

## Memorandum

### Leases - Omnibus

November 18, 2022

To: Members of the Board  
From: Ricky A. Perry, Jr., Senior Analyst  
Thru: Monica R. Valentine, Executive Director  
Subject: **Considerations for finalizing lease term omnibus amendment** (Topic C)

#### INTRODUCTION

The briefing material includes a staff summary and analysis of GASB's omnibus amendments to its lease term guidance.

#### REQUEST FOR FEEDBACK BY DECEMBER 5

**Prior to the Board's December meeting**, please review staff's analysis, recommendations, and the pre-ballot Statement. Please respond to the ensuing questions no later than December 5.

Please provide responses to Mr. Perry at [PerryRA@fasab.gov](mailto:PerryRA@fasab.gov), with a cc to Ms. Valentine at [ValentineM@fasab.gov](mailto:ValentineM@fasab.gov).

#### NEXT STEPS

**Pending Board member feedback**, staff intends to ballot soon after the December meeting.

#### ATTACHMENTS

1. Staff recommendations and analyses
2. *SFFAS XX, Omnibus Amendments 2023: Leases-Related Topics II*, pre-ballot draft
3. Leases project plan

#### REFERENCE MATERIAL

1. [SFFAS 54, Leases, as amended by SFFAS 60](#)
2. [GASB Statement No. 99, Omnibus 2022](#)



## Staff Analysis

### Leases

November 18, 2022

#### CONTEXT

As part of the leases project, the Board has identified and proposed a few additional omnibus amendments to facilitate implementation of SFFAS 54 and enhance the clarity of the Statement.

At the August meeting, members approved a majority of the omnibus proposals and several finalizing changes to those proposals, mostly clarifying in nature, based on public comments. Members *tentatively approved* the proposed amendment to paragraph 19 of SFFAS 54, *Leases*. The tentative approval was subject to staff consultations with Governmental Accounting Standards Board (GASB) staff on the proposed lease term amendment and, if necessary, staff agreed to provide subsequent updates on such consultations.

On August 29, staff met with GASB staff to discuss the paragraph 19 proposed amendment. GASB staff provided additional information for FASAB staff to consider. GASB staff also shared staff papers to inform additional staff analysis for Board consideration. These staff papers were informative and facilitated further staff understanding and analysis of GASB deliberations and omnibus actions affecting its lease term and transfer of ownership guidance (under GASB Statement No. 99, *Omnibus 2022*).

#### SUMMARY OF RECOMMENDATIONS AND ANALYSES

In reviewing the GASB staff papers on GASB Statement No. 99, FASAB project staff identified additional opportunities to clarify lease term determination and transfer of ownership guidance through similar omnibus actions.<sup>1</sup>

The below analysis summarizes the basis for staff's recommendation to proceed with revised omnibus actions. Staff also recommends monitoring for implementation guidance candidates related to this matter. These candidates can be included in the AAPC's project to update Technical Release 20 to conform the guidance to this omnibus pronouncement—a project planned for calendar year 2023.

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## ANALYSIS

### Part 1 – An Overview of the Un-Amended Requirements

GASB Codification, Section L20, .109-.110, .116, (GASB 87 par. 12-13), <i>un-amended</i>	SFFAS 54, par. 19 and 25, <i>un-amended</i>
<p><b>[Lease term section] .109</b> 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 the following periods, if applicable:</p> <ul style="list-style-type: none"> <li><b>a.</b> Periods covered by a lessee's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option</li> <li><b>b.</b> Periods covered by a lessee's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessee will not exercise that option</li> <li><b>c.</b> Periods covered by a lessor's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessor will exercise that option</li> <li><b>d.</b> Periods covered by a lessor's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessor will not exercise that option.</li> </ul> <p>Periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party (or if both parties have to agree to extend) are cancelable periods and are excluded from the lease term. For example, a rolling month-to-month lease, or a lease that continues into a holdover period until a new lease contract is signed, would not be enforceable if both the lessee and the lessor have an option to terminate and, therefore, either could cancel the lease at any time. Provisions that allow for termination of a lease due to (1) purchase of the underlying asset, (2) payment of all sums due, or (3) default on payments, are not considered termination options.</p> <p><b>.110</b> A fiscal funding or cancellation clause allows governmental lessees to cancel a lease, typically on an annual basis, if the government does not appropriate funds for the lease payments. This type of clause should affect the lease term only if it is reasonably certain that the clause will be exercised.</p> <p><b>[Transfers of ownership section] .116</b> A contract that (a) transfers ownership of the underlying asset to the lessee by the end of the contract and (b) does not contain termination options (see paragraph .109), but that may contain a fiscal funding or cancellation clause that is not reasonably certain of being exercised (see paragraph .110), should be reported as a financed purchase of the underlying asset by the lessee or sale of the asset by the lessor.</p>	<p><b>[Lease term section] 19.</b> In determining the lease term for both the lessee and lessor, the following specific provisions should be applied:</p> <ul style="list-style-type: none"> <li><b>a.</b> Periods for which both the lessee and lessor (1) have an option to terminate the lease without permission from the other party or (2) have to agree to extend are cancelable periods and are excluded from the lease term. For example, 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 would be considered cancelable if both the lessee and the lessor have an option to terminate. Therefore, either could cancel the lease at any time. These holdover periods are cancelable periods and should be excluded from the lease term.</li> <li><b>b.</b> If the lease provisions allow for the termination of a lease due to (a) the purchase of the underlying asset, (b) the payment of all sums due, or (c) the default on payments, these provisions are not considered options to terminate.</li> <li><b>c.</b> An availability of funds or cancellation clause allows federal lessees to cancel a lease agreement, typically on an annual basis, if funds for the lease payments are not appropriated. This type of clause should affect the lease term only when it is probable that the clause will be exercised.</li> </ul> <p><b>[Transfers of ownership section] 25.</b> A contract or agreement that (a) transfers ownership of the underlying asset to the lessee by the end of the contract or agreement and (b) does not contain options to terminate (par. 14-19), but that may contain an availability of funds or cancellation clause that is not probable of being exercised (par. 19.c), should be reported as a purchase of that asset by the lessee or as a financed sale of the asset by the lessor.</p>

There are presentation and organization differences between the *un-amended versions* of par. 19 of SFFAS 54 and GASB Codification Section L20 paragraphs .109-.110. Comparative differences in presentation and organization are not of concern, nor do they necessitate additional omnibus actions by the Board.

