

Omnibus Amendments: Technical Clarifications Addressing Lessee and Lessor Discount Rates and Sale-leasebacks

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Please provide your name.

Name: Cecilia Coates, Deputy Comptroller

Please identify your organization, if applicable.

Organization: Department of State: Bureau of the Comptroller and Global Financial Services, Bureau of Overseas Buildings Operations

Please email your responses to fasab@fasab.gov. If you are unable to respond by email, please call (202) 512-7350 to make alternate arrangements.

This proposed Statement would address certain ongoing areas of concern related to leases implementation that were not addressed in SFFAS 60, *Omnibus Amendments 2021*, including:

- 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; and
- clarifying the applicability of paragraphs 89-92 of SFFAS 54 to intragovernmental sale-leasebacks and the disclosure requirements applicable to them

QFR 1 Do you agree or disagree with the proposed amendments to address discounting lease liabilities and receivables, as reflected in paragraphs 3-7 (amending par. 42, 47-48, and 59 of SFFAS 54), and the Board's basis for such proposals? Please provide the rationale for your answer.

QFR 2 Do you agree or disagree with the proposed amendments to clarify the applicability of paragraphs 89-92 of SFFAS 54 to intragovernmental sale-leasebacks and the disclosure requirements applicable to them, as reflected in paragraphs 8-9, and the Board's basis for such proposals? Please provide the rationale for your answer.

RESPONSE:

The Department of State (State) has reviewed and generally agrees with the approach on the Omnibus Amendments: *Technical Clarifications Addressing Lessee and Lessor Discount Rates and Sale-leasebacks*. Based on our preliminary review, we see no issues complying with these clarifications at this time.

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However, State has the following additional concerns and comments on the SFFAS 54 [Leases](#), SFFAS 58 [Deferral of the Effective Date of SFFAS 54, Leases](#), and the Implementation Guidance outlined in Technical Release 20, specifically question 91 as it relates to the treatment of overseas residential leases.

The overseas residential leases administered by State but occupied by other Federal agency employees are unique in their business process and do not align with traditional and expected lease scenarios as outlined in SFFAS 54 in the following manner:

- State does not execute subleases or occupancy agreements to Federal agencies.
- State does not establish reimbursable agreements, bill or collect reimbursement (i.e., cash consideration) from agencies operating overseas.
- State operates with disbursing authority to make payments for Federal agencies to include payments in foreign currencies, such as for lease payments to landlords.
- State does not pay landlords on behalf of agencies who do not provide their appropriate funds cite timely. Instead, they work with the agency to obtain the fund cite. State funds do not back overseas residential leases.

We appreciate FASAB's initial consideration of these scenarios and the guidance provided under TR 20, question 91 as well as the continued support we receive through the Lease Task Force. However, State identified remaining gaps in our ability to effectively implement the guidance as promulgated by FASAB when State has assisted other agencies with obtaining leases with services provided through the Interagency Cooperative Administrative Support Services (ICASS), the shared administrative services platform at overseas posts. As a result of these outstanding unique accounting challenges, State cannot finalize the accounting entries, processes and system requirements and execute the associated financial reporting preparation and system implementations without further guidance. *Therefore, State is requesting 1) that SFFAS 58 [Deferral of the Effective Date of SFFAS 54, Leases](#), be modified to allow State and other agencies two additional years (FY2026) to continue to address these challenges, and 2) that TR20, question 91, be removed or modified.*

Justification for extending the implementation date as outlined in SFFAS 58:

- SFFAS 54 and associated guidance do not provide sufficient clarity to apply to the unique nature of leases administered by State but occupied by other agency employees overseas. As we outline in further detail below, State cannot implement SFFAS 54 in accordance with TR 20 question 91 as provided currently because State does not receive (or record) revenue nor make (or record) payments (expenses). State's association with lease payments for leases occupied by non-State employees overseas is as a Disbursing Office akin to Treasury and is not associated with State's financial records. State needs additional time to engage with FASAB Staff and identify accounting entries that will satisfy the intent of SFFAS 54 without requiring significant changes and costs to the business processes for arranging and paying for housing for Federal employees serving at overseas posts. The options we identified during preliminary discussions with FASAB Staff (described below) involve unprecedented and complex accounting scenarios, without resolution to the underlying issues.
 - Scenario A: State is considered a lessee for leases where another agency pays for the lease directly. In this situation, to calculate the lease liability, draw down on the liability over time

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without cash exchanged, and recognize the always unfunded nature of the lease liability, we will need to consider how to account for consideration that is not in the form of a payment from State to the landlord (i.e., State budgetary resources will never fund non-State occupied lease payments).

