cannot be readily determined, the lessee's incremental borrowing rate should be used.

## LEASE ASSET

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30. A lessee should initially measure the lease asset as the sum of the following:
- a. The amount of the initial measurement of the lease liability (see par. 21)

- b. Lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor
  - c. Initial direct costs that are ancillary charges necessary to place the lease asset into service
- 31. The lease asset should be amortized in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset, except as provided in paragraph 32. The amortization of the lease asset should be reported as amortization expense.
- 32. The presence of a bargain purchase option in a lease contract/agreement is not equivalent to a provision that transfers ownership of the underlying asset; therefore a bargain purchase option should be treated as any other purchase option included in a lease. If the lease contains a purchase option that the lessee has determined is probable of being exercised, the lease asset should be amortized over the useful life of the underlying asset. In this circumstance, if the underlying asset is non-depreciable, such as land, then the lease asset should not be amortized.
- 33. The lease asset generally should be adjusted by the same amount when the corresponding lease liability is remeasured based on paragraphs 25–29. However, if this change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain.
- 34. The presence of impairment indicators (described in par. 12 of SFFAS 44, *Accounting for Impairment of General Property, Plant, and Equipment Remaining in Use*) with respect to the underlying asset may result in a change in the manner or duration of use of the lease asset. The change in the manner or duration of use of the lease asset is an indicator that the lease asset may be impaired. The period for which the underlying asset has less usable capacity should be the relevant factor(s) in determining the magnitude of the decline in service utility of the lease asset. If a lease asset is impaired, it should be reduced first for any change in the corresponding lease liability. Any remaining amount should be recognized as an impairment.<sup>10</sup>

## DISCLOSURE REQUIREMENTS FOR LESSEES

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- 35. A lessee should disclose the following about its lease activities (which may be grouped for purposes of disclosure), other than short-term leases:
  - a. A general description of its leasing arrangements, including:
    - i. the basis, terms, and conditions on which variable lease payments not included in the lease liability are determined
    - ii. the existence, terms, and conditions of residual value guarantees provided by the lessee

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<sup>10</sup> See SFFAS 44, *Accounting for Impairment of General Property, Plant, and Equipment Remaining in Use*, par. 18 – 25.

- b. The total amount of lease assets, and the related accumulated amortization, to be disclosed separately from other PP&E assets
- c. The amount of lease expense recognized for the period for variable lease payments not previously included in the lease liability
- d. Principal and interest requirements to maturity, presented separately, for the lease liability for each of the five subsequent years and in five-year increments thereafter
- e. The amount of the annual lease expense and the discount rate used to calculate the lease liability

## RECOGNITION AND MEASUREMENT FOR LESSORS

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36. At the beginning of the lease term, a lessor should recognize a lease receivable and a deferred revenue, except as provided in paragraph 37 and paragraphs 59–61 (short-term leases). Any initial direct costs incurred by the lessor should be reported as an expense of the period.

### LEASES THAT TRANSFER OWNERSHIP

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37. A lease contract/agreement that transfers ownership of the underlying asset to the lessee at or before the end of the lease, and does not contain termination options (see par. 14) should be reported as a financed sale of that asset.

### LEASE RECEIVABLE

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38. A lessor should measure the lease receivable initially at the present value of lease payments to be received for the lease term, reduced by any provision for uncollectible amounts. Measurement of the lease receivable should include the following types of payments that might be required by a lease:
- a. Fixed payments
  - b. Variable payments that depend on an index or a rate (such as the Consumer Price Index or a market interest rate), initially measured using the index or rate as of the beginning of the lease
  - c. Portions of variable payments that are fixed in substance (as described in par. 39)
  - d. Residual value guarantees that are fixed payments in substance (as described in par. 40).
39. Variable payments based on future performance of the lessee or usage of the underlying asset should not be included in the receivable. Those payments should be recognized as revenue in the period to which those payments relate. However, any component of those variable payments that is fixed in substance should be included in the lease receivable. For example, if a lease payment is based on a percentage of sales but has a required minimum



payment, that required minimum is a fixed payment in substance. Similarly, a residual value guarantee is an in-substance fixed payment if it stipulates the underlying asset will be sold at the end of the lease term, with the lessee assuming a liability for any shortfall if the sales price is less than an agreed-upon minimum amount.

40. Amounts to be received under residual value guarantees (that are not fixed in substance) should be recognized as a receivable and revenue when (a) a guarantee payment is required (as agreed to by the lessee and lessor) and (b) the amount can be reasonably estimated. Amounts to be received for the exercise price of a purchase option or penalties for lease termination should be recognized as a receivable and revenue when those options are exercised.
41. The future lease payments to be received should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease. Lessors are not required to apply imputed interest but may do so as a means of determining the rate implicit in the lease.
42. At subsequent financial reporting dates, the lessor should calculate the amortization of the discount on the receivable and report that amount as interest revenue for the period. It should be calculated so as to produce a constant periodic rate of return on the receivable. Any payments received should be allocated first to the accrued interest receivable and then to the lease receivable.
43. The lessor should remeasure the lease receivable and update the discount rate at subsequent financial reporting dates if either of the following changes have occurred and are expected to significantly affect the amount of the receivable:
  - a. There is a change in the lease term.
  - b. There is a change in the rate the lessor charges the lessee.
44. If a lease receivable is remeasured for either of the changes in paragraph 43, the receivable also should be remeasured for any change in an index or rate used to determine variable lease payments if that change in the index or rate is expected to significantly affect the amount of the receivable. A lease receivable is not required to be remeasured solely for a change in an index or rate used to determine variable lease payments.
45. If the discount rate is updated based on the provisions in paragraph 43, the receivable should be discounted using the revised rate.

## DEFERRED REVENUE

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46. A lessor should measure the deferred revenue at the initial value of the lease receivable, less any provision for uncollectible amounts (see par. 38), plus the amount of any payments received at or prior to the beginning of the lease that relate to future periods (for example, the final month's rent). A lessor subsequently should recognize deferred revenue in a systematic and rational manner over the term of the lease.

47. The deferred revenue should generally be adjusted using the same amount as the change resulting from the remeasurement of the lease receivable as discussed in paragraphs 43-44.

## UNDERLYING ASSET

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48. A lessor should **not** derecognize the asset underlying the lease. A lessor should continue to apply other applicable guidance to the underlying asset, including depreciation and impairment. However, if the lease agreement requires the lessee to return the asset in its original or enhanced condition, a lessor should not depreciate the asset during the lease term.

## DISCLOSURES FOR LESSORS

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49. A lessor should disclose the following about its lease activities (which may be grouped for purposes of disclosure), other than short-term leases:
- a. A general description of its leasing arrangements, including the basis, terms, and conditions on which any variable lease payments not included in the lease receivable are determined
  - b. The carrying amount of assets on lease or held for leasing, by major classes of assets, and the amount of accumulated depreciation
  - c. The total amount of revenue (for example, lease revenue, interest revenue, and any other lease-related revenue) recognized in the reporting period from leases
  - d. The amount of revenue recognized in the reporting period for variable lease payments and other payments not previously included in the lease receivable, including revenue related to residual value guarantees and termination penalties.
50. In addition to the disclosures in paragraph 49, if a federal entity's principal ongoing operations consist of leasing assets through the use of non-intragovernmental leases, the federal entity should disclose a schedule of future lease payments that are included in the lease receivable, showing principal and interest, for each of the five subsequent years and in five-year increments thereafter.

## CONTRACT/AGREEMENTS WITH MULTIPLE COMPONENTS

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51. Lessors and lessees may enter into one contract/agreement that contains multiple components, such as a contract/agreement that contains both a lease component and a nonlease component, or a lease that contains multiple underlying assets.
52. If a lessor or lessee enters into a contract/agreement that contains both a lease (such as the right to use a building) and a nonlease component (such as a maintenance services for the building), the federal entity should account for the lease and nonlease components as separate contract/agreements, unless the contract/agreement meets the exception in paragraph 55.b. or paragraph 55.c.

53. If a lease involves multiple underlying assets, lessors and lessees should account for each underlying asset as a separate lease component if the assets have different lease terms. The provisions of this paragraph should be applied unless the contract/agreement meets the exception in paragraph 55.b or paragraph 55.c
54. To allocate the consideration required under the contract/agreement to the different components, lessors and lessees should first use any prices for individual components that are included in the contract/agreement, if they are reasonable based on other observable stand-alone prices. Stand-alone prices are those that would be paid or received if the same or similar assets were leased or if the same or similar nonlease components (such as services) were contracted individually. Some contract/agreements provide discounts for bundling multiple leases or lease and nonlease components together in one contract/agreement. These discounts may be taken into account when determining whether individual component prices are reasonable. For example, if the individual component prices are each discounted by the same percentage from normal market prices, those component prices would be considered reasonable.
55. If a contract/agreement does not include prices for individual components, or if those prices are not reasonable based on other observable stand-alone prices, lessors and lessees should do the following, unless the components as a whole are insignificant:
- a. If observable stand-alone prices are readily available for *all* components, the federal entity should allocate the consideration based on the relative values of the observable stand-alone prices.
  - b. If observable stand-alone prices are readily available for *some* (but not all) components, the federal entity should allocate the observable stand-alone price to each component for which it is readily available. The federal entity may (1) estimate the allocation of the remaining consideration to the remaining components or (2) account for the remaining components as a single lease unit.
  - c. If observable stand-alone prices are not readily available for *any* of the components, the federal entity may (1) estimate the prices for each component or (2) account for the entire contract/agreement as a single lease unit.
56. When multiple components are accounted for as a single lease unit, as provided for in paragraphs 55.b. and 55.c., the accounting for that unit should be based on the primary lease component within that unit. For example, the primary lease component's lease term should be used for the unit if the lease components have different lease terms.

## CONTRACT/AGREEMENT COMBINATIONS

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57. Contract/agreements that are entered into at or near the same time with the same counterparty should be considered to be part of the same lease contract/agreement if either of the following criteria is met:
- a. The contract/agreements are negotiated as a package with a single objective.

- b. The amount of consideration to be paid in one contract/agreement depends on the price or performance of the other contract/agreement.

58. If multiple contract/agreements are determined to be part of the same lease contract/agreement, that lease should be evaluated in accordance with the guidance on contract/agreements with multiple components in paragraphs 51–56.

## SHORT-TERM LEASES

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59. A short-term lease is a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised. For a lease that is cancelable by either the lessee or the lessor, such as a month-to-month lease or a year-to-year lease, the maximum possible term is the noncancelable period, including any notice periods. For a lease that is cancellable only by the lessee, the maximum possible term should be evaluated under the requirements of the lease term as defined in paragraph 14.