## Part 2 – An Overview and Analysis of GASB's Omnibus Action

GASB Codification Section L20, .109-.113, .119, as amended by GASB Statement No. 99, <i>Omnibus 2022</i> <sup>2</sup>	FASAB staff analysis
<p><b>[Lease term section] .109</b> 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 the following periods, if applicable:</p> <ul style="list-style-type: none"> <li>a. Periods covered by a lessee's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option</li> <li>b. Periods covered by a lessee's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessee will not exercise that option</li> <li>c. Periods covered by a lessor's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessor will exercise that option</li> <li>d. Periods covered by a lessor's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessor will not exercise that option.</li> </ul> <p><del>Periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party (or if both parties have to agree to extend) are cancelable periods and are excluded from the lease term. For example, a rolling month-to-month lease, or a lease that continues into a holdover period until a new lease contract is signed, would not be enforceable if both the lessee and the lessor have an option to terminate and, therefore, either could cancel the lease at any time.</del> <b>[A]</b> Provisions that allow for termination of a lease due to (1) purchase of the underlying asset, <b>[B]</b> (2) payment of all sums due, <b>[C]</b> or (3) default on payments, <b>[D]</b> are not considered termination options.</p> <p><u>.110 For purposes of applying paragraph .109, an option to terminate is an unconditional right that exists within the contract. A provision that gives a lessee or lessor the right to terminate the lease only in certain circumstances or upon the occurrence of certain events, such as the action or inaction of the other party to the lease contract, should not be considered an option to terminate the lease for purposes of determining the lease term. For example, provisions that allow for termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease.</u></p> <p><u>.111 If a lessee has the option to purchase the underlying asset during the lease term and the contract is not a contract that transfers ownership that is required to be reported in accordance with paragraph .119 of this section, the lease term should exclude the period, if any, after the date at which the option is reasonably certain to be exercised.</u> <b>[E]</b></p> <p><u>.112 Periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party (or if both parties have to agree to extend) are cancellable periods and are excluded from the lease term. For example, a rolling month-to-month lease, or a lease that continues into a holdover period until a new lease contract is signed, would not be enforceable if both the lessee and the lessor have an option to terminate and, therefore, either could cancel the lease at any time.</u></p> <p><del>.113 440</del> A fiscal funding or cancellation clause allows governmental lessees to cancel a lease, typically on an annual basis, if the government does not appropriate funds for the lease payments. This type of clause should affect the lease term only if it is reasonably certain that the clause will be exercised.</p> <p><b>Par. .114-.116 (short-term lease criteria) are omitted here, as they are not relevant to this analysis.</b></p> <p><b>[Transfers of ownership section] .119-446</b> A contract that (a) transfers ownership of the underlying asset to the lessee by the end of the contract and (b) does not contain termination options (see paragraph .109), but that may contain a fiscal funding or cancellation clause that is not reasonably certain of being exercised (see paragraph .110), should be reported as a financed purchase of the underlying asset by the lessee or sale of the asset by the lessor. <u>For this purpose, provisions that allow for termination of a lease due to (1) purchase of the underlying asset, (2) payment of all sums due, or (3) default on payments are not considered termination options.</u> <b>[F]</b></p>	<p><b>[A]:</b> Moved to a new paragraph, .112.</p> <p><b>[B]:</b> Addressed in new paragraphs, .110-.111.</p> <p><b>[C]:</b> In practice, lease provisions do not provide for terminations after payments of all sums due. The lessor has an ongoing obligation to provide access to the underlying asset. As a result, GASB removed this from the lease term guidance.</p> <p><b>[D]</b> Moved to example in new paragraph, .110 (last sentence).</p> <p><b>[E]</b> Staff views this as additional clarification. In staff's opinion, this clarification may be helpful for ensuring consistent implementation. However, absent this omnibus action, other criteria in GASB 87 (and SFFAS 54) constructively provides this criterion.</p> <p><b>[F]</b> Establishes linkage between transfer of ownership definitional criterion and paragraph .110 criterion. Staff does not view items (2) and (3) in the sentence as necessary due to an existing x-ref in the paragraph to lease term guidance paragraphs (.109-.110).</p>

<sup>2</sup>This GASB amendment is effective for fiscal years beginning after June 15, 2022.

At GASB, the above-stricken language at the end of Codification section L20, paragraph .109, was originally included (within paragraph 12 of GASB Statement No. 87) due to concerns related to *contracts that transfer ownership*.

The GASB requirements for contracts that transfer ownership (which aligns with par. 25 of SFFAS 54) provide that a contract that transfers ownership and does not contain termination options should be reported as a financed purchase of a capital asset.

