

Memorandum

Leases Educational Session

February 5, 2025

To: Members of the Board
From: Ricky A. Perry, Jr.
Thru: Monica R. Valentine, Executive Director
Subject: Leases Education Session: Technical Inquiry Data Analysis - **Topic C.2**

OBJECTIVE

SFFAS 54, *Leases*, became effective in fiscal year 2024. At the February meeting, staff will present an educational session analyzing leases technical inquiries submitted between October 1, 2023, and February 1, 2025 (attachment 1). The Board will have the opportunity to discuss these data and ask questions at the meeting.

REQUEST FOR FEEDBACK BY FEBRUARY 20TH

Prior to the February meeting, please review the attached educational material.

Responses to the enclosed educational materials are not requested; however, members may submit questions or comments in advance of the meeting. Please submit any questions or comments to Mr. Perry, with a cc to Ms. Valentine, by February 20th.

NEXT STEPS

Not applicable.

ATTACHMENTS

1. Staff analysis / educational session material

REFERENCE MATERIALS

None

Staff Analysis

Leases Educational Session

February 5, 2025

Attachment 1

INTRODUCTION

The effective reporting period for implementation of SFFAS 54, *Leases*, began in fiscal year (FY) 2024. The Board previously agreed to monitor implementation of the standard. The objective of this report is to discuss a key component of those monitoring efforts—tracking and analysis of technical inquiry data.¹

RESULTS IN BRIEF

This educational session presentation on leases technical inquiries includes:

- staff observations on common technical inquiry leases topic areas,
- the sufficiency of the standards to address technical inquiries, and
- future guidance candidates.

Overall, staff found that the leases post-issuance project, including omnibus amendments, transitional amendment, and implementation guidance, have been helpful to practitioners. The volume of technical inquiries during implementation was considerably lower than expected and inquiries were adequately addressed by the extant standards and guidance.

METHODOLOGY

To respond to leases technical inquiries, staff first assessed the answerability of the question to develop a response strategy (formal or informal) based on factors, such as:

- the nature and formality of the submission,
- the specificity-level of the question,
- whether the question was broadly applicable or frequently raised,
- whether applicable sections of the standard were identified,
- the adequacy of any fact patterns provided to clarify the appropriate application of the standards,

¹ A part-time detailee was assigned to assist with efforts to monitor SFFAS 54 technical inquiries during the period of implementation, beginning in FY 2024. This detail assignment included: (1) researching, analyzing, and drafting responses to technical inquiries that were submitted to FASAB staff by federal financial management personnel; (2) assisting the FASAB leases project manager in critically evaluating the sufficiency of technical inquiry submissions and identifying additional informational needs and technical assistance risks associated with the inquiries; and (3) facilitating the tracking and analysis of leases-related technical inquiries over the course of the detail.

- whether the inquiry involved a dispute or other sensitive matter, and
- and whether the question fell within the scope of FASAB's standards.

Staff consulted with the executive director when determining an approach and formulating responses. Each response appropriately noted that staff analysis and response is not intended to reflect authoritative views of FASAB or a majority view of its staff. Official positions of FASAB are determined only after extensive due process and deliberations. Furthermore, management is responsible for the preparation and fair presentation of the financial statements in accordance with generally accepted accounting principles, and management may not delegate its own judgment.

To track and analyze the leases technical inquiries, staff logged each inquiry and categorized them by paragraph references, topic areas, and whether the inquiries were addressed by existing guidance or would be good candidates for future clarifying amendments or updates to implementation guidance. Inquiries were categorized by topic area(s) as a matter of judgment through discussion between the detailee and the leases project manager after reviewing documentation and guidance related to the inquiry. These topic area categories were then compiled to identify trending topics and the rate at which the existing standards sufficiently addressed them.

To identify candidates for future guidance, the detailee and FASAB leases project manager considered (a) the prevalence of the issue, and (b) whether there were existing references to the topic in the standards that could be clarified with implementation guidance or whether an omnibus amendment may be necessary to address it under the Board's rules of procedure.