### LESSEE TREATMENT OF SHORT-TERM LEASES

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60. A lessee should recognize short-term lease payments as expense based on the payment provisions of the contract/agreement. The lessee should not apply the recognition and measurement requirements of paragraphs 19–35 but should recognize an asset if payments are made in advance of the period to which they relate, or a liability for rent due if payments are made subsequent to that period. The lessee should recognize any rent holiday period (for example, one or more months free) as reductions of lease rental expense on a straight-line basis over the lease term.

### LESSOR TREATMENT OF SHORT-TERM LEASES

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61. A lessor should recognize short-term lease payments as revenue based on the payment provisions of the contract/agreement. The lessor should not apply the recognition and measurement requirements of paragraphs 36–50 but should recognize a liability if payments are received in advance of the period to which they relate, or an asset for rent due if payments are received subsequent to that period. The lessor should recognize any rent holiday period (for example, one or more months free) as reductions of lease rental income on a straight-line basis over the lease term.

## LEASE TERMINATIONS AND MODIFICATIONS

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62. A lease contract/agreement may be amended while it is in effect. Examples of amendments include a change in consideration, a lengthening or shortening of the lease term (see par. 25 and 43), or adding or removing an underlying asset. An amendment to a lease contract/agreement should be considered a lease modification unless the lessee's right to use the underlying asset decreases. If the lessee's right to use the underlying asset decreases (for example, the lease term is shortened or the number of underlying assets is reduced), that change should be accounted for as a partial lease termination (see par. 64 - 65).

63. If a lease modification gives the lessee an additional right to use an underlying asset that was not included in the original lease and provides a price comparable to its stand-alone price (in the context of that particular contract/agreement), both the lessee and the lessor should account for that additional portion of the modified lease as a new lease, separate from the original portion of the lease.

## LEASE TERMINATIONS

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### LESSEE TREATMENT OF LEASE TERMINATIONS

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64. A lessee generally should account for the full or partial termination of a lease by reducing the carrying values of the lease asset and lease liability and recognizing a gain or loss for the difference. However, if the lease is terminated as a result of the lessee purchasing the underlying asset from the lessor, the lease asset should be reclassified to the appropriate class of owned asset. The lease liability should be changed to reflect only those payments yet to be made, and that change should be reflected in the cost of the purchased asset.

### LESSOR TREATMENT OF LEASE TERMINATIONS

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65. A lessor should account for the full or partial termination of a lease by reducing the carrying values of the lease receivable and related deferred revenue and recognizing a gain or loss for the difference. If the lease is terminated as a result of the lessee purchasing an underlying asset from the lessor, the carrying value of the underlying asset also should be derecognized and included in the calculation of any resulting gain or loss.

## LEASE MODIFICATIONS

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### LESSEE TREATMENT OF LEASE MODIFICATIONS

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66. A lessee should account for a lease modification by remeasuring the lease liability. The lease asset should be adjusted by the difference between the remeasured liability and the liability immediately before the lease modification. However, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the flows statement as a gain.

### LESSOR TREATMENT OF LEASE MODIFICATIONS

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67. A lessor should account for a lease modification by remeasuring the lease receivable. The deferred revenue should be adjusted by the difference between the remeasured receivable and the receivable immediately before the lease modification. However, if the change relates to payments for the current period, the change should be recognized in the flows statement for the current period as revenue.

## SUBLEASES

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68. A sublease involves three parties: the original lessor, the original lessee (who also is the lessor in the sublease), and the new lessee. The original lessor should continue to apply the general lessor guidance. The federal entity that is the original lessee and becomes the lessor in the sublease should account for the original lease and the sublease as two separate transactions, as a lessee and a lessor, respectively. Those two separate

transactions should not be offset against one another. The new lessee should apply the general lessee guidance.

69. The original lessee (and now the lessor in a sublease) should include the sublease in its disclosure of the general description of lease arrangements. Its lessor transactions related to subleases should be disclosed separately from its lessee transactions related to the original lease.

## SALE-LEASEBACK TRANSACTIONS

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70. Sale-leaseback transactions involve the sale of an underlying asset by the owner and a lease of the property back to the seller. A sale-leaseback transaction should include an exchange transaction sale<sup>11</sup> in order to be eligible for sale-leaseback accounting. A sale-leaseback transaction that does not include an exchange transaction sale should be accounted for as a borrowing by both the seller-lessee and the buyer-lessor.
71. The sale and leaseback portions of a sale-leaseback transaction should be accounted for as two separate transactions – a sale transaction and a lease transaction – except that the difference between the carrying value of the capital asset that was sold and the net proceeds from the sale should be reported as a deferred revenue or deferred expense to be recognized in the flow statement over the term of the lease. However, if the leaseback portion of the transaction qualifies as a short-term lease, any gain or loss on the sale should be recognized immediately.
72. A sale-leaseback transaction is considered to have off-market terms if there is a significant difference between (a) the sales price and the estimated fair value of the asset or (b) the present value of the contractual lease payments and the estimated present value of what the lease payments for that asset would be at a market price, whichever of the two differences is more readily determinable. The difference should be reported based on the substance of the transaction (for example, as a borrowing, a nonexchange transaction, or an advance lease payment) rather than as a part of the sales-leaseback transaction. The following are examples of off-market terms:
- a. A transaction has a sale price and lease payments that are both significantly higher than market
  - b. A transaction has a sale price that is significantly higher than market but the lease payments are at or below market
  - c. A transaction has a sale price that is significantly lower than market.
73. A seller-lessee should disclose the terms and conditions of sale-leaseback transactions in addition to the disclosures required of a lessee (par. 35). A buyer-lessor should provide the disclosures required of a lessor (par. 49).

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<sup>11</sup> See SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, par. 295.

## LEASE-LEASEBACK TRANSACTIONS

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74. In a lease-leaseback transaction, an asset is leased by one party (first party) to another party and then leased back to the first party. The leaseback part of the transaction may involve an additional asset (such as leasing a building that has been constructed by a developer on land owned by and leased back to a federal entity) or only a portion of the original asset (such as leasing back only one floor of a building to the owner). A lease-leaseback transaction should be accounted for as a net transaction. Both parties to a lease-leaseback transaction should disclose the gross amounts of each portion of the transaction.

## STANDARDS FOR INTRAGOVERNMENTAL LEASES

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75. This section describes the overall recognition, measurement, and disclosure requirements for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, *Reporting Entity*. Any lease that meets the definition of an intragovernmental lease would be required to follow the accounting guidance described in paragraphs 77 – 95 below.

### INTRAGOVERNMENTAL LEASES – LESSEE ACCOUNTING

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76. The following sections articulate the general recognition guidance for lessees of intragovernmental leases and detailed recognition guidance regarding several specific intragovernmental lease topics, as well as disclosure guidance.

#### RECOGNITION AND MEASUREMENT

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##### GENERAL GUIDANCE FOR RECOGNITION OF INTRAGOVERNMENTAL LEASES<sup>12</sup>

77. A lessee should recognize lease payments, including lease-related operating costs (for example, maintenance, utilities, taxes, etc.) paid to the lessor, as expenses based primarily on the payment provisions of the lease. A lessee would not recognize a lease asset and a corresponding liability for an intragovernmental lease. Accordingly, a lessee would not recognize amortization expense related to a lease asset or interest expense on a lease liability.
78. Recognition should be based on the payment provisions of the lease. Prepaid rent or a payable for rent due should be recognized as an asset or liability, respectively, and an expense should be recognized in the appropriate period based on the specifics of the lease provisions.

##### GUIDANCE FOR RECOGNITION OF SPECIFIC INTRAGOVERNMENTAL LEASE TOPICS

79. Rental Increases – Rental increases may be fixed in the lease and take place with the passage of time (for example, be based on such factors as anticipated increases in costs or anticipated appreciation in property values, but the amount of the increase is specified in the lease) or they may be contingent on future events.
80. Contingent rental increases are based on changes in specific economic factors, for example, future activity levels or future inflation (for example, tied to a specific economic indicator where the specific amount of the change is not known).

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<sup>12</sup> SFFAS 4, *Managerial Cost Accounting Standards and Concepts*, par. 105-115 (as amended by SFFAS 30), continue to apply for non-reimbursed or under reimbursed intragovernmental lease arrangements.



81. If the lease provides for rental increases, a lessee should recognize the expense in the period of the increase as provided in the lease.<sup>13</sup>
82. Lease Incentives – Lease incentives include lessor payments made to or on behalf of the lessee to entice the lessee to sign a lease. Lease incentives may include up-front cash payments to the lessee; for example, moving costs, termination fees to lessee’s prior lessor, or lessor’s assumption of the lessee’s lease obligation under a different lease with another lessor.
83. Lease incentives should be recognized as reductions of lease rental expense by the lessee on a straight-line basis over the lease term. The lessee should recognize the expenses or losses to which the incentives relate in the period the costs are incurred. For example, an incentive equal to the moving expense incurred to occupy the leased space reduces rent expense over the lease term and the moving expense is recognized in the period incurred (that is, when the move occurs).
84. Lease Concessions – Lease concessions are rent discounts made by the lessor to entice the lessee to sign a lease. Lease concessions include rent holidays/free rent periods, reduced rents, or commission credits.
85. Lease concessions should be recognized as reductions of lease rental expense by the lessee on a straight-line basis over the lease term.
86. Leasehold Improvements – Leasehold improvements are additions, alterations, remodeling, renovations or other changes to a leased property that either extend the useful life of the existing property or enlarge or improve its capacity and are paid for (financed) by the lessee. Leasehold improvements that are placed in service at or after the beginning of the lease term should be amortized over the useful life (the normal operating life in terms of utility to the owner) of the leasehold improvement, but no longer than the expected lease term.

## DISCLOSURES

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87. Lessees should disclose a broad summary of significant intragovernmental leasing arrangements, including
- a. existence of intragovernmental leases and annual expense,
  - b. general lease terms with specific intragovernmental requirements (which may be grouped for purposes of disclosure), and
  - c. annual lease expense by major leased asset category.

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<sup>13</sup> Par. 79 – 81 outlines the general guidance for increases in rental payments; however guidance for other changes in rental payments is outlined in par. 82 – 85.

## INTRAGOVERNMENTAL LEASE ARRANGEMENTS – LESSOR ACCOUNTING

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88. The following sections articulate general recognition guidance for lessors of intragovernmental leases and detailed recognition guidance regarding several specific intragovernmental lease topics as well as disclosure guidance.

### RECOGNITION AND MEASUREMENT

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#### GENERAL GUIDANCE FOR RECOGNITION OF INTRAGOVERNMENTAL LEASES

89. A lessor should recognize lease receipts, including lease-related operating costs (for example, maintenance, utilities, or taxes) received from the lessee as income based primarily on the provisions of the lease.