There were concerns at GASB (when developing its leases exposure draft that led to GASB Statement No. 87) that a number of contracts that transfers of ownership might contain provisions that could end the lease if they were triggered. For example, having a choice to purchase the underlying asset before the scheduled transfer date would “end the lease,” as the lessee would no longer have control of the right to use another entity’s asset (it would be the lessee’s asset). Additionally, many contracts have a termination provision if a party defaults on payments. The original language was intended to mean that such contracts could still qualify for treatment as a financed purchase and transfer of ownership.<sup>3</sup>

Based on this information, GASB implemented the above amendments in order to make clear (a) an option to terminate for purposes of determining the lease term and (b) a termination option related to contracts that transfer ownership.<sup>4</sup>

For leases that otherwise meet the criteria for transfers of ownership under paragraph 25 of SFFAS 54, purchase options that are assessed as probable of being exercised prior to a transfer of ownership should not be a basis for exempting the lease from the provisions of paragraph 25. For this reason, staff recommends an action, as discussed below (items 1-2).

GASB Statement No. 99, basis for conclusions paragraph B20, explains the GASB’s belief that contract provisions that allow for the termination of a lease due to a violation of contract terms and conditions should not be considered an option to terminate because those provisions are contingent upon the action or inaction of one of the parties to the lease. FASAB staff concurs with this view. As noted in B20, the prescriptive nature of paragraph 12 (19.b of SFFAS 54) absent the omnibus action implies that such provisions could be viewed as options to terminate more broadly. As previously noted, the paragraph was intended only to clarify what types of provisions cannot be considered termination options for purposes of a defining transfers of ownership.

The GASB omnibus action (under section L20 paragraph .110) enhances the clarity of criteria for evaluating what constitutes an option to terminate. Notably, under basis paragraph B20, the GASB elected to establish a “principle that will provide a basis for the evaluation of a range of contract provisions” rather than establish an additional specific exclusion for violations of contract terms and conditions. Examples of provisions that would also likely *not* be considered options to terminate, for purposes of measuring lease term, under this clarified criterion, include:

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<sup>3</sup>Scott Anderson et al. “Memorandum re: Omnibus Preballot Draft of an Exposure Draft, Omnibus 20XX” (issue paper presented to the Governmental Accounting Standards Board, Norwalk, CT, May 2021).

<sup>4</sup>Ibid.

- provisions allowing the lessor to terminate if it decides to tear down the building
- provisions allowing the lessor to terminate if it is in the public's best interest
- provisions allowing the lessor to terminate if it plans infrastructure improvements that would interfere with the lease
- provisions allowing the lessor to terminate if modifications of relevant laws no longer permit performance under the lease

Similar steps can be taken by FASAB to clarify these matters through three recommended actions similar to those taken by GASB.

### Recommendations

1. Implement similar omnibus amendments to those made by GASB in paragraph 19 of SFFAS 54.

*Paragraph 19 of SFFAS 54 is amended as follows:*

*19. In determining the lease term for both the lessee and lessor, the following specific provisions should be applied:*

*a. Periods for which the lessee and lessor (1) have an option to terminate the lease without permission from the other party or (2) have to agree to extend are cancelable periods and are excluded from the lease term. For example, 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 would be considered cancelable if both the lessee and the lessor have an option to terminate. Therefore, either could cancel the lease at any time. These holdover periods are cancelable periods and should be excluded from the lease term.<sup>4</sup>*

*b. An option to terminate is an unconditional right that exists within the contract. A provision that gives a lessee or lessor the right to terminate the lease conditional upon certain circumstances or upon the occurrence of certain events, such as the action or inaction of the other party to the lease contract, should not be considered an option to terminate the lease for purposes of determining the lease term. For example, provisions that allow for termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease. If the lease provisions allow for the termination of a lease due to (a) the purchase of the underlying asset, (b) the payment of all sums due, or (c) the default on payments, these provisions are not considered options to terminate.*

*c. An availability of funds or cancellation clause allows federal lessees to cancel a lease agreement, typically on an annual basis, if funds for the lease payments are not appropriated. This type of clause should affect the lease term only when it is probable that the clause will be exercised.*

*d. If a lessee has the option to purchase the underlying asset during the lease term and the contract is not a contract that transfers ownership that is required to be reported in accordance with paragraph 25, the lease term should exclude the period, if any, after the date at which the option is probable of being exercised.*



This action would be consistent with GASB's omnibus amendments under section L20 paragraph .110-.111 of its Codification. It would also address the implementation issues discussed under Part 2 above.

As discussed in August, it is also important to clarify that improbable purchase options and payment-related matters are not relevant to cancelable period identifications. This omnibus action takes care of this concern as well.

**2. Option 1 (recommended by staff):** Implement similar omnibus amendments to those made by GASB in paragraph 25 of SFFAS 54.

Paragraph 25 of SFFAS 54 is amended as follows:

25. A contract or agreement that (a) transfers ownership of the underlying asset to the lessee by the end of the contract or agreement and (b) does not contain options to terminate (par. 14-19), but that may contain an availability of funds or cancellation clause that is not probable of being exercised (par. 19.c), should be reported as a purchase of that asset by the lessee or as a financed sale of the asset by the lessor.<sup>5</sup> [For this purpose, options to purchase the underlying asset prior to the transfer of ownership are not considered options to terminate.](#)

This action would be consistent with GASB's omnibus amendment to its transfers of ownership criteria under paragraph .119. Staff did not include provisions that allow for termination of a lease due to "payment of all sums due" in this recommendation. Such provisions do not exist in practice. Lessors would have an ongoing obligation to provide access to the underlying asset regardless the status of sums that were previously due. Continued inclusion of such language has not, but may inadvertently cause confusion in the future. GASB staff have received numerous technical inquiries on this matter.

Please also note that this particular omnibus amendment is not necessarily *needed* due to the already existing cross-reference to paragraphs 14-19 in the paragraph. This cross-reference will now reference the needed clarification recommended under recommendation 1, which amends paragraph 19.

**Option 2 (viable alternative):** Implement an omnibus amendment that more precisely mirrors the omnibus action of GASB.