- Scenario B: State is considered a lessor to other agencies under sublease. In this situation we will need to consider how to recognize sublease revenue without sublease agreements, reimbursable agreements, and payments directly from other agencies.

In each of these instances, State needs additional time to determine whether existing FASAB standards can be used in conjunction with SFFAS 54 to resolve the implementation challenges or if new guidance will be required from FASAB and/or Treasury.

- System Updates – State has been working to identify, analyze and document the significant changes needed for our lease, property inventory and global accounting systems. As noted by other agencies such as the Department of Interior and the Department of Veterans Affairs, the complexity of the standard along with the interpretations and judgments required to facilitate establishing new procedures, policies, systems functionality and the substantial amount of testing required for the systems takes time, substantial resources and investment. State uses an off-the-shelf financial system to conduct our global operations. State anticipates the basic lease functionality from our global financial system vendor, which services many impacted Federal agencies, to be available in Spring 2024. However, establishing the accounting requirements and the subsequent impact to financial systems has been and will continue to be further delayed as long as the accounting for overseas residential leases is uncertain. This uncertainty impacts lease reporting for over 30 customer agencies.

Given the complex nature of these processes, the impact it has to State and other agencies' operations, and our need to successfully update our systems, policies and procedures around this treatment and the overall SFFAS 54 implementation, we are concerned about our implementation timeline and the resources needed to be compliant by FY 2024.

Justification for the removal or modification of TR 20, question 91

State has identified implementation issues as it relates to SFFAS 54 in conjunction with TR20, question 91. Our concerns are as follows:

1. **TR 20, question 91, asserts State is a lessee with a third party, but State cannot account for leases where payments are not made to a lessor [landlord] with State funding.** SFFAS 54 paragraph 6, states: "A lease is defined as a contract or agreement whereby one entity (lessor) conveys the right to control the use of PP&E (the underlying asset) to another entity (lessee) for a period of time as specified in the contract or agreement in exchange for **consideration**." While consideration is not defined under the standard as "payment" or "cash", paragraph 40 requires the recognition of the lease liability be measured at the present value of **payments**, including fixed payments, variable payments, and other probable payments. This liability is then drawn down as payments are made to the lessor, including the amortized lease interest expense. In many cases, as outlined further below, State is not responsible for, and does not receive funding to pay for these leases. State's association with lease payments for leases occupied by non-State employees overseas is as a Disbursing Office akin to the Department of Treasury and is not associated with State's financial records. Given the guidelines in SFFAS 54, we are unable to determine how State would assert we are a lessee and

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account for the corresponding liability and liquidation when no revenue is received, and no disbursement (expense) is made.

2. **TR 20, question 91, also asserts State is a lessor and other agencies are in a sub-lease relationship with State, but State cannot account for lease revenue as required in paragraph 38 of SFFAS 54.** Under paragraph 38, point b, agencies are required to disclose “Future lease **payments** that are to be received to the end of the lease term for each of the five subsequent fiscal years and in five-year increments thereafter”. State is unable to implement this requirement as we do not receive payments from other agencies for these leases. Rather, the occupying agencies’ funds are used to pay the landlord directly in accordance with the original lease. State does not receive lease payments from the occupying agencies and therefore does not recognize rent revenue associated with these leases in accordance with GAAP. State also does not have sub-lease, occupancy, or reimbursable agreements with other agencies related to these rent payments.
3. If the guidance is not modified or clarified, and State is expected to strictly adhere to TR20 as written, then State and more than 30 agencies would take on an undue ongoing burden to revise current effective and accountable operational business process for overseas leasing and housing support that were designed specifically to achieve efficiencies and reduce the administrative burden of administrative services overseas. In light of the Board’s efforts to contain and minimize the implementation costs of SFFAS 54, **we believe this is not the intention of the Board.**