#### GUIDANCE FOR RECOGNITION OF SPECIFIC INTRAGOVERNMENTAL LEASES

90. Lease Incentives – Lease incentives include lessor payments made to or on behalf of the lessee to entice the lessee to sign a lease. Lease incentives may include up-front cash payments to the lessee (for example, moving costs, termination fees to lessee's prior lessor, or lessor's assumption of the lessee's lease obligation under a different lease with another lessor). Lease incentives should be recognized as reductions of lease rental income by the lessor on a straight-line basis over the lease term.
91. Lease Concessions – Lease concessions are rent discounts made by the lessor to entice the lessee to sign a lease. Lease concessions include rent holidays/free rent periods, reduced rents, or commission credits.
92. Lease concessions should be recognized by the lessor as reductions in rental income on a straight-line basis over the lease term.
93. Lessor Improvements – Lessor improvements are additions, alterations, remodeling, renovations or other changes to a leased property that either extend the useful life of the existing property or enlarge or improve its capacity and are paid for (financed) by the lessor rather than by the lessee. These capital improvements are components of the leased property and should be capitalized and depreciated by the lessor over their useful life consistent with the lessor's accounting for property, plant, and equipment.<sup>14</sup>
94. Initial Direct Costs – Lessor initial direct costs should be expensed when incurred by the lessor.

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<sup>14</sup> This recognition is consistent with PP&E capital improvements outlined in SFFAS 6, par. 37.

## DISCLOSURES

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95. Lessors should disclose the following regarding intragovernmental leases:

- a. Future lease rental income as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding fiscal years for lease arrangements over the lease term
- b. A broad summary of significant leases (which may be grouped for purposes of disclosure), including a breakdown of the number of leases with federally-owned assets and privately-owned assets

## AMENDMENTS TO SFFAS 5, *ACCOUNTING FOR LIABILITIES OF THE FEDERAL GOVERNMENT* AND SFFAS 6, *ACCOUNTING FOR PROPERTY, PLANT, AND EQUIPMENT*

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96. This Statement replaces the measurement and reporting requirements for lease accounting established in SFFAS 5, *Accounting for Liabilities of the Federal Government*, paragraphs 43 – 46. Therefore, the paragraphs marked below are rescinded.

### **SFFAS 5: *Accounting for Liabilities of the Federal Government***

~~[43.] **Capital leases** are leases that transfer substantially all the benefits and risks of ownership to the lessee. If, at its inception, a lease meets one or more of the following four criteria, the lease should be classified as a capital lease by the lessee:~~

- ~~• The lease transfers ownership of the property to the lessee by the end of the lease term.~~
- ~~• The lease contains an option to purchase the leased property at a bargain price.~~
- ~~• The lease term is equal to or greater than 75 percent of the estimated economic life of the leased property.~~
- ~~• The present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equals or exceeds 90 percent of the fair value of the leased property.~~

~~The last two criteria are not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property. If a lease does not meet at least one of the above criteria it should be classified as an operating lease.~~

~~[44.] The amount to be recorded by the lessee as a liability under a capital lease is the present value of the rental and other minimum lease payments during the lease term, excluding that portion of the payments representing executory cost to be paid by the lessor. [footnote <sup>20</sup>: “The cost of general property, plant, and equipment acquired under a capital lease shall be equal to the amount recognized as a liability for the capital lease at its inception. See SFFAS No. 6, *Accounting for Property, Plant, and Equipment*.] However, if the amount so determined exceeds the fair value of the leased property at the inception of the lease, the amount recorded as the liability should be the fair value. If the portion of the minimum lease payments representing executory cost is not determinable from the lease provisions, the amount should be estimated.~~

~~[45.] The discount rate to be used in determining the present value of the minimum lease payments ordinarily would be the lessee's incremental borrowing rate unless (1) it is practicable for the lessee to learn the implicit rate computed by the lessor and (2) the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both these conditions are met, the lessee shall use the implicit rate. The lessee's incremental borrowing rate shall be the Treasury borrowing rate for securities of similar maturity to the term of the lease.~~

~~[46.] During the lease term, each minimum lease payment should be allocated between a reduction of the obligation and interest expense so as to produce a constant periodic rate of interest on the remaining balance of the liability. [footnote<sup>21</sup>: OMB Circular No. A-11, "Preparation and Submission of Annual Budget Estimates," explains the measurement of budget authority, outlays, and debt for the budget in the case of lease purchases and other capital leases. Circular A-94, "Guidelines and Discount Rates for Benefit Cost Analysis of Federal Programs," provides the requirements under which a lease purchase or other capital lease has to be justified and the analytical methods that need to be followed.]~~

97. This Statement replaces the measurement and reporting requirements for lease accounting established in SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraphs 20 and 29. Therefore, the paragraphs marked below are rescinded.

### **SFFAS 6: *Accounting for Property, Plant, and Equipment***

~~[20.] Capital leases are leases that transfer substantially all the benefits and risks of ownership to the lessee. If, at its inception, a lease meets one or more of the following four criteria, [footnote<sup>7</sup>: Note that the criteria for identifying capital leases for financial reporting purposes differ from OMB criteria for budget scoring of leases. OMB Circular No. A-11, *Preparation and Submission of Budget Estimates*, includes criteria for identifying operating leases in Appendix B. OMB provides four additional criteria which relate to the level of private sector risk involved in a lease purchase agreement. This is necessary because, for budget purposes, there is a distinction between lease purchases with more or less risk. This distinction is not made in the financial reports and, therefore, FASAB does not include the four criteria related to risk levels.] the lease should be classified as a capital lease by the lessee. Otherwise, it should be classified as an operating lease. [footnote<sup>8</sup>: "Operating leases" of PP&E are leases in which the Federal entity does not assume the risks of ownership of the PP&E. Multi-year service contracts and multi-year purchase contracts for expendable commodities are not capital leases.]~~

- ~~• The lease transfers ownership of the property to the lessee by the end of the lease term.~~
- ~~• The lease contains an option to purchase the leased property at a bargain price.~~
- ~~• The lease term is equal to or greater than 75 percent of the estimated economic life [footnote<sup>9</sup>: "Estimated economic life of leased property" is the estimated remaining period during which the property is expected to be economically usable by one or more users, with normal repairs and maintenance, for the purpose for which it was intended at the inception of the lease, without limitation by the lease term.] of the leased property.~~
  - ~~• The present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equals or exceeds 90 percent of the fair value [footnote<sup>10</sup>: "Fair value" is the price for which an asset could be bought or sold in an~~

~~arm's-length transaction between unrelated parties (e.g., between a willing buyer and a willing seller). (adapted from Kohler's Dictionary for Accountants)] of the leased property.~~

~~The last two criteria are not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property.~~

~~[29.] The cost of general PP&E acquired under a **capital lease** shall be equal to the amount recognized as a liability for the capital lease at its inception (i.e., the net present value of the lease payments calculated as specified in the liability standard [footnote <sup>24</sup>]. See Statement of Recommended Accounting Standards No. 5, *Accounting for Liabilities of the Federal Government*.] unless the net present value exceeds the fair value of the asset).~~

98. This Statement also amends Technical Release (TR) 16, *Implementation Guidance for Internal Use Software*, paragraphs 26, 27, and 29 to delete the "capital and operating lease" references, as follows.

#### **Technical Release 16: *Implementation Guidance for Internal Use Software***

[26.] Software License: If the term of software license(s) is 2 years or more with periodic payments, the license should be evaluated against lease criteria as stated in SFFAS X ~~SFFAS 5 paragraphs 43-46 and SFFAS 6 paragraph 20 to determine if it is a capital or operating lease.~~ If the license(s) is perpetual with an upfront cost [footnote <sup>9</sup>: The cost could be charged as a one-time payment or financed over a set period of time.] to use the software for its entire lifetime, then the entity is purchasing IUS and should apply its existing policy for capitalization thresholds to determine if the license should be capitalized or expensed.

[27.] A license agreement may include executory costs for maintenance and technical support. Agency judgment should apply in determining what portions of license fees are attributable to software capitalizable costs versus executory costs. Assuming lease ~~capitalization~~ criteria and thresholds are met, software license capitalization amounts [footnote <sup>10</sup>: SFFAS X ~~SFFAS 5, paragraph 44.~~] may be derived from the payment schedule contained in the license agreement. ~~As stated in SFFAS 5, If the portion of the minimum lease payments representing executory cost is not determinable from the lease provisions, the amount should be estimated. Agencies may also want to consider having each license agreement specifically identify the various costs throughout the license lifecycle, for example, initial license, maintenance, and enhancement.~~

[29.] If a cloud computing arrangement includes a software license, the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses in accordance with the lease criteria stated in SFFAS X ~~SFFAS 5 and SFFAS 6~~, and as discussed in paragraph 26 of this TR. ~~SFFAS 10 is not applicable to a cloud computing arrangement that does not convey a contractual right to the IUS or to ones that do not include an IUS license. The entity that develops and owns the software, platform, or infrastructure that is used in the cloud computing arrangement would account for the software development in accordance with SFFAS 10. If the funding to develop cloud computing is shared among entities without clear ownership, the service provider entity that receives funding and is responsible for~~

maintaining the software, platform, or infrastructure should account for the software in accordance with SFFAS 10 and the full cost/inter-entity cost requirements of SFFAS 4.

## IMPLEMENTATION

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99. This Statement requires that leases unexpired at the beginning of the reporting period in which the standard is implemented be recognized and measured using the facts and circumstances that exist at the beginning of the reporting period. Therefore, in the period of implementation,
- a. the determination of the lease term would assume that the lease term began as of the beginning of the period of implementation and
  - b. the lease liability and lease asset should initially be measured based on the remaining lease term and associated lease payments as of the beginning of the period of implementation.
100. The following implementation addresses specific leasing circumstances.
- a. Prospective Implementation - Entities should report the effect of implementing this Statement on existing leases prospectively in accordance with paragraph 13 of SFFAS 21, *Reporting Correction of Errors and Changes in Accounting Principles, Amendment of SFFAS 7, Accounting for Revenue and Other Financing Sources*. Accordingly, any changes in assets or liabilities related to existing leases should be treated prospectively. The change should be accounted for in the period of implementation and applicable future periods. No adjustments should be made to previously reported expenses or revenue.
  - b. Lease Term - The lease term should be determined based on the provisions of this Statement (see par. 14 – 18). However, the lease term of an existing lease should be based on the number of years remaining in the lease contract/agreement as of the beginning of the period of implementation and not the number of years in the initial lease term. For example, if the initial lease term was 20 years, with no options, at the beginning of Year 20X1 and the entity implements this Statement in Year 20X7 (6 years into the lease at the beginning of Year 20X7), the initial lease term upon implementation would be 14 years.
  - c. Short-term leases - A short-term lease would be determined based on the provisions of this Statement (see par. 59 – 61). However, if the remaining lease term of an existing lease meets the definition of a short-term lease (has a maximum possible term under the contract or arrangement of 24 months or less, including any options to extend, regardless of their probability of being exercised) that lease should apply the short-term lease guidance. For example, if the initial lease term was 60 months as of the beginning of Year 20X1, with no options to extend, and the entity implements this Statement in Year 20X5 (48 months into the lease at the beginning of Year 20X5); the initial lease term at implementation would be 12 months and the lease would meet the definition of a short-term lease. Hence, the entity should account for the lease as a short-term lease.