ANALYSIS

Technical inquiry topic areas

This report primarily focuses on the results of data found during and after the period of implementation (submitted between October 1, 2023, and February 1, 2025, as these technical inquiries better indicated where entities were having difficulty understanding or applying the new lease standards. Technical inquiries leading up to the period of implementation (FY 2023 and prior) tended to be broader questions (i.e., "What is required for reporting and disclosure?") or inquiries regarding ongoing Board deliberations or pending decisions during the implementation guidance, omnibus, or transitional amendment projects.

During this 16-month period, leases technical inquiries focused on a range of topics. Most technical inquiries related to sections of SFFAS 54 related to implementation of the new standard, whether contract/agreements fit the definition of a lease (scope), how those leases should be classified, and how elements of the lease should be recognized.

Figure 1: Common Topics of Leases Technical Inquiries

SFFAS 54 ¶	Topic area category	Count
1-5	Scope	7
6-13	Definitions	3
14-21	Lease Term	2
22-24	Short-Term Leases	0
25	Contracts or Agreements that Transfer Ownership	0
26-38	Intragovernmental Leases	6
39-54	Lessee Recognition, Measurement, and Disclosures for Leases Other than Short-Term Leases, Contracts or Agreements that Transfer Ownership, and Intragovernmental Leases	8
55-68	Lessor Recognition, Measurement, and Disclosures for Leases Other than Short-Term Leases, Contracts or Agreements that Transfer Ownership, and Intragovernmental Leases	5
69	Financial Report of the U.S. Government Disclosures	0
70-71	Lease Incentives and Lease Concessions	3
72-77	Contracts or Agreements with Multiple Components	2
78-79	Contract or Agreement Combinations	4
80-86	Lease Terminations and Modifications	1
87-88	Subleases	0
89-92	Sale-Leaseback Transactions	0
93	Lease-Leaseback Transactions	0
96-97	Implementation	8
98	Effective Date	0

High frequency (> 5)	Moderate frequency (3-5)	Low frequency < 3
----------------------	--------------------------	-------------------

The emphasis on implementation and lease categories made sense, as practitioners navigated where to locate information in the new standard and determined how to transition from the old standard during the effective reporting period. However, those topics will likely be seen less in technical inquiries going forward as practitioners become accustomed to navigating and applying the new standard in the future.

Special topics that were most asked about included disclosure requirements, embedded leases, advances/prepayments, and intragovernmental reimbursable work agreements. Many of these topics are more nuanced and may be a matter of management judgment.

Sufficiency of existing standards and guidance

Staff evaluated the rate at which technical inquiries were covered by existing standards and guidance, including applicable Statements, Technical Releases, and Technical Bulletins.² These determinations were made through review of the technical inquiries and discussions between the detailee and the leases project manager.

² The primary sources cited in response to leases technical inquiries included SFFAS 54, *Leases*, as amended; Technical Release 20, *Implementation Guidance for Leases*; and Technical Bulletin 2023-1, *Intragovernmental Leasehold Reimbursement Work Agreements*.

For the 16-month period, 98% of technical inquiries were considered sufficiently addressed by the standards. Forty-one of the 42 technical inquiries were directly addressed or explained in the standards and guidance, while one of 42 inquiries pertaining to a low-frequency topic area (see fig. 1 above) was partially addressed or explained in the standards and guidance. The affected parties were able to reach a resolution on all 42 inquiries.

Overall, staff found that the standards and guidance sufficiently addressed the technical inquiries submitted. Technical inquiries were readily answerable, allowing staff to cite standards and guidance in responding to the inquiries of practitioners. Many of the citations provided by staff were affected by promulgated during the post-issuance phase of the leases project (i.e., clarifying omnibus amendments that amended SFFAS 54 and implementation guidance provided by Technical Release 20).

The volume of technical inquiries, both formal and informal, totaling 42 inquiries during the 16-month period, serves as another indicator regarding the effectiveness of the Board's post-issuance activities. The Board's post-issuance activities resulted in a lower-than-expected and manageable volume of technical inquiries during the 16-month period.

Staff will continue to receive and record technical inquiries and any omnibus amendment or implementation guidance candidates that are identified, consult with the executive director and the Board as necessary, and bring candidates before the Board for discussion when appropriate.