Paragraph 25 of SFFAS 54 is amended as follows:

25. A contract or agreement that (a) transfers ownership of the underlying asset to the lessee by the end of the contract or agreement and (b) does not contain options to terminate (par. 14-19), but that may contain an availability of funds or cancellation clause that is not probable of being exercised (par. 19.c), should be reported as a purchase of that asset by the lessee or as a financed sale of the asset by the lessor.<sup>5</sup> [For this purpose, provisions that allow for termination of a lease due to \(1\) purchase of the underlying asset, \(2\) payment of all sums due, or \(3\) default on payments are not considered options to terminate.](#)

This action would enhance consistency with GASB's guidance. However, staff prefers option 1. Staff does not believe that mention of "payment of all sums due" is necessary. Such rare situations would, in the context of a transfer of ownership contract, amount to an accelerated purchase option in substance. Defaults on payments are already addressed under the paragraph through the cross-reference to paragraphs 14-19. Paragraph 19.b and the related omnibus action recommended by staff (recommendation 1 above) clarifies that "provisions that allow for termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease." As a result, staff does not have due process concerns for removing either of these items. Rather, staff believes that the divergence from GASB enhances clarity. That said, GASB's omnibus action continues to be a viable alternative. This option mitigates the significance of the omnibus change while maintaining technical accuracy.

3. Staff also recommends bringing implementation guidance update candidates to the AAPC related to recommendations 1 and 2 above. These candidates can be included in the AAPC's project to update Technical Release 20 to conform the guidance to this omnibus pronouncement. The AAPC project is planned for calendar year 2023.

Staff will consider implementation issues identified by the AAPC, those submitted through technical inquiries or the task force, and those that might be included in GASB's 2023 Implementation Update project.<sup>5</sup>

Recommendations 1-3 do not substantively change the requirements of paragraphs 14-21 and 25 in SFFAS 54. These recommended omnibus actions are not in response to technical inquiries received by FASAB staff. Rather, they are proactive actions in response to exposure draft feedback and numerous technical inquiries received by GASB staff on analogous requirements addressed under GASB Statement No. 99.

The guidance in SFFAS 54 is already widely understood. Accordingly, staff considers these additional proposed amendments to be clarifying in nature and not warranting re-exposure. Specifically, the proposed edits further clarify the original paragraph 19.b and paragraph 25 by expanding on and further clarifying the treatment of purchase options and defaults on payments.

These omnibus actions are not expected to result in additional costs to preparers. Rather, they will reduce expected implementation costs by providing clarity on existing requirements.

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<sup>5</sup>A GASB exposure draft is forthcoming. Staff will review the exposure draft for any potentially relevant updates related to analogous omnibus amendments under GASB Statement No. 99.



Amendment Comparison

GASB Codification Section L20, .110-.113, .119, <b>as amended</b> by GASB Statement No. 99, Omnibus 2022	SFFAS 54, par. 19 and 25, <i><b>illustrative staff-recommended amendments</b></i> , <i><b>differences highlighted</b></i>
<p><b>.110</b> For purposes of applying paragraph .109, an option to terminate is an unconditional right that exists within the contract. A provision that gives a lessee or lessor the right to terminate the lease <b>only in</b> certain circumstances or upon the occurrence of certain events, such as the action or inaction of the other party to the lease contract, should not be considered an option to terminate the lease for purposes of determining the lease term. For example, provisions that allow for termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease.</p> <p><b>.111</b> If a lessee has the option to purchase the underlying asset during the lease term and the contract is not a contract that transfers ownership that is required to be reported in accordance with paragraph .119 of this section, the lease term should exclude the period, if any, after the date at which the option is <b>reasonably certain to be</b> exercised.</p> <p><b>.112</b> Periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party (or if both parties have to agree to extend) are cancellable periods and are excluded from the lease term. For example, a rolling month-to-month lease, or a lease that continues into a holdover period until a new lease contract is signed, would not be enforceable if both the lessee and the lessor have an option to terminate and, therefore, either could cancel the lease at any time.</p> <p><b>.113</b> A fiscal funding or cancellation clause allows governmental lessees to cancel a lease, typically on an annual basis, if the government does not appropriate funds for the lease payments. This type of clause should affect the lease term only if it is reasonably certain that the clause will be exercised.</p> <p><b>.119</b> A contract that (a) transfers ownership of the underlying asset to the lessee by the end of the contract and (b) does not contain termination options (see paragraph .109), but that may contain a fiscal funding or cancellation clause that is not reasonably certain of being exercised (see paragraph .110), should be reported as a financed purchase of the underlying asset by the lessee or sale of the asset by the lessor. For this purpose, provisions that allow for termination of a lease due to (1) purchase of the underlying asset, (2) payment of all sums due, or (3) default on payments are not considered termination options.</p>	<p><b>19.</b> In determining the lease term for both the lessee and lessor, the following specific provisions should be applied:</p> <p><b>a.</b> Periods for which the lessee and lessor (1) have an option to terminate the lease without permission from the other party or (2) have to agree to extend are cancelable periods and are excluded from the lease term. For example, 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 would be considered cancelable if both the lessee and the lessor have an option to terminate. Therefore, either could cancel the lease at any time. These holdover periods are cancelable periods and should be excluded from the lease term.<sup>4</sup></p> <p><b>b.</b> An option to terminate is an unconditional right that exists within the contract. A provision that gives a lessee or lessor the right to terminate the lease <b>conditional upon</b> certain circumstances or upon the occurrence of certain events, such as the action or inaction of the other party to the lease contract, should not be considered an option to terminate the lease for purposes of determining the lease term. For example, provisions that allow for termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease.</p> <p><b>c.</b> An availability of funds or cancellation clause allows federal lessees to cancel a lease agreement, typically on an annual basis, if funds for the lease payments are not appropriated. This type of clause should affect the lease term only when it is probable that the clause will be exercised.</p> <p><b>d.</b> If a lessee has the option to purchase the underlying asset during the lease term and the contract is not a contract that transfers ownership that is required to be reported in accordance with paragraph 25, the lease term should exclude the period, if any, after the date at which the option is <b>probable of being</b> exercised.</p> <p><b>25.</b> A contract or agreement that (a) transfers ownership of the underlying asset to the lessee by the end of the contract or agreement and (b) does not contain options to terminate (par. 14-19), but that may contain an availability of funds or cancellation clause that is not probable of being exercised (par. 19.c), should be reported as a purchase of that asset by the lessee or as a financed sale of the asset by the lessor.<sup>5</sup> For this purpose, options to purchase the underlying asset prior to the transfer of ownership are not considered options to terminate.</p>