## EFFECTIVE DATE

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101. The requirements of this Statement are effective for reporting periods beginning after September 30, 2018. Early adoption is not permitted.

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| The provisions of this Statement need not be applied to immaterial items. |
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## APPENDIX A: BASIS FOR CONCLUSIONS

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This appendix discusses some factors considered significant by Board members in reaching the conclusions in this Statement. It includes the reasons for accepting certain approaches and rejecting others. Individual members gave greater weight to some factors than to others. The standards enunciated in this Statement—not the material in this appendix—should govern the accounting for specific transactions, events, or conditions.

### PROJECT HISTORY

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- A1. This project was undertaken primarily because
- a. the current lease accounting standards, Statement of Federal Financial Accounting Standards (SFFAS) 5, *Accounting for Liabilities of the Federal Government* and SFFAS 6, *Accounting for Property, Plant, and Equipment*, have been criticized as ineffective because they do not make meaningful distinctions between capital and operating leases based on the substance of lease transactions, and
  - b. the lease accounting standards in SFFAS 5 and 6 are based on Financial Accounting Standards Board (FASB) lease accounting standards which have been amended; in addition existing FASAB standards are not comprehensive and do not provide meaningful information on federal leasing activities.
- A2. Lease accounting was first addressed by the FASAB during the development of SFFAS 5 and 6. At that time the Board decided to use the high level language on lease accounting from FASB Statement of Financial Accounting Standards (SFAS) No. 13 *Accounting for Leases* [subsequently codified in Accounting Standards Codification (ASC) - Topic 840 *Leases*]. This minimal lease guidance included the definition of a capital lease, the criteria for capital leases, and the measurement of a capital lease asset and liability. The Board had plans to use this preliminary guidance as a placeholder until it was prepared to add lease accounting to its agenda as a separate project. Lease accounting had been on the list of potential Board agenda items each time the Board has considered its agenda for new projects.
- A3. There are several areas of lease accounting that were covered by the FASB standards that were never specifically covered in the FASAB standards. Some of those topics include leasehold improvements, lease terms, leveraged leases, and subleases. The federal community often stressed that the federal standards on lease accounting should be comprehensive to alleviate questions on when and if FASB standards apply to federal entities when the federal standards are silent on a topic.
- A4. In August 2011, FASAB began a project to revise its current standards on lease accounting. FASAB staff formed a task force to assist in developing the proposed standards for leases. Task force members included accounting, budget, and subject matter experts from federal agencies and independent public accounting firms.
- A5. The task force met several times over the course of the project and also exchanged numerous ideas and recommendations electronically. The task force views and recommendations were sought by staff in developing and describing alternatives to



present to the Board during the development of these standards. The task force's assistance was essential and its views carefully considered by members during deliberations. The task force played an important role in the research and release of this exposure draft.

- A6. In evaluating an approach applicable to federal leases, the Board considered the approaches used in the following documents:
- Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) 13, *Accounting for Leases* [Superseded by FASB Accounting Standards Codification (ASC) 840, which was subsequently superseded by ASC 842]
  - Governmental Accounting Standards Board (GASB) Exposure Draft, *Leases*, January 25, 2016
  - International Accounting Standards Board (IASB) International Accounting Standard (IAS) 17, *Leases*, which was superseded by International Financial Reporting Standard (IFRS) 16.
  - International Public Sector Accounting Standards Board (IPSASB) International Public Sector Accounting Standard (IPSAS) 13, *Leases*.
- A7. At the inception of the project the Board decided to coordinate with GASB on the lease project because of the similarities among governmental entities regarding lease activities and reporting objectives. Staff worked closely with GASB staff during the development of the proposals. In 2014 FASAB and GASB met jointly to discuss similar issues related to each of their ongoing lease accounting projects. As a result of this collaboration, similar wording may appear in some sections of the FASAB and GASB standards.<sup>15</sup>
- A8. This Statement amends the lease accounting standards in SFFAS 5, SFFAS 6, and TR 16. This Statement also establishes distinct standards for intragovernmental leases.

## KEY AREAS OF IMPROVEMENT

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- A9. This lease proposal will improve the existing lease accounting standards in SFFAS 5 and SFFAS 6 by
- a. providing relevant and meaningful financial information needed by federal financial statement users and
  - b. providing comprehensive lease standards that appropriately address the various lease transactions/activities of the federal community.
- A10. The Board believes that in a lease transaction, a lessee receives the right to use an underlying asset (the asset that is subject to the lease, such as a vehicle or building) at the beginning of the lease term. In exchange, the lessee promises to make payments over time for the right to use that underlying asset. The guidance in SFFAS 5 and 6 was based on the notion that some leases are essentially financed purchases of the underlying asset (classified as capital leases) and other leases (classified as operating leases) are not. The classification of a lease as capital or operating depended on whether the lease met any of

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four tests. Those tests were intended to determine whether most of the risks and benefits of ownership of the underlying asset were transferred to the lessee. Those tests have been criticized because their bright-line nature often resulted in very similar leases being accounted for in different ways.

## SCOPE

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- A11. For purposes of applying this Statement, a lease is defined as a contract or agreement that conveys the right to use a nonfinancial asset<sup>16</sup> (the underlying asset) for a period of time in an exchange transaction. Leases include contracts or agreements that, although not explicitly identified as leases, meet the definition of a lease (which reflects the substance of a lease). This definition does not include contracts or agreements for services unless that contract or agreement also conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.
- A12. This Statement does not apply to leases of federal natural resources as defined in Technical Bulletin (TB) 2011-1, *Accounting for Federal Natural Resources Other than Oil and Gas* and leases of federal oil and gas resources as defined in SFFAS 38, *Accounting for Federal Oil and Gas Resources*.
- A13. GASB's Leases exposure draft specifically excludes, "contracts that meet the definition of a service concession arrangement in paragraph 4 of Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements* (SCAs)." Currently FASAB standards are silent on SCAs. Through its discussions the lease task force identified several federal entities that have SCAs, and there was a concern that the proposed lease definition could inadvertently include SCAs. The Board considered specifically excluding SCAs from the lease standard. To accomplish the exclusion, the Board considered adopting GASB's definition of SCA from Statement No. 60 due to the lack of a federal definition of SCA.
- A14. Because SCAs are not currently addressed in federal accounting standards, the Board decided that specifically excluding SCAs from the lease standard would raise more questions. Furthermore, SCAs are expected to be addressed in the public-private partnership recognition and measurement project and therefore the Board agreed to remain silent on SCAs in the lease proposal. In conclusion, the Board believes the GAAP hierarchy will continue to guide preparers and auditors in accounting for SCAs.

## DEFINITIONS

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- A15. In this Statement, a lease is defined as a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction. In the early stages of the project the Board deliberated over the use of "contract" or "agreement" in the definition of a lease. The Board considered the GASB approach that the term contract is more precise and limiting and requires that a lease be legally enforceable. Because legal enforceability is not the primary driver in

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<sup>16</sup> Examples of nonfinancial assets include land, buildings, vehicles, equipment, internal use software, and intangible assets. Examples of financial assets include cash, investments, and receivables.

intragovernmental leasing transactions, the Board decided to add “agreement” in addition to “contract” in the lease definition to alleviate ambiguity in the application of the definition, especially in the case of intragovernmental leases which are often referred to as “lease agreements.”

## LEASE TERM -- RENEWAL AND TERMINATION OPTIONS

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- A16. Federal leases often include lessee options to renew, extend, or terminate a lease. Due to federal budget scoring rules and fiscal funding mechanisms, many federal leases include relatively short noncancelable periods. The Board concluded that the lease term used to measure the lease liability should not be limited to the noncancelable lease periods, but should include certain probable renewal option periods and consider the probability of termination options being exercised, so that the lease term reflects how long the lease is expected to be in effect.
- A17. The probability of a renewal or termination option being exercised applies only if that option pertains to the lessee alone. If either the lessee or the lessor has the option to cancel a lease (or if both parties have to agree to renew), the lease contract/agreement is not enforceable beyond that point. In those cases when either the lessee or the lessor could cancel the lease at any time, for example month-to-month lease holdovers, rolling lease extensions, or any lease that continues into a holdover period until a new contract or agreement is signed, the contract or agreement would be considered cancelable. When a lease contains a lessor-only option to terminate the lease, a lessee would have difficulty evaluating the likelihood of that option being exercised. This difficulty and the resulting cost outweigh the potential benefits of including the extra periods in the lease term. The Board also agreed that the presence of a bargain purchase option in a lease contract/agreement is not equivalent to a provision that transfers ownership of the underlying asset; therefore, a bargain purchase option should be treated as any other purchase option included in a lease.
- A18. The Board considered several potential probability thresholds for including a period covered by a renewal or termination option in the lease term. The Board considered its own definition of probable, GASB’s definition of probable, and FASB’s probability threshold “reasonably certain.” FASB’s probable definition equates to more likely than not (>50% probability). GASB’s probable definition equates to likely to occur and has a higher threshold of probability than more likely than not. FASB’s reasonably certain has an even higher threshold than likely to occur. The Board agreed to retain its definition of probable because it is more clearly defined and there seemed to be no compelling reason to introduce a new term for the sake of a higher threshold.

## REMEASUREMENT

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- A19. This Statement requires that when a lease liability is remeasured, the corresponding lease asset be adjusted by the same dollar amount (except in cases of impairment and in cases in which the adjustment would cause the asset to be reported as a negative amount). While acknowledging that adjusting the lease asset for a change in the lease liability

results in the lease asset no longer being measured at adjusted historical cost, the Board believes that such an adjustment is practical.

## NON-INTRAGOVERNMENTAL LEASES

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### RECOGNITION AND MEASUREMENT FOR LESSEES – LEASE LIABILITY

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- A20. SFFAC 5 defines a liability as a present obligation of the federal government to provide assets or services to another entity at a determinable date, when a specified event occurs, or on demand. The Board believes that the lessee taking possession of the underlying asset or gaining access to use the underlying asset is an event that creates such an obligation until the end of the lease term.
- A21. The Board believes the present value of future lease payments to be made for the lease term, which represent the obligations of the lessee under the lease contract/agreement, is the appropriate measurement of the liability. Such a calculation is consistent with the premise that a lease is a financing transaction and supports recognition of the cost of the financing.

### RECOGNITION AND MEASUREMENT FOR LESSEES – LEASE ASSET

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- A22. Assets are defined in SFFAC 5 as resources that embodies economic benefits or services the federal government controls. Lessees should recognize a lease asset to correspond with the lease liability. At the beginning of a lease, the lessee obtains the right to use the underlying asset and that right is a resource embodying economic benefits. The Board believes this right meets the definition of an asset. Because the lease liability represents the amount to be paid for the lease asset, the Board concluded that the initial measurement of the lease asset should be based on the measurement of the associated lease liability. PP&E assets generally are measured at historical cost, which is the amount paid for those assets. Therefore, measuring the lease asset based on the lease liability is consistent with historical cost accounting applicable to PP&E.