Omnibus amendment candidates

Staff has not identified any omnibus amendment candidates at this time. As noted above, nearly every inquiry submitted during the 16-month period between October 1, 2023, and February 1, 2025, was considered adequately addressed by the standards and guidance. These inquiries generally required directing the individual(s) to the applicable paragraph reference(s) that the submitter may have been unfamiliar or inexperienced with applying. Many of the common questions submitted during the year of implementation will become less relevant and frequent after the initial period of implementation as practitioners improve and solidify their accounting policies. For example, prospective implementation requirements and initial recognition and measurement questions are expected to be less prevalent going forward. Staff expects complex inquiries may continue to be submitted from time to time, however. Those that warrant Board action will be brought before the Board for discussion.

As previously discussed with the Board, staff has continued to monitor certain aspects of the standard to determine whether clarifying omnibus candidates may emerge. For example, in FY 2024 practitioners raised tentative concerns regarding PP&E unit-of-account issues during a government-wide leases working group meeting regarding implementation of paragraph 67.b of SFFAS 54. Paragraph 67.b requires lessors to report the carrying amount of assets on lease by major classes of assets, and the amount of related accumulated depreciation. Staff collected lessor disclosure data to

analyze the implementation of this requirement. Staff was particularly interested in reviewing GSA's implementation of the requirement, because GSA often leases only small portions of its buildings to non-intragovernmental lessees (e.g., retail space at the street level), while the remainder of the buildings are leased to intragovernmental customers. Upon review, staff found that lessors, including GSA, appropriately implemented the requirement in a representationally faithful manner based on the nature of their portfolios of PP&E assets on lease.³ Accordingly, staff does not view omnibus amendment action on this disclosure requirement as necessary, provided that members agree with staff's analysis of lessor reporting results.⁴

Implementation guidance candidates

Topics that may be considered good candidates for future implementation guidance are often those that are common and broadly applicable, pertain to topics that have not been previously answered or may be difficult to interpret, and/or are needed to clarify cross-cutting standards issues.

Staff has previously discussed an intention to compile implementation guidance candidates so that the Board may consider a second update to Technical Release 20, *Implementation Guidance for Leases*, once a sufficient number of candidates are identified.⁵ In earlier discussions with the Board it was generally agreed that a minimum of 8-10 candidates would likely be appropriate. To date staff has identified three implementation guidance topic candidates. Staff does not view any of these three candidates as being urgent in nature.

Candidates

1. Contract combinations. Reporting entities may enter into a lease for a single underlying asset unit that is substantially similar to a group of other underlying asset units recently leased as part of a larger contract. There are no bright-line criteria under paragraph 78 of SFFAS 54 for contracts or agreements entered into "at or near the same time." A question-and-answer scenario could discuss why treating these contracts or agreements as separate leases rather than a combination could have implications associated with unit of account, such as capitalization thresholds. (SFFAS 54, par. 78-79)
2. Substantive right of substitution. Reporting entities may lease an underlying asset, such as equipment, on the condition that a vendor replace it if it fails during the lease term (substantive right of substitution). A guidance scenario could discuss why it is appropriate to amortize the lease asset over the lease

³ See topic C.1, p. 14 of 21, paragraph 67.b disclosures.

⁴ Ibid.

⁵ The first update to Technical Release 20 was Technical Release 22, *Leases Implementation Guidance Updates*, which was issued in October 2023.

term rather than the useful life of the underlying asset in cases when a substantive right of substitution is present. (SFFAS 54, par. 50-51)

3. Escalation rates. Reporting entities occasionally enter into leases with an escalation rate. Escalation rates are annual rental increases *fixed into the lease contract or agreement*. Some lease contracts may disclose a base rent amount along with an escalation rate, while other lease contracts may disclose a schedule that reflects rent escalation. In both cases, the amounts are fixed rent payments, and the escalation rate does not represent the interest rate. A question-and-answer scenario could explain the difference between escalation rates and interest rates and contrast the effects of each on measurement of lease liabilities. (SFFAS 54, par. 40.a and 42)

Concluding Remarks

Staff will continue to monitor SFFAS 54 implementation and reporting in fiscal year 2025 through tracking and analysis of technical inquiries, outreach with practitioners and central agencies, and analysis and collection of omnibus and implementation guidance candidates that may come to the attention of staff.