The GASB-FASAB differences highlighted in paragraph 19.b and 25 are not significant. They enhance clarity and phrasing linkage across SFFAS 54. The paragraph 19.b difference is intended to create linkage to the first sentence of the sub-paragraph. The paragraph 19.d difference is based on the already existing GASB-FASAB difference in lease term criteria related to the terms “reasonably certain” and “probable.” The paragraph 25 difference is to further clarify the treatment of purchase options. Items other than purchase options that are discussed under GASB’s paragraph .119 would already be considered earlier in the paragraph (through existing references to paragraphs 14-19); as a result, staff propose omitting these items under the paragraph 25 omnibus.

### **Questions for the Board #1-3**

1. Do you agree with staff's recommendations? If not, do you prefer to more closely align with GASB's omnibus actions? Members with such preference are asked to provide tentative reasoning to staff for consideration.
2. Do you agree with staff's recommendation 2 option 1, or do you prefer option 2 or some other alternative, such as no omnibus action? Please explain.
3. Do members have any comments on staff's corresponding revisions to the summary and basis for conclusions (see Attachment 2)?



## OMNIBUS AMENDMENTS 2023

LEASES-RELATED TOPICS II

**Statement of Federal Financial Accounting Standards XX**

**March XX, 2023**

**Pre-ballot copy**

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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.

Accounting standards are 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. FASAB publishes the proposed standards in an exposure draft for public comment. In some cases, FASAB publishes a discussion memorandum, invitation for comment, or preliminary views document on a specific topic before an exposure draft. 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 standards 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 and other items of interest are available at [www.fasab.gov](http://www.fasab.gov):

- [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](#)
- [Documents for comment](#)
- [Statements of Federal Financial Accounting Standards and Concepts](#)
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**Commented [PR(1)]:** GASB recently moved into their new headquarters.

## SUMMARY

This Statement of Federal Financial Accounting Standards (SFFAS) amends certain paragraphs in SFFAS 54, *Leases*, and SFFAS 60, *Omnibus Amendments 2021*.

In August 2019, the Accounting and Auditing Policy Committee—which operates under the general oversight of the Federal Accounting Standards Advisory Board (FASAB or “the Board”)—undertook a project to develop proposed implementation guidance for SFFAS 54 as a Technical Release. During the course of the project, implementation issues were identified that are best addressed through omnibus amendments to clarify existing leases guidance rather than through a Technical Release. The issues require modifications to the existing Statements to provide technical clarifications and address areas of concern. A substantial majority of those issues were addressed in SFFAS 60; however, a few outstanding implementation issues required additional research and deliberations. This Statement addresses those outstanding issues by clarifying

- the Board's original intent for discounting lease liabilities and receivables, which should result in a more consistent and comparable application of SFFAS 54, *Leases*, requirements;
- ~~interactions between paragraphs 19.a and 19.b of SFFAS 54~~the treatment of purchase options and defaults on payments for purposes of (a) determining the lease term and (b) assessing contracts or agreements that transfer ownership for options to terminate; and
- the applicability of paragraphs 89-92 of SFFAS 54 to intragovernmental sale-leasebacks and disclosure requirements applicable to them.

## MATERIALITY

The provisions of this Statement need not to be applied to information if the effect of applying the provision(s) is immaterial.<sup>1</sup> A misstatement, including omission of information, is material if, in light of surrounding facts and circumstances, it could reasonably be expected that the judgment of a reasonable user relying on the information would change or be influenced by the correction or inclusion of the information. Materiality should be evaluated in the context of the specific reporting entity. Determining materiality requires appropriate and reasonable judgment in considering the specific facts, circumstances, size, and nature of the misstatement. Consequently, after quantitative and qualitative factors are considered, materiality may vary by financial statement, line item, or group of line items within an entity.

<sup>1</sup> Refer to Statement of Federal Financial Accounting Concepts 1, *Objectives of Federal Financial Reporting*, chapter 7, titled *Materiality*, for a detailed discussion of the materiality concepts.

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## STANDARDS

### SCOPE

1. This Statement applies to federal entities that present general purpose federal financial reports (GPFFRs), including the consolidated financial report of the U.S. Government (CFR), in conformance with generally accepted accounting principles (GAAP), 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*.
2. This Statement amends SFFAS 54, *Leases*, and SFFAS 60, *Omnibus Amendments 2021*, by providing additional guidance, along with technical corrections and clarifications.

### AMENDMENTS TO SFFAS 54 AND SFFAS 60

3. Paragraph 19.b of SFFAS 54 is amended as follows:

19. In determining the lease term for both the lessee and lessor, the following specific provisions should be applied: ...