### RECOGNITION AND MEASUREMENT FOR LESSORS

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- A23. Symmetry between the lessee and lessor accounting models is important in establishing accounting and financial reporting standards. The Board believes that federal entity lessees and lessors should account for the same transaction in a way that mirrors how the other party accounts for it.
- A24. The lease contract gives the lessor the right to receive payments in exchange for the lessee's right to use the underlying asset. The Board believes that right meets the definition of an asset in SFFAC 5. Assets are defined as a resource that embodies economic benefits or services that the federal government controls. The right to receive payments is a resource that can be drawn upon, and the lessor presently controls that right.

### SHORT-TERM LEASE EXCEPTION

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A25. The Board considered the short-term lease exception GASB proposed, which requires governments to recognize leases with useful lives or maturities of less than one year. The Board decided to align the lease short-term exception with the PP&E standard which defines PP&E as a tangible asset with an estimated useful life of 24 months or more. The reporting of short-term leases in this Statement is intended to reduce the cost to federal entities of implementing these standards. This short-term exception eliminates the need for preparers to calculate amounts for short-term lease assets and liabilities. This exception requires lessees and lessors to recognize expense and revenue based on the payment provisions of those lease contracts/agreements with useful lives or maturities of less than two years. This measurement approach is not cash-basis recognition, as federal entities are still required to recognize receivables and payables for lease payments paid or received before or after the period to which they apply.

## INTRAGOVERNMENTAL LEASES

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A26. During the research phase of the project, the General Services Administration (GSA) provided an educational session to the Board where GSA representatives explained in-depth GSA's role in federal leasing. Based primarily on that discussion, the Board agreed that intragovernmental leases should be accounted for differently than leases between federal entities and non-federal entities. The Board agreed that a simplified approach for recognizing intragovernmental leases would be pragmatic and cost efficient.

A27. This Statement provides the overall recognition, measurement, and disclosure requirements for intragovernmental leases. An intragovernmental lease is a contract or agreement that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, *Reporting Entity*.

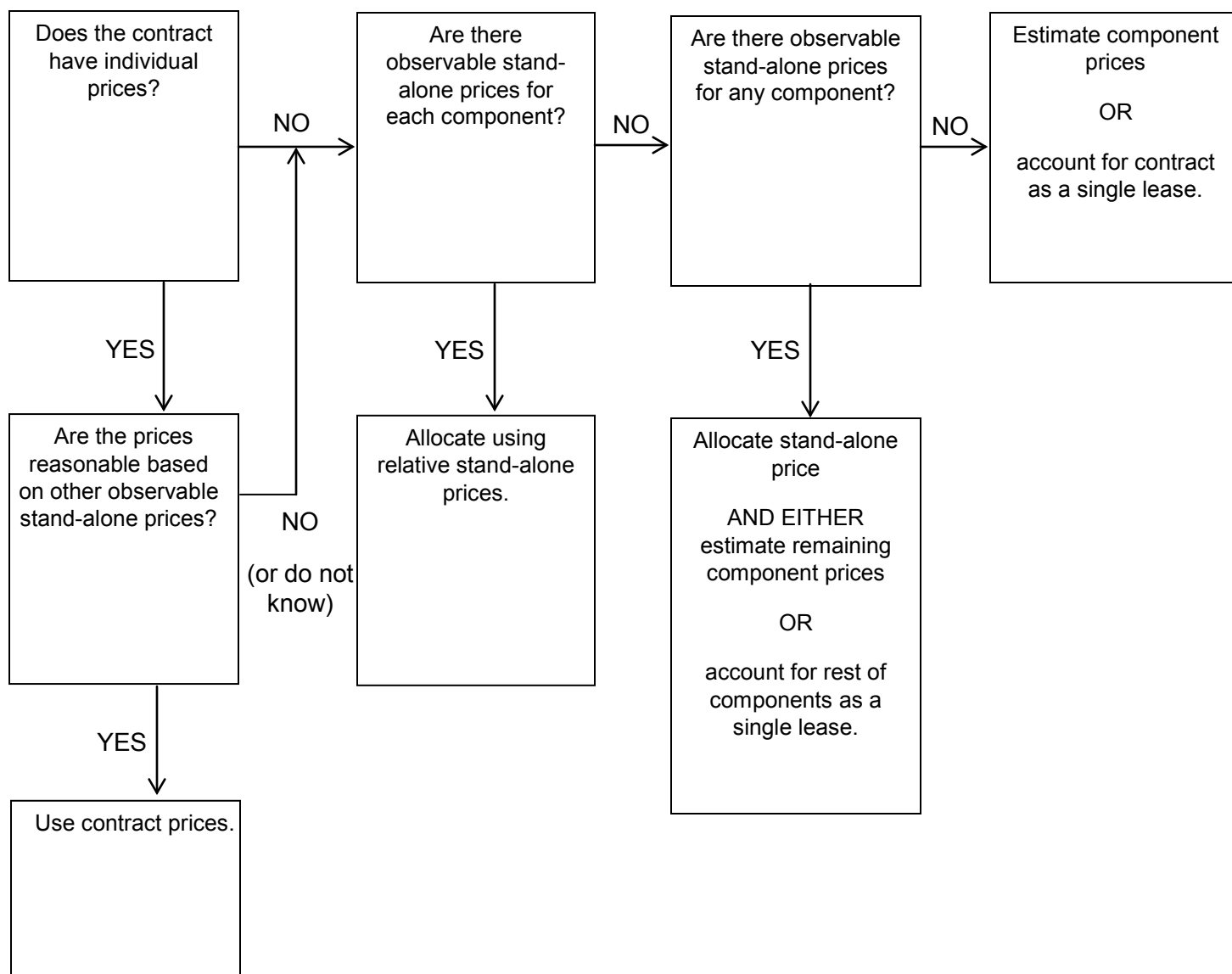
A28. The terms "intragovernmental" and "inter-entity" have been used interchangeably. Earlier FASAB standards predominately used "inter-entity." However, government-wide usage of "intragovernmental" has become more common, and therefore the Board decided to use intragovernmental in this Statement to describe leases occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47.

A29. This Statement provides general guidance on the recognition and measurement of lease rental increases, as well as guidance on other changes in the lease payments, such as lease incentives and lease concessions. The Board believes that rent increases are related to economic events, while lease incentives and concessions are more closely aligned with marketing cost. Therefore lessee rental increases should be recognized as expense in the period of the increase as provided in the lease; lease incentives and concessions should be recognized by the lessee/lessor as reductions of lease rental expense/lease rental income on a straight-line basis over the lease term.

## APPENDIX B: ILLUSTRATION

This appendix illustrates the application of the provisions of this Statement to assist in clarifying their meaning. The facts assumed in these examples are illustrative only and are not intended to modify or limit the requirements of this Statement or to indicate the Board's endorsement of the situations or methods illustrated. Additionally, these illustrations are not intended to provide guidance on determining the application of materiality. Application of the provisions of this Statement may require assessing facts and circumstances other than those illustrated here and require reference to other applicable Standards.

The following flowchart<sup>17</sup> is intended to aid in the application of the provisions for contracts with multiple components of this Statement – paragraphs 51 - 56.



<sup>17</sup> This illustration has been adapted from the GASB Lease ED, Appendix C, *Flowchart for Allocation of Consideration to Multiple Components*.

## APPENDIX C: ABBREVIATIONS

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|        |  |
|--------|--|
| ASC    | Accounting Standards Codification                      |
| CFR    | Consolidated financial report of the U.S. Government   |
| ED     | Exposure draft   |
| FASAB  | Federal Accounting Standards Advisory Board            |
| FASB   | Financial Accounting Standards Board                   |
| GAAP   | Generally Accepted Accounting Principles               |
| GAO    | Government Accountability Office                       |
| GASB   | Governmental Accounting Standards Board                |
| IPSASB | International Public Sector Accounting Standards Board |
| PP&E   | Property, Plant, and Equipment                         |
| SCA    | Service Concession Arrangement                         |
| OMB    | Office of Management and Budget                        |
| SFAS   | Statement of Financial Accounting Standards (FASB)     |
| SFFAC  | Statement of Federal Financial Accounting Concepts     |
| SFFAS  | Statement of Federal Financial Accounting Standards    |
| TB     | Technical Bulletin                                     |
| TR     | Technical Release                                      |

## APPENDIX D: GLOSSARY

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### Lease

A lease is a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction.

### Intragovernmental Lease

A lease occurring within a consolidation entity or between two or more consolidation entities as defined under SFFAS 47, *Reporting Entity*.<sup>18</sup>

### Probable

That which can reasonably be expected or believed to be more likely than not on the basis of available evidence or logic but which is neither certain nor proven.

### Lease Option Periods

Lease option periods are additional lease periods beyond the initial lease term – the options may be included in the initial lease or may be agreed to later in the lease term.

### Initial Direct Costs

Initial direct costs are costs that are directly attributable to negotiating and arranging a lease or portfolio of leases and would not have been incurred without entering into the lease.

### Short-Term Lease

A short-term lease is a lease that, at the beginning of the lease, has a maximum possible term under the contract or arrangement of 24 months or less, including any options to extend, regardless of their probability of being exercised.

### Lessee's Incremental Borrowing Rate

The lessee's incremental borrowing rate is the estimated rate that would be charged for borrowing the lease payment amounts for the lease term.

### Discount Rate

A discount rate is an interest rate that is used in present value calculations to equate amounts that will be received or paid in the future to their present value.

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<sup>18</sup> SFFAS 47, *Reporting Entity*, outlines the characteristics as a whole that an organization would have to be considered a consolidated entity (see SFFAS 47 par. 38-42).



## **FASAB Board Members**

D. Scott Showalter, Chairman

Gila J. Bronner

Robert F. Dacey

George A. Scott

Michael H. Granof

Christina Ho

Sam M. McCall

Mark Reger

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**Excerpts from FASAB Meeting Minutes  
February 22, 2017**

**Leases**

Ms. Valentine, assistant director, presented to the Board (from [tab C1](#) and [tab C2](#)) the 25 comment letters received on the *Leases* ED, several tables that summarized the comment letters, an initial staff analysis of the most significant issues identified by respondents, and thirteen questions for Board discussion.

Mr. Showalter first asked the Board if it wanted to hold a public hearing on the *Leases* ED. A public hearing would be an open invitation to anyone who wanted to speak with the Board about the *Leases* ED. Ms. Payne also posed two alternatives to a public hearing. One alternative would be to only invite a select few respondents to address the Board and provide further clarification on their responses. The second alternative to holding a public hearing would be to extend an invitation to all respondents of the ED to address the Board and provide further clarification on their responses.