While we agree this population of leases should be accounted for within the Government-wide portfolio, we are still unclear as to how these leases should be accounted for by State or other agencies and are requesting additional engagement with FASAB Staff and the impacted agencies and additional guidance or changes to the standard so that we may comply. Through our implementation planning and reviews of SFFAS 54, State believes that we have an effective and appropriate treatment for these leases that will comply with SFFAS 54 and provide each agency with accurate lease populations and amounts for reporting. We request the opportunity to discuss the accounting challenges and options to resolve these challenges in more detail with FASAB. This affects over 14,500 leases, over 5,000 of which are occupied by non-State employees and is significant to State’s financial statements.

We are providing additional background on the overseas residential lease population in the flowchart and paragraphs below. We additionally outline key differences between the Overseas leasing process and the traditional domestic leasing processes.

We appreciate FASAB’s assistance on this matter to date. We thank FASAB for consideration in these matters and look forward to ongoing collaboration to address them, to allow for clarified, auditable financial reporting.

Overseas Residential Leasing Portfolio - Background:

State administers (acts as the real estate and signing agent for) leases for Federal agencies with employees who reside overseas per the *Foreign Service Buildings Act of 1926*. Over 14,500 leases are established across 245 posts in 169 countries within housing pools to accommodate the needs of State and over 30 agencies with employees serving in overseas positions. State employees represent approximately 60% of housing pool assignments. Leases are assigned through IAHBs (comprised of multiple agency representatives at each post) based on the Federal employee’s tour length, rank and family size, without regard to the employee’s home agency. Housing assignments are documented in

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the IAHB minutes, but no formal lease or occupancy agreement is executed beyond the original lease with the landlord. Occupying agency employee overseas assignment lengths can vary across the lease term (i.e., a 9-year lease could have 3 tenants for 3 years each from different occupying agencies).

Once an agency employee is assigned to a lease within the housing pool, the employee's agency is required to pay rent and rent-related operating costs directly to the landlord based on the terms of the original lease agreement for the duration of the employee's assignment until the residence is reassigned, up to 90 days following move out. State does not cover non-payments or late payment penalties assessed on these leases. If an agency needs to adjust an employee assignment (i.e., early termination), the lease goes back to the IAHB for reassignment to another incoming employee who meets the lease criteria or is considered for termination, depending on the needs of the overall housing pool participants. These processes were put in to place with the goal of reducing the administrative burden and costs of potentially redundant processes by multiple agencies abroad and continuously rotating U.S. Government personnel. Refer to the below flowchart of the overseas residential housing leasing, assignment and disbursing processes.