~~19.b An option to terminate is an unconditional right that exists within the contract. A provision that gives a lessee or lessor the right to terminate the lease conditional upon certain circumstances or upon the occurrence of certain events, such as the action or inaction of the other party to the lease contract, should not be considered an option to terminate the lease for purposes of determining the lease term. For example, provisions that allow for termination of a lease due to a violation of lease terms and conditions, such as a default on payments, are not considered options to terminate the lease. Lease provisions that allow for the termination of a lease due to (a) the purchase of the underlying asset, (b) the payment of all sums due, or (c) the default on payments are not considered options to terminate for purposes of identifying cancelable periods to exclude from the lease term in accordance with paragraph 19.a.~~

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4. Paragraph 19.d is added as follows:

19. In determining the lease term for both the lessee and lessor, the following specific provisions should be applied: ...

19.d If a lessee has the option to purchase the underlying asset during the lease term and the contract is not a contract that transfers ownership that is required to be reported in accordance with paragraph 25, the lease term should exclude the period, if any, after the date at which the option is probable of being exercised.

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5. Paragraph 25 of SFFAS 54 is amended as follows:

25. A contract or agreement that (a) transfers ownership of the underlying asset to the lessee by the end of the contract or agreement and (b) does not contain options to terminate (par. 14-19), but that may contain an availability of funds or cancellation clause that is not probable of being exercised (par. 19.c), should be reported as a purchase of

that asset by the lessee or as a financed sale of the asset by the lessor.<sup>5</sup> For this purpose, options to purchase the underlying asset prior to the transfer of ownership are not considered options to terminate.

FN 5 - See SFFAS 6, par. 26A.

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**Commented [PR(2):** Staff recommendation 2, option 1. See staff analysis for an illustration of option 2.

6. Paragraph 42 of SFFAS 54 and the previously-issued amendment thereto (SFFAS 60, par. 19) are amended as follows:

42. The future lease payments should be discounted using the interest rate the lessor charges the lessee. If the interest rate is not stated in the lease, the interest rate should be based on the interest rate on marketable Treasury securities at the commencement of the lease term (or at the subsequent financial reporting date in accordance with par. 44), with a similar maturity to the term of the lease. ~~lessee's estimated incremental borrowing rate<sup>7</sup> (the estimated rate that would be charged for borrowing the lease payment amounts for the lease term) should be used.~~

FN 7—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.

7. Paragraphs 42A-42C are added to SFFAS 54 as follows:

42A. If the interest rate is based on marketable Treasury securities, it should be consistent with the interest rate on marketable Treasury securities at the commencement of the lease term, in accordance with paragraphs 40 and 42 (or the interest rate on marketable Treasury securities on the subsequent financial reporting date, in accordance with par. 46 and 48). The interest rate may be based on a recent interest rate on marketable Treasury securities or historical average interest rate on marketable Treasury securities of a similar maturity to the term of the lease, provided that the interest rate is consistent with the interest rate on marketable Treasury securities on the commencement of the lease term (or subsequent financial reporting date).

42B. When selecting an interest rate based on marketable Treasury securities of similar maturity to the term of the lease, reporting entities may round up or down to the nearest maturity or interpolate the interest rate for the period between two maturities. The methodology for selecting an interest rate based on marketable Treasury security maturities should be consistent from period to period.

42C. Reporting entities should not extrapolate beyond the longest Treasury maturity when the lease term exceeds it; rather, reporting entities should select the longest Treasury maturity. For example, if the longest Treasury maturity at commencement of the lease term is 30 years, reporting entities should select the 30-year rate as the discount rate for a lease with a 75-year term.

8. Paragraphs 47 and 48 of SFFAS 54 are amended as follows:

47. A lease liability is not required to be remeasured, nor is the discount rate required to be reassessed, solely for a change in the interest rate on marketable Treasury securities ~~lessee's estimated incremental borrowing rate.~~

48. If the discount rate is required to be updated based on the provisions in paragraph 46, the discount rate should be based on the revised interest rate the lessor charges the lessee at the time the discount rate is updated. If that interest rate cannot be readily determined, the interest rate on marketable Treasury securities with a similar maturity to the term of the lease ~~lessee's estimated incremental borrowing rate at the time the discount rate is updated should be used (see par. 42-42C above).~~

9. Paragraph 59 of SFFAS 54 and the previously-issued amendment thereto (SFFAS 60 par. 25) are amended as follows:

59. The future lease payments to be received should be discounted using the interest rate the lessor charges the lessee. If the interest rate is not stated in the lease, the interest rate should be based on the interest rate on marketable Treasury securities at the commencement of the lease term (or at the subsequent financial reporting date in accordance with par. 61), with a similar maturity to the term of the lease ~~lessor's estimated incremental borrowing rate should be used.~~<sup>9A</sup>

FN 9A—A federal lessor'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.

10. Paragraphs 59A-59C are added to SFFAS 54 as follows:

59A. If the interest rate is based on marketable Treasury securities, it should be consistent with the interest rate on marketable Treasury securities at the commencement of the lease term, in accordance with paragraphs 56 and 59 (or the interest rate on marketable Treasury securities on the subsequent financial reporting date, in accordance with par. 63). The interest rate may be based on a recent interest rate on marketable Treasury securities or historical average interest rate on marketable Treasury securities of a similar maturity to the term of the lease, provided that the interest rate is consistent with the interest rate on marketable Treasury securities on the commencement of the lease term (or subsequent financial reporting date).

59B. When selecting an interest rate based on marketable Treasury securities of similar maturity to the term of the lease, reporting entities may round up or down to the nearest maturity or interpolate the interest rate for the period between two maturities. The methodology for selecting an interest rate based on marketable Treasury security maturities should be consistent from period to period.

59C. Reporting entities should not extrapolate beyond the longest Treasury maturity when the lease term exceeds it; rather, reporting entities should select the longest Treasury maturity. For example, if the longest Treasury maturity at commencement of the lease term is 30 years, reporting entities should select the 30-year rate as the discount rate for a lease with a 75-year term.