Members expressed the following views in regards to seeking additional feedback from respondents:

- Respondents raised a lot of issues in the comment letters, and the Board may not have fully appreciated the depth of some of these concerns. The Board should invite some of the key respondents to express their concerns. Those agencies having the most significant concerns (the General Services Administration, DoD, and the Department of Homeland Security) should be asked to participate.
- The Board should invite the respondents it believes would be most affected by the proposed standards once they are finalized. The Board could invite other respondents that may have raised different issues. The purpose of having a public hearing is for the Board to get better clarity about issues raised in a comment letter, but if members fully understand the letter there is no need for further clarification. The reason FASAB would want to invite a respondent is to further explore the respondent's comments.
- Anyone who wants to make a point and express his/her views on the ED should have the opportunity to do so. If FASAB wants credibility among its constituents, FASAB has to ensure that these constituents believe they are being heard.

Ms. Motley stated if the Board's purpose is to get clarity from comments, then a public hearing is not necessary and inviting a subset would be fine. However, if the purpose is broader, meaning to understand the range of concerns in general, then she would suggest having a public hearing.

Mr. McNamee asked if staff would be developing a list of questions for members to ask the respondents during the session and if those questions would be provided to the presenters before the meeting. Mr. Showalter replied yes to both questions and stated the members have the option to use the prepared questions or not.

After discussing the three options, the Board concluded to extend an invitation to all ED respondents to address the Board and provide further clarification on their responses to the *Leases* ED at the April meeting.

Several questions were posed to the Board by staff based on the initial analysis of issues identified by respondents.

Staff noted that some of the respondents thought that the definition of “lease” was too broad, and the scope of the standards should be narrowed. Staff noted the definition needs to be broad to apply to leasing activities of all federal entities. Implementation guidance will provide more details on applying the standards. Staff recommends implementation guidance be developed as soon as the standards are finalized. Staff would like to reconvene the leases task force and move towards the issuance of implementation guidance as soon as the amended standards become final.

Mr. Scott asked if implementation guidance will address the questions asked by the respondents or if it is necessary to expand the standards to include more definitions and examples.

Ms. Valentine stated the implementation guidance can take on many different formats, such as illustrations or questions and answers. The format is flexible as long as the guidance stays within the bounds of the final Leases standards. The implementation guidance will be developed through the leases task force.

**Question 1:** Does the Board agree with staff’s recommendation that implementation guidance will be necessary to assist entities to effectively implement the amendments to the Leases standards?

The Board agreed with staff that implementation guidance would be necessary to assist entities to effectively implement the amendments to the Leases standards.

Staff noted a couple of respondents thought the definition of a lease should include the notion of control to better understand what transactions meet the definition of a lease. The definition of an asset in SFFAC 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*, includes control by the federal government; therefore, control is an implied characteristic of all assets of the federal government. However, staff also noted that GASB and the Financial Accounting Standards Board (FASB) have included the notion of control in their lease definitions. Staff recommended the definition of a lease proposed in the ED be modified to add the notion of control and include additional language connecting the definition to SFFAC 5’s definition of an asset.

Members questioned why adding the notion of control to the lease definition was needed if control is embedded in the definition of an asset. Staff noted the addition would clarify the connection of control to a lease. The members discussed the differences in the wording between GASB and FASB. GASB proposes a lease is defined as “a contract that conveys control of the right to use...” FASB defines a lease as “a contract, or part of a contract, that conveys the right to control the use...” The Board preferred the FASB wording and asked staff to inquire about the differences between the two definitions. Staff will work on the wording to ensure clarity around what is being controlled and what the right is.

**Question 2:** Does the Board agree with staff’s recommendation to add the notion of control to the lease definition and include additional language connecting the definition to SFFAC 5’s definition of an asset?

The Board asked staff to revise the proposed definition based on the discussion and present the revisions at a later meeting.

Staff added that at least one respondent noted the use of “nonfinancial asset” in the lease definition should be changed to “nonmonetary assets” to be consistent with other FASAB guidance. Based on staff’s review, both terms “nonfinancial” and “nonmonetary” are used throughout the FASAB Handbook; however, neither term is defined by FASAB. Staff found that “nonfinancial” most often referred to information and “nonmonetary” referred to assets. Staff also discovered that industry definitions of the terms are synonymous. The *Leases* ED’s use of “nonfinancial” was derived from GASB’s proposed lease definition.

The Board generally agreed with staff’s proposed change from “nonfinancial asset” to “nonmonetary asset.” The Board also asked staff to include a definition of the term ultimately used in the final standards.

**Question 3:** Does the Board agree with staff’s recommendation to change the term “nonfinancial asset” to “nonmonetary asset” in the final amended Leases standards?

The Board wants to take into consideration the respondents’ concerns about the scope of the lease definition before a final decision is made.

Staff noted that some respondents disagreed with assessing the probability of termination clauses (such as fiscal funding clauses) and renewal options to determine the lease term.

Ms. Ho asked if the fiscal funding clause legally relieved the federal government’s obligations to the provisions of the lease contract/agreement. Mr. Reger responded that it does relieve the government’s obligation; however, the entity will be subject to the cancellation penalties of the contract/agreement, which could be the total amount of remaining lease payments. He also made the point that, contractually, it would allow the federal entity to leave the contract. It does not necessarily relieve the entity of the monetary obligation associated with leaving the contract. Mr. Reger expounded that this

is usually the case with real property, but he does not know if it holds true for airplanes, ships, or other items the federal government leases. Mr. Reger suggested asking DoD this question during the respondents' clarification discussion at the April meeting.

**Question 4:** Does the Board agree with staff's recommendation to carry forward into the final standards the method used in determining the lease term, including what is considered the "noncancelable period" proposed in the ED?

There were no objections to staff's recommendation to carry forward into the final standards the method used in determining the lease term, including what is considered the "noncancelable period" proposed in the ED. Mr. Reger expressed again that he would like to get clarification to his question about cancellation penalties.

Staff noted there were some respondents who thought the Leases proposal should be more consistent with FASB and GASB, using a probability threshold of reasonably certain (which is higher than FASAB's proposed threshold of probable—more likely than not).

The Board had discussed the issue of using probable versus several other thresholds utilized by standard setters quite extensively during the standards development process. Staff recommended the Board remain consistent with the probable threshold. A member suggested that before making a conclusion on the issue the Board may wish to hear more feedback from the respondents. The respondents had raised several cost-benefit issues, and it is important for them to convey those issues to the Board at the next meeting, before a final decision is made.

**Question 5:** Does the Board agree with staff's recommendation to carry forward into the final standards the probability threshold used when assessing whether renewal and termination options will be exercised?

The Board agreed to hear more feedback from the respondents before making a final decision on the probability threshold issue.

Several respondents disagreed with the proposed initial lessee recognition of a liability and an asset. One respondent noted the government does not always have the benefits of the asset and often has limited control over the use of the asset being leased. Other respondents thought the minimum lease payments schedule currently required in lease disclosures is sufficient information to the reader.

Similarly, members suggested deferring the decision on this issue, pending additional input from respondents.

**Question 6:** Does the Board agree with staff's recommendation to carry forward into the final standards the initial lessee recognition proposed in the ED?

There were no objections to the suggestion to defer a decision on the initial lessee recognition proposed in the ED until after the discussion with the respondents.

Staff noted some respondents disagreed with the recognition and measurement of the lease liability by the lessee proposed in the ED. One respondent stated valuing the lease liability at the net present value of the cash flows for the duration of the lease term potentially overstates the debt for an agreement that can be terminated when the shorter noncancelable period has expired. Respondents also noted the requirement is inconsistent with valuing the asset at the lesser of fair market value and net present value.

A member requested that the respondents who participate in the clarification session be asked to talk about the burden created by these proposed standards. Another member stated the burden may be due to the entity's self-inflicting processes or it may be a true burden of the standards.

**Question 7:** Does the Board agree with staff's recommendation to carry forward into the final standards the recognition and measurement of the lease liability by the lessee proposed in the ED?

There was no Board decision on staff's recommendation; the Board would like additional feedback from the respondents on the issue.

Staff noted some of the respondents disagreed with the interest rate used to calculate the lease liability proposed in the ED. One respondent stated the lessor's interest rate often is not identified in the lease and cannot be readily determined. Because the alternative is to use the lessee's interest rate, which will always be considerably lower, there would be a huge variation in the interest rates used for this calculation.

Based on these comments, several members noted it appeared some respondents did not understand the language in the ED: "The future lease payments should be discounted using the rate the lessor charges the lessee, which may be the interest rate implicit in the lease."

**Question 8:** Does the Board agree with staff's recommendation to carry forward into the final standards the interest rate used to calculate the lease liability proposed in the ED?

There was no Board decision on staff's recommendation; the Board would like additional feedback from the respondents on the issue.

Staff noted some respondents disagreed with the circumstances when the lessee must remeasure the lease liability proposed in the ED. One respondent was concerned that the remeasurement of the liability also requires the asset value to change, which would alter methodology of recording assets at historical cost.

One member stated the Board deliberated quite extensively on the circumstances when the lessee must remeasure the lease liability. The member expounded that unless a respondent enlightens the Board with additional facts the Board is unaware of, or gives evidence that this requirement is more burdensome than expected, the Board should keep the proposed requirements for liability remeasurement.

**Question 9:** Does the Board agree with staff's recommendation to carry forward into the final standards the circumstances when the lessee must remeasure the lease liability proposed in the ED?

There was no disagreement with the recommendation to carry forward into the final standards the circumstances when the lessee must remeasure the lease liability proposed in the ED, unless the Board is persuaded by respondents during the April clarification discussion that this requirement is more burdensome than the Board had originally expected.

Staff noted some respondents disagreed with the recognition and measurement of the lease asset by the lessee proposed in the ED. One respondent stated if the Board requires a liability be recorded for leases, then the asset should be recorded in the amount of the liability only; to require agencies to record other costs as an asset and then amortize the amounts creates a burden.

**Question 10:** Does the Board agree with staff's recommendation to carry forward into the final standards the recognition and measurement of the lease asset by the lessee proposed in the ED?

There was no Board decision on staff's recommendation; the Board would like additional feedback from the respondents on the issue.

Staff noted some respondents prefer a 12-month requirement for short-term leases and other respondents prefer a longer time requirement for short-term leases, like five years. During the development of the ED, the Board considered the short-term lease exception of 12 months; however, the Board decided to align the lease short-term exception with the Property, Plant, and Equipment (PP&E) standards, which define PP&E as a tangible asset with an estimated useful life of 24 months or more. Another respondent noted inconsistencies between paragraph 14 and paragraph 59 of the ED. The current wording of each paragraph may cause differing interpretations of what would qualify as a short-term lease.