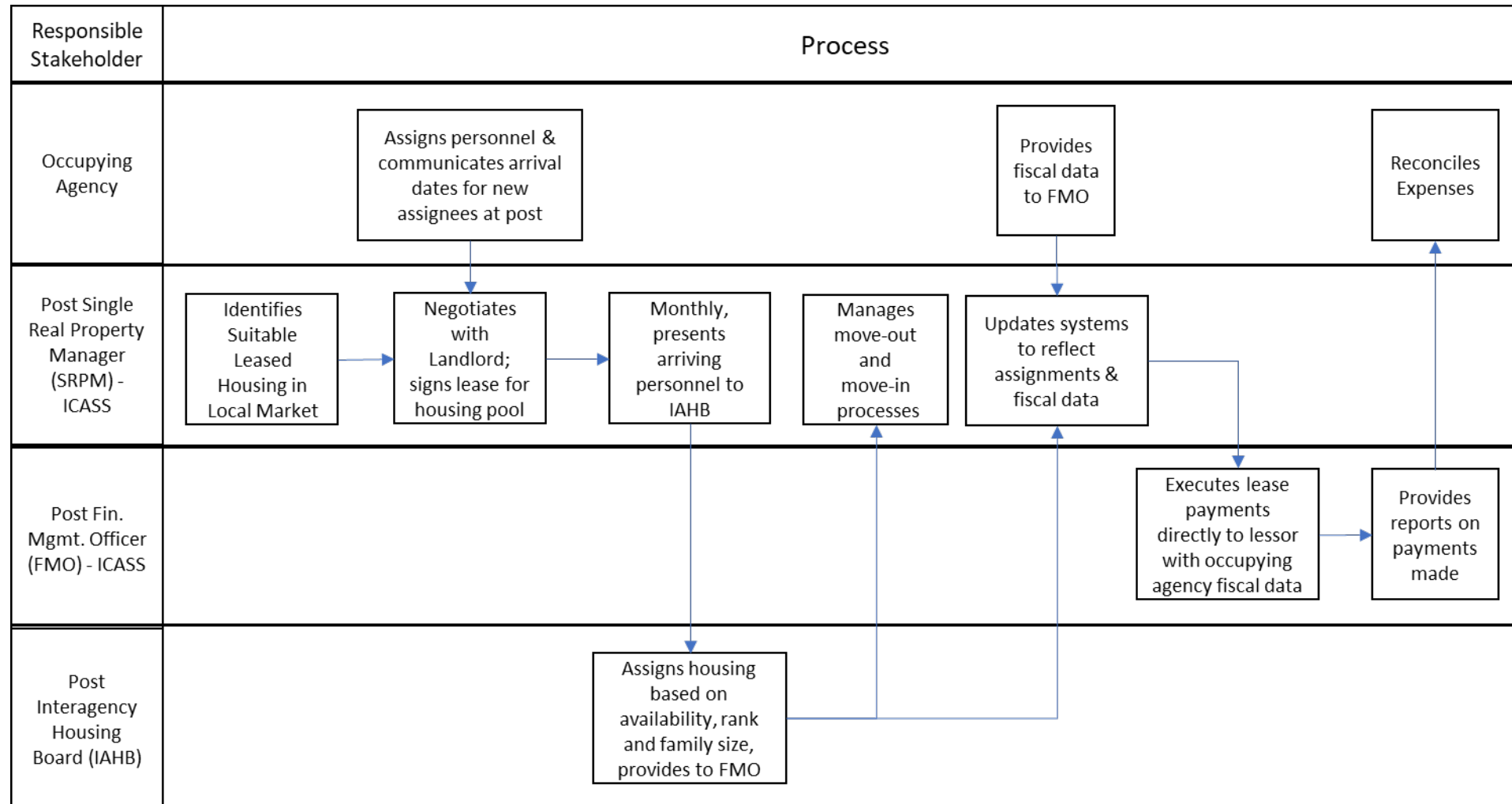
Key Distinctions between Overseas Residential Leasing and Standard Federal Leasing

State and over 30 other Federal agencies execute their missions overseas. To prevent redundancies for Federal processes overseas, State provides a number of administrative services on behalf of other federal Agencies. State administers the cost recovery ICASS system¹ to execute administrative functions (including acting as a contracting agent that includes leases). State also serves as a disbursing agent overseas for transactions (many of which are in foreign currencies) on behalf of Federal agencies with employees stationed overseas. The administration of these processes is executed in collaboration with other agencies in the form of the ICASS Councils and IAHBs, which include representatives from across the agencies stationed at each post. The nature of these services results in leasing processes that are fundamentally different from the domestic leasing processes employed by GSA and other agencies with leasing authority and responsibilities.

¹ The ICASS system is the principal means that the U.S. Government provides and shares the cost of common administrative support needed to ensure effective operations at its more than 200 diplomatic and consular posts abroad. In the spirit of the Government Performance and Results Act, the ICASS system seeks to provide quality services at the lowest cost, while attempting to ensure that each agency bears the cost of its presence abroad.

Exposure Draft Questions for Respondents (QFR)

Due: July 8, 2022

Omnibus Amendments: Technical Clarifications Addressing Lessee and Lessor Discount Rates and Sale-leasebacks² FAM 233: ALLOCATING LEASED RESIDENTIAL SPACE, <http://fam.a.state.sbu/fam/15fam/15fam0230.html>³ 15 FAM 251: LOCAL REAL ESTATE MARKET, <http://fam.a.state.sbu/fam/15fam/15fam0250.html>⁴ 15 FAM 234: PREASSIGNING HOUSING <http://fam.a.state.sbu/fam/15fam/15fam0230.html>