11. Paragraph 61 of SFFAS 54 is amended (without amendment to its sub-paragraphs or footnote) as follows:

61. The lessor should remeasure the lease receivable at subsequent financial reporting ~~dates~~ periods if one or more of the following changes have occurred at or before that financial reporting ~~date~~ period, based on the most recent lease contract or agreement

before the changes,<sup>10</sup> and the changes individually or in the aggregate, are expected to significantly affect the amount of the lease receivable since the previous measurement:

12. Footnote 11 to paragraph 89 of SFFAS 54 is amended as follows:

89. Sale-leaseback transactions involve the sale of an underlying asset by the owner and a lease of the property back to the seller (original owner). A sale-leaseback should include a transaction that qualifies as a sale<sup>11</sup> to be eligible for sale-leaseback accounting. A sale-leaseback transaction that does not include a transaction that qualifies as a sale should be accounted for as a borrowing by both the seller-lessee and the buyer-lessor.

FN 11 – See SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, par. 295 (with the public) and par. 314-315 (intragovernmental).

13. Paragraph 92 of SFFAS 54 is amended as follows:

92. A seller-lessee should disclose the terms and conditions of sale-leaseback transactions as part of ~~in addition to~~ the disclosures required of a lessee (par. 37 or 54, as applicable). A buyer-lessor should disclose the terms and conditions as part of ~~provide~~ the disclosures required of a lessor (par. 38 or 67, as applicable).

#### EFFECTIVE DATE

14. The requirements of this Statement are effective for reporting periods beginning after September 30, 2023.

The provisions of this Statement need not be applied to information if the effect of applying the provision(s) is immaterial. Refer to Statement of Federal Financial Accounting Concepts 1, *Objectives of Federal Financial Reporting*, chapter 7, titled *Materiality*, for a detailed discussion of the materiality concepts.

## APPENDIX A: BASIS FOR CONCLUSIONS

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 proposed Statement—not the material in this appendix—would govern the accounting for specific transactions, events, or conditions.

This Statement may be affected by later Statements. The FASAB Handbook is updated annually and includes a status section directing the reader to any Statements that affects this Statement. Within the text of the Statements, the authoritative sections are updated for changes. However, this appendix will not be updated to reflect subsequent changes. The reader can review the basis for conclusions of amending Statements for the rationale for each amendment.

### PROJECT HISTORY

- A1. The Federal Accounting Standards Advisory Board (FASAB or “the Board”) issued SFFAS 54, *Leases*, in April 2018 with an effective date for reporting periods beginning after September 30, 2020. The effective date was later amended by SFFAS 58, *Deferral of the Effective Date of SFFAS 54, Leases*, to reporting periods beginning after September 30, 2023.
- A2. FASAB and the Accounting and Auditing Policy Committee (AAPC) commenced projects on their technical agendas to identify implementation challenges and develop guidance related to SFFAS 54.
- A3. The AAPC assembled a large group of task force members—over 100 stakeholders—to identify and analyze numerous SFFAS 54 implementation topics.
- A4. In June and August 2020, the Board discussed omnibus amendments candidates identified by project staff and the task force to include in the exposure draft (ED) of an initial omnibus amendments proposal (the proposal was eventually approved and issued as SFFAS 60). The Board considered input provided by ED respondents and the task force during due process.
- A5. Some respondents and task force members requested additional guidance on the selection and use of incremental borrowing rate estimates to discount lease liabilities and receivables. One respondent suggested that the Board clarify whether sale-leaseback requirements under paragraphs 89-92 of SFFAS 54 apply to intragovernmental transactions (see SFFAS 60, Basis for Conclusions, par. A8.b and A8.d). The Board decided to address those outstanding issues through subsequent actions.
- A6. Following the issuance of SFFAS 60, the leases implementation task force recommended that the Board clarify numerous aspects of SFFAS 54, paragraphs 42 and 59, which provided for the use of estimated incremental borrowing rates to discount lease liabilities and receivables. These recommendations were consistent with those raised by respondents to the ED of SFFAS 60.

- A7. The Board considered numerous factors when evaluating paragraphs 42 and 59 of SFFAS 54 and developing omnibus amendments:
- a. Elements identified by task force members as requiring additional clarification
  - b. Technical implementation issues for entities with independent borrowing authorities
  - c. Cost-benefit considerations and qualitative characteristics of information in financial reports
    - i. Paragraphs 152-153 of Statement of Federal Financial Accounting Concepts (SFFAC) 1, *Objectives of Federal Financial Reporting*, provide that accounting standards can have many different kinds of effects that must be considered, including effects on the activities of accountants and auditors. It also provides that the Board must be aware of these potential effects when considering the costs and benefits of any given accounting alternative. In this particular context, the Board considered potential effects on costs of implementation, auditability, and consistent application when assessing the level of detail needed.
    - ii. Paragraph 160 of SFFAC 1 provides that reliability can be affected by the degree of estimation in the measurement process and uncertainties inherent in what is being measured.
    - iii. Paragraph 164 of SFFAC 1 provides that differences among financial reports should be caused by substantive differences in the underlying transactions or organizations rather than by the mere selection of different alternatives in accounting practices.
  - d. Approaches used in the following documents
    - i. SFFAS 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits* (par. 28-32)
    - ii. Governmental Accounting Standards Board (GASB) Statement 87, *Leases*<sup>2</sup>
    - iii. Financial Accounting Standards Board Accounting Standards Update 2021-09, *Discount Rate for Lessees that Are Not Public Business Entities*
- A8. The Board discussed its original intent to subject intragovernmental sale-leasebacks to the requirements of paragraphs 89-92 of SFFAS 54. The Board agreed that the original intent was not sufficiently clear due to an absence of references to intragovernmental transaction guidance, including paragraphs 314-315 of SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, and paragraphs 37-38 of SFFAS 54.
- A9. In light of these considerations, the Board agreed to propose omnibus amendments to clarify the discounting of lease liabilities and receivables (par. 42, 47-48, and 59 of SFFAS

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54) and the scope and applicability of sale-leaseback requirements (par. 89-92 of SFFAS 54) to intragovernmental leases.