**Question 11:** Does the Board agree with staff's recommendation to carry forward into the final standards the lease term of 24 months or less for a short-term lease proposed in the ED?

**Question 12:** Does the Board agree with staff's recommendation to change the definition of short-term lease from "a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised" to "a lease with a lease term (as defined in paragraph 14) of 24 months or less"?

There were no objections to staff's recommendation to (1) carry forward into the final standards the lease term of 24 months or less for a short-term lease proposed in the ED and (2) change the definition of short-term lease from "a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised" to "a lease with a lease term (as defined in paragraph 14) of 24 months or less."

Staff noted the respondents were split on the proposed effective date of reporting periods beginning after September 30, 2018, or FY 2019. Staff recommended the effective date be changed to FY 20 (reporting periods beginning after 9/30/2019) to give entities adequate time to effectively implement the amended Leases standards.

**Question 13:** Does the Board agree with staff's recommendation to change the effective date of the amended Leases standards to FY 20?

There were no objections to staff's recommendation to change the effective date of the amended Leases standards to FY 20.

**Next Steps:** Staff will extend an invitation to all 25 respondents of the *Leases* ED to speak before the Board to provide members with further clarification on their responses to the ED. Members will also ask questions of the respondents. The clarifying discussion will take place on April 26, the first day of the next FASAB meeting. Staff will also prepare a package for the Board with materials to facilitate the discussion. Additionally, staff will continue with the analysis for Board consideration of the more significant issues raised, as well as the remaining issues raised, in the comment letters.



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## **History of Board Lease Discussions**

- ❖ At the February Board meeting, staff provided to the Board the 25 comment letters received on the *Leases* ED, several tables that summarized the comment letters, an initial staff analysis of issues identified by respondents, and questions for Board discussion.

Members agreed to extend an invitation to all respondents of the ED to address the Board and provide further clarification on their responses to the *Leases* ED at the April meeting.

The Board agreed with staff that implementation guidance would be necessary to assist entities to effectively implement the amendments to the *Leases* standards.

The Board discussed issues raised in the responses to the *Leases* ED. There were no Board decisions based on staff's recommendations because members wanted additional feedback from the respondents on the following issues:

- The addition of the notion of control to the lease definition as well as language connecting the definition to that of an asset in Statement of Federal Financial Accounting Concepts 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*
- The change of the term “nonfinancial asset” to “nonmonetary asset” in the final amended *Leases* Statement
- The method used in determining the lease term, including what is considered the “noncancelable period” proposed in the ED
- The probability threshold used when assessing whether renewal and termination options will be exercised
- The initial lessee recognition proposed in the ED
- The recognition and measurement of the lease liability by the lessee proposed in the ED
- The interest rate used to calculate the lease liability proposed in the ED
- The circumstances when the lessee must remeasure the lease liability proposed in the ED
- The recognition and measurement of the lease asset by the lessee proposed in the ED
- The lease term of 24 months or less for a short-term lease proposed in the ED
- The change of the definition of short-term lease from “a lease that, at the beginning of the lease, has a maximum possible term under the contract/agreement of 24 months or less, including any options to extend, regardless of its probability of being exercised” to “a lease with a lease term (as defined in paragraph 14) of 24 months or less”

- The change of the effective date of the amended leases standards to fiscal year 2020

Next Steps: Staff will extend an invitation to all 25 respondents of the *Leases* ED to allow them to speak before the Board to provide clarification on their responses to the ED and for the members to ask questions of the respondents. The clarifying discussion will take place on April 26, the first day of the next FASAB meeting. Staff will also prepare a package for the Board with materials to facilitate the discussion. Additionally, staff will continue with an analysis of the comments for Board consideration.

- ❖ The Board released for public comment on September 26, 2016 the proposed SFFAS entitled *Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government and SFFAS 6, Accounting for Property, Plant, and Equipment*, which was. The Board requested comments on the exposure draft by January 6, 2017.
- ❖ At the August Board meeting, staff provided to the Board a pre-ballot draft ED on lease accounting. The objective of the session was for the Board to provide feedback to staff and approve the Lease ED pre-ballot draft.

The following topics were presented by staff and discussed by the Board.

- Comment Period End Date – The Board agreed to the comment period end date of January 6, 2017.
- Proposed Effective Date – Staff proposed an effective date of periods beginning after September 30, 2019. Members agreed to propose an effective date of September 30, 2018, and revise the date to September 30, 2019, if the Board gets a negative reaction to the 2018 effective date. The Board also agreed to not allow early adoption of the standard to maintain consistency among the reporting entities.
- Public Hearing – Staff proposed scheduling a public hearing for April 26, 2017, and providing notice of the public hearing in the ED. The Board agreed that scheduling a public hearing should be determined based on the responses to the comment letters. Therefore, the ED will not include the scheduling of a public hearing; however, the possibility of a public hearing will be noted in the ED.
- Remeasurement Respondent Questions – The Board agreed to add a question to the ED to address the effect of remeasurement on the lease liability and asset, as well as language in the basis for conclusions to reflect the Board's rationale. They also agreed to add a question to address whether certain remeasurement triggers would cause significant costs to the preparer.
- Implementation Guidance – The Board agreed to propose the prospective implementation approach, which requires that leases unexpired at the beginning of the reporting period be recognized and measured using the facts and

circumstances that exist at the beginning of the period of implementation. This approach includes examples of implementation scenarios.

Next steps: The next steps are to incorporate all of the Board's edits, send the Board a ballot draft of the ED for approval, and release the ED by the end of September.

- ❖ At the June Board meeting, staff provided to the Board a draft ED on lease accounting and task force responses to several lease-related questions posed by staff. The objective of the session was to review responses to seven questions staff had posed to the lease task force related to issues in which the Board had requested additional information and review a draft Lease ED.

The Board made the following tentative decisions.

- The Board agreed with the staff recommendation to propose the use of FASAB's definition of probable (more likely than not – >50%) as the probability threshold in the Lease ED. The Board also directed staff to include probability threshold as a question in the ED.
- The Board agreed to propose that the leased asset be classified as property, plant, and equipment (PP&E) unless the underlying asset is not PP&E; in those cases the leased asset would be classified to align with the nature of the underlying asset.
- The Board agreed that the basis for conclusions should tell the story of how the Board arrived at its conclusions and the Board's collaboration with the Governmental Accounting Standards Board (GASB). The basis for conclusions should not specifically note when FASAB's proposed guidance diverges from GASB's guidance unless the Board deliberated on GASB's approach. In those instances when the Board considered GASB's approach, staff will include the highlights of the discussion and how the Board came to its conclusions.
- The Board agreed to add some verbiage to the basis for conclusions on rent increases, lease incentives, and lease concessions.

Next steps: Staff will make the revisions discussed at the meeting to the draft ED and provide a pre-ballot draft for the August meeting.

- ❖ At the April Board meeting staff members presented to the Board one issue related to developing the exposure draft (ED) of the proposed standards on non-intragovernmental lease accounting. The Board previously directed staff to use the Governmental Accounting Standards Board's (GASB) proposal on Leases as a platform for developing the federal standards on non-intragovernmental lease – the GASB ED was released for comment in January 2016.

The objective of the session was to address the issue of service concession arrangements (SCAs) in the proposed lease standards. Staff noted GASB's Leases ED specifically excludes, "Contracts that meet the definition of a service concession arrangement in paragraph 4 of Statement No. 60, Accounting and Financial

Reporting for Service Concession Arrangements.” Currently FASAB standards are silent on SCAs.

The Board agreed that because SCAs is a topic not previously addressed in federal accounting standards, specifically excluding SCAs from the lease standard would raise more questions about SCAs. Therefore, members concluded that SCAs should not be addressed in the lease standard. Although SCAs are expected to be addressed in the P3 recognition and measurement project, the Board agreed to remain silent about SCAs in the lease proposal but to include the Board’s rationale in its BFC. The Board may also consider asking a question about SCAs of the respondents to the ED.

- ❖ At the February 2016 meeting staff updated the Board on the lease project, including the status of the GASB lease project. The Board had previously directed staff to use the GASB lease proposal as a platform for developing the FASAB standards on non-intragovernmental leases.

Staff made several revisions to the language contained in the GASB proposal to reflect differences at the federal level, any conflicts with existing FASAB standards, and any changes to which the Board had previously agreed. In addition, staff also posed 23 questions to the Board related to the draft. The questions highlight areas where the FASAB proposal deviates from the GASB proposal, areas where the task force has raised questions, and areas where overall general questions on the proposal were appropriate.

Mr. Showalter asked staff to highlight only the areas in which Board members had additional questions, as well as the areas in which staff would like further direction from the Board, due to the number of questions put forth by the staff.

Capitalization Thresholds: Staff stated that because SFFAS 6, Accounting for Property, Plant, and Equipment (PP&E) specifically addresses capitalization thresholds, a task force member questioned whether the lease standards would allow federal entities to establish capitalization thresholds for lease assets. Staff also noted that GASB does not address the issue of capitalization thresholds in the standards sections of the lease ED, but in the basis for conclusions.

The Board agreed to not specifically address capitalization thresholds in the lease proposal but to discuss overall materiality in the application of the standard, which would then apply to the materiality of the related lease liability and lease asset.

Lessee Incremental Borrowing Rate: Staff noted that GASB proposes use of the incremental borrowing rate if the actual or implicit rate charged by the lessor cannot be readily determined. This is consistent with current FASAB standards. However, the incremental rate for federal borrowers is the Treasury rate—a risk-free rate.

Staff noted that the risk-free rate is not reflective of the lessor's implicit rate, and the risk-free rate would understate the interest expense. Staff also suggested that the language in paragraph 20 be modified from "If the rate cannot be readily determined..." to "If the rate cannot be reasonably estimated by the lessee, the lessee's incremental borrowing rate (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used."

The Board agreed with the revised language.

*Lease Liability Remeasurement—Due to a Change in an Index or Rate:* Staff noted that GASB proposes that the lease asset be adjusted when the corresponding lease liability is remeasured. GASB also proposes that the effects of a lease liability remeasurement, due to a change in an index or rate used to determine variable payments, be recognized the same way as the effects of remeasurement for other reasons. This would be an adjustment to the lease asset, rather than recognition in the flows statement (as proposed in the Preliminary Views). GASB proposed the change primarily due to cost-benefit concerns.

The Board agreed to remain consistent with GASB's approach that the lease asset be adjusted when the corresponding lease liability is remeasured in all instances.

*Insignificant Lease Components:* Staff noted that the Board had previously agreed that the guidance should exempt leases with multiple insignificant and unpriced components from applying methods to disaggregate the components.

The draft language would read, "If a contract/agreement does not include prices for individual components, or if those prices are not reasonable based on other observable stand-alone prices, lessors and lessees should do the following, unless the components as a whole are not considered significant."

The Board had no objections to the edit.

- ❖ At the December 2015 meeting staff updated the Board on the lease project, including the status of the GASB lease project. The Board had previously directed staff to use the GASB lease proposal as a platform for developing the FASAB standards on non-intragovernmental leases.

Staff noted that the GASB is in the final stages of finalizing their exposure draft (ED) and expects to release the ED for comment in early February 2016. FASB plans to release their final lease standard in early 2016 with an effective date of 2019.

Staff's goal is to have the FASAB lease ED available for comment by mid-2016. Staff also held a lease task force meeting in early-February 2016.

There was also a brief discussion on the accounting for lease holdovers, in light of a recent GAO report.

Lastly, there are plans to convene another FASAB/GASB joint meeting in 2016.

Staff will continue to work with the task force to further develop the lease standards and will continue to follow the progress of the GASB lease discussions.

- ❖ At the October 2015 meeting staff updated the Board on GASB's deliberations of their lease project. The Board had previously directed staff to use the GASB Lease proposal as a platform for developing the FASAB standards on non-intragovernmental leases.

Staff provided the Board with excerpts from the tentative GASB Board meeting minutes from their September 1, 2015 lease discussion. The following GASB lease topics were presented to the Board.

- Airport Leases and Related Issues
- Lessee Disclosures
- Lessor Disclosures
- Short-Term Lease Exception
- Lease Terminations and Modifications
- Subleases and Leaseback Transactions

Staff will continue to work with the task force to further develop the lease standards and will continue to follow the progress of the GASB lease discussions.

- ❖ At the August 2015 meeting staff updated the Board on GASB's deliberations of their lease project. The Board had previously directed staff to use the GASB Lease proposal as a platform for developing the FASAB standards on non-intragovernmental leases.

Staff provided the Board with eleven discussion items that staff compiled from the last three GASB lease discussions (April, June, and July 2015). The eleven issues represented those lease topics that GASB either changed its position from the November 2014 Lease Preliminary Views document or topics that FASAB will need to further discuss as the exposure draft is developed. The following discussion items were presented to the Board.

- Defining "nonfinancial asset"
- Intangible (lease) assets
- The role of "control" in determining whether a transaction qualifies as an asset
- Service concession agreements
- Bargain purchase options
- Month-to-month holdover periods
- Probability threshold
- Lessee renewal/termination options
- Fiscal funding clauses

- Lease liability remeasurement
- Allocation of consideration to multiple components

A Board member suggested just giving examples or asset classes of nonfinancial assets, if a clearer definition cannot be developed. The Board asked staff if federal leases would go beyond the scope of capital assets (real and personal property). The Board asked staff to comeback with options to defining nonfinancial assets.

Staff noted that the FASAB “probable” definition equates to “more likely than not” and “reasonably certain” has an even higher threshold than GASB’s “probable (likely to occur).” Since FASAB previously noted that it was comfortable with the differences between our “probable” and GASB’s “probable,” staff recommends not accepting GASB’s change to “reasonably certain” and staying with the FASAB “probable” definition, because there seems to be no compelling reason to introduce a new term for the sake of a higher threshold. The Board did not disagree with staff’s recommendation.

The Executive Director reminded the Board that all of the issues will be brought back to the Board for more discussion before the exposure draft is finalized.

Staff will continue to work with the task force to further develop the lease standards and will continue to follow the progress of the GASB lease discussions.

- ❖ At the April meeting staff presented to the Board an initial draft exposure draft (ED) for the intragovernmental portion of the leases standard. Staff noted that the lease standard will include guidance for all federal leases, including intragovernmental leases. The Board has tentatively agreed that intragovernmental leases should be accounted for similar to current operating leases guidance. The draft ED included definitions of relevant terms, as well as specific provisions that address the recognition and measurement of intragovernmental leases for both the lessee and the lessor. Staff asked the Board if they agreed with the proposed language. The Board generally agreed with the staff proposal and asked staff to provide clarifying language in several sections of the proposal.

Staff also presented to the Board a summary of possible FASAB-relevant comments from the Governmental Accounting Standards Board’s (GASB) Preliminary Views (PV) on Leases. The Board had previously directed staff to use the GASB Lease PV as a platform for developing the FASAB standards on non-intragovernmental leases. GASB received 37 comment letters on their lease PV and held three public hearings and expects to issue its exposure draft in February 2016 and a final standard in early 2017. Since the Board previously agreed to use the GASB lease accounting proposal as the foundation for the FASAB lease account proposal and any wording differences could denote a difference in meaning, staff recommended that the FASAB ED also be released close to that same timeframe as the GASB ED. The Board agreed to stay in sync with the GASB timeline for the release of the lease ED and final standard.



- ❖ At the February meeting staff presented to the Board a discussion paper that provided an analysis of the final six chapters of the Governmental Accounting Standards Board (GASB) Preliminary Views (PV) on Leases. The GASB PV on Leases is being used as a foundation for the development of the FASAB lease standards on non-intragovernmental lease agreements – the GASB PV was released for comment in November 2015. The topics discussed included lessee accounting, lessor accounting, short-term exception, lease terminations and modifications, subleases and leaseback transactions, and leases with related parties, and intra-entity leases.
- ❖ At the December 2014 meeting staff presented to the Board proposed guidance for intragovernmental leases. The proposed guidance included definitions of relevant terms, as well as specific provisions that address features of leases and is based on the current Financial Accounting Standards Board operating lease guidance. The Board had previously directed staff to simplify the intragovernmental lease accounting guidance. Staff presented revisions to the previously proposed recognition and disclosure lessee and lessor guidance for intragovernmental lease arrangements. The Board stressed consistency and the need for symmetry between the lessee and lessor accounting for intragovernmental leases

Staff also presented an analysis of the first three chapters of the GASB Preliminary Views (PV) on Leases so that the Board could discuss the GASB concepts as it relates to the development of federal lease standards. The GASB PV on Leases will be used as a foundation for the development of the FASAB lease standards on non-intragovernmental lease agreements– the GASB PV was released for comment in November. The topics discussed were project objective, project background, applicability, scope, and lease term.

- ❖ At the October 2014 meeting staff presented to the Board proposed draft guidance for intragovernmental leases. The proposed guidance included definitions of relevant terms, as well as specific provisions that addressed features of leases and that is based on the current FASB operating lease guidance.

Staff proposed seven lease-related definitions to the Board for discussion. The first three definitions – lease, intragovernmental and intragovernmental lease agreement – were discussed and tentatively agreed to by the Board at previous meetings. The remaining four proposed lease-related definitions – intragovernmental lease inception, intragovernmental minimum lease payments, intragovernmental noncancelable lease term, and intragovernmental sublease – were adapted from FASB’s existing operating lease guidance. The Board asked staff to simplify the proposed definitions and discuss with the task force.

Staff also presented proposed recognition and disclosure lessee guidance for intragovernmental lease arrangements. The Board agreed that the lessee general guidance would be to recognize lease payments as they are received and specific provisions would address those instances when the “due and payable” is not applicable.

The Board also agreed that certain scheduled rent increases, rent holidays, and lease incentives should be recognized on a straight-line basis – possibly using the proposed language used for the amortization of leasehold improvements.

- ❖ At the August 2014 meeting the Board discussed and agreed to a definition for the term “intragovernmental” to refer to occurring within a consolidation entity or within or between two or more consolidation entities.

The Board discussed and agreed to proposed definitions of leases and of intragovernmental lease arrangements.

The Board discussed staff's proposal for recognizing operating leases--straight-line for lease costs and in the current period for executory costs. The Board members agreed with the straight-line concept for lease payments, but would like additional information before deciding whether executory costs should be required to be separated from the rental payment.

The next decision related to the proposed disclosure of future lease payments. Some questioned whether this disclosure was necessary for intragovernmental lease arrangements. The Board agreed to exclude the disclosure, but to ask a question in the exposure document whether the disclosure is necessary.

The Board agreed that the lessor revenue recognition would match the lessee's expense recognition—on the straight-line basis.

The Board agreed that upfront lease costs for lessors would be expensed

Regarding potential disclosures of future lease payments of lessors, there were no objections to the proposed disclosures.

- ❖ At the June 2014 Board meeting a majority of the Board agreed with a simplified approach for recognizing amounts arising from intragovernmental lease arrangements. The Board agreed that intragovernmental lease arrangements should be accounted for differently than leases between federal entities and non-federal entities.

The Board suggested referring to the project as “leases, including similar intragovernmental lease arrangements” (similar intragovernmental lease arrangements are in substance leases) to differentiate the intragovernmental arrangements from the non-federal arrangements. This would allow the two types of transactions to be disclosed separately.

The Board also agreed not to pursue issuing a preliminary views (PV) document on leases and to tentatively plan to issue its exposure draft (ED) on leases and other similar arrangements close to when the Governmental Accounting Standards Board (GASB) will issue its ED. Because GASB plans to issue a PV prior to its ED, staff will have an opportunity to seek informally feedback from the federal community on the GASB PV.

- ❖ At the April 2014 meeting the U.S. General Services Administration (GSA) provided an educational session with the goal of the Board gaining a better understanding of several GSA lease-related topics.
- ❖ At the March 2014 the Board met jointly with the GASB to discuss similar issues related to each of their ongoing lease accounting projects. Both Boards agreed that they should begin with the goal of developing symmetry between the lessee and lessor models. The FASAB was also very focused on the intragovernmental leasing issues involving federal entities and those federal-specific lease issues.
- ❖ In January 2014 staff asked the Board to provide their input in a survey format on the tentative decisions made by the GASB on their lease project to date. Based on the results of the survey, staff identified several topics for further discussion during the joint meeting with GASB.
- ❖ At the December 2013 meeting the Board briefly discussed the GASB tentative decisions on their leases project to date with the GASB Practice Fellow leading their leases project.
  - ✓ The Board tentatively agreed that based on Statement of Federal Financial Accounting Concepts (SFFAC) 5's definition of an asset and liability a federal entity's **right to use** a leased asset and the **obligation to make lease payments** are assets and liabilities of the entity.
  - ✓ All of the members agreed to explore the single-model approach as opposed to the dual-model approach.

#### *Other Lease Discussions*

- ❑ FASAB staff members met with OMB staff on April 30, 2014 to discuss budget scoring for capital leases. OMB staff explained that Appendix B of OMB Circular A-11, which provides instructions on the budgetary treatment of lease-purchases and leases of capital assets, is consistent with the scorekeeping rule developed by the executive (OMB) and legislative branches (CBO) originally in connection with the Budget Enforcement Act of 1990 (BEA). Statement of Financial Accounting Standards 13, issued by FASB, was the "support" for the scorekeeping rules developed. Because the lease budget scoring rules were developed in connection with the BEA and cannot be changed unless all of the scorekeepers (OMB, CBO, and the Budget Committees) agree, it is not likely that the rules will change based on potential changes in the financial accounting for leases. OMB staff provided other helpful insights which we will explore further later in the project.