#### SUMMARY OF OUTREACH AND RESPONSES

- A10. The Board released an exposure draft (ED) proposal on May 9, 2022, for public comment, with comments requested by July 8, 2022. Upon release of the ED, FASAB notified constituents through the FASAB website and listserv, the Federal Register, and FASAB newsletter. FASAB also provided news releases to its press contacts, including various news organizations and committees of professional associations generally commenting on EDs in the past. To encourage responses, a reminder notice was provided to FASAB's listserv near the comment deadline.
- A11. Sixteen comment letters were received in response to the ED. Respondents were generally supportive of the proposed Statement. In response to comment letters, the Board identified and agreed upon further changes to improve the technical clarity the proposal and the related guidance in SFFAS 54.
- A12. The Board and its technical staff consulted with GASB technical staff in response to feedback received from respondents related to lease term guidance. The Board elected to implement additional clarifying omnibus amendments in paragraphs 19 and 25 in response to these consultations. The Board believes these amendments will assist reporting entities with consistently evaluating a range of contract and agreement provisions and determining whether an option to terminate exists and its effect, if any, on lease term and the identification of contracts or agreements that transfer ownership. The omnibus amendments to these paragraphs are generally consistent with those implemented by the GASB under GASB Statement 99, *Omnibus Amendments 2022*.<sup>3</sup>
- A13. Improvements and additional changes included:
- Improving consistency in terminology and linkage across interacting paragraphs to enhance clarity of the original omnibus proposals.
  - Clarifying the treatment of purchase options and defaults on payments for purposes of determining whether or not such provisions represent an option to terminate. Adding explanatory language to the end of sub-paragraph 19.b of SFFAS 54 to clarify that the sub-paragraph is strictly intended to interact with sub-paragraph 19.a rather than otherwise affect aspects of lease term measurements that are not relevant to paragraph 19.a provisions.
  - Aligning phrasing in paragraphs 44 and 61 of SFFAS 54.
- A14. The Board considered other input provided by respondents that did not result in further modifications to the Statement.
- A few respondents expressed concerns that paragraph 42B and 59B guidance may not be applied consistently to the leases in reporting entities' respective lease portfolios. The Board considered these comments and decided that the criteria for entities to follow *methodologies* consistently from period to period (as provided for

<sup>3</sup> Ibid.

under par. 42B and 59B) sufficiently provides for such consistency. The discounting of future lease payments under paragraphs 42-42C and 59-59C inherently involves the application of sound, objective, and reasonable professional judgments when developing and implementing accounting procedures or practices. The Board believes that these paragraphs help inform those professional judgments, while providing reasonable guardrails in support of the qualitative characteristics of reliability, consistency, and comparability (see SFFAC 1, par. 160, 163-164).

- b. One respondent noted that the options for selecting interest rates could lead to inconsistencies in values between sub-components within larger reporting entities. SFFAS 47, Reporting Entity, paragraph 68, provides that consolidated component reporting entities may consolidate sub-component reporting entity statements prepared in accordance with SFFAS 34 without conversation for any differences in accounting policies among the organizations. As previously mentioned, the Board believes that this guidance provides sufficient criteria in support of reliability, consistency, and comparability. Additionally, consolidated reporting entities and their sub-components may manage and harmonize their accounting policies at their discretion for purposes of further supporting these qualitative characteristics.
- c. A few respondents requested that the Board directly reference or hyperlink to a source of marketable Treasury securities to facilitate compliance with the requirements. It is not the role of the Board to provide this information in its pronouncements. The Board must be mindful that information sources and hyperlinks can change, thus it cannot provide such information in its pronouncements.

#### BOARD APPROVAL

A15. Pending

## APPENDIX B: ABBREVIATIONS

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AAPC	Accounting and Auditing Policy Committee
ED	Exposure Draft
FASAB	Federal Accounting Standards Advisory Board
FAF	Financial Accounting Foundation
GASB	Governmental Accounting Standards Board
SFFAC	Statement of Federal Financial Accounting Concepts
SFFAS	Statement of Federal Financial Accounting Standards

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## Leases Project Plan

	<u>Deferral</u> SFFAS 58	<u>Implementation Guidance</u> TR 20 Updates To TR 20	<u>Omnibus</u> SFFAS 60 SFFAS TBD	<u>Leases-Related</u> <u>Intragovernmental RWAs</u> TB TBD	Training / Outreach
FY 2020	Draft Exposure Period Finalize Issuance SFFAS 58 ISSUED	Draft	Research Draft		Provide
FY 2021		Exposure Period Finalize / Approve Research	Exposure Period Finalize / Approve Research	Research Draft	Provide
FY 2022		Issuance TR 20 ISSUED Research	Issuance SFFAS 60 ISSUED Research Draft Exposure Period Finalize	Research Draft Exposure Period Finalize	Provide
FY 2023 Q1		Research	Finalize / Approve Issuance ( <i>original plan</i> )	Finalize / Approve (target)	Draft FY 23 content
FY 2023 Q2		Draft	Projected Issuance <i>Behind schedule</i>	Finalize / Approve (projected) Issuance ( <i>original plan</i> )	Provide
FY 2023 Q3		Draft Exposure Period		Target Issuance	Provide
FY 2023 Q4		Finalize / Approve Target / Projected Issuance		Projected Issuance <i>Behind schedule</i>	Provide
FY 2024 Q1	SFFAS 54 effective				

Last updated: November 2022.