

Transitional Amendment to SFFAS 54

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This [proposal](#) would amend the implementation section of Statement of Federal Financial Accounting Standards (SFFAS) 54, *Leases*, by providing transitional accommodations to reporting entities in the area of “embedded leases” (a common industry term which generally describes contracts or agreements that contain lease component[s] and nonlease component[s], such as service components, and serve a primary purpose attributable to the nonlease component[s] as well as the related requirements of SFFAS 54, par. 72-77).

QFR 1 Do you generally agree, partially agree, or disagree with the proposed transitional amendment to SFFAS 54 as a whole? Please provide reasons for your views.

VA supports the Board’s objective of providing relief to federal entities through transitional accommodation in the area of embedded leases. We do not agree that the transitional accommodation language, as written, meets that objective. We do support the alternative view, with comments, and believe that the alternative view goes much further in meeting the Board’s intent to provide relief.

QFR 2 Proposed paragraph 96A provides that the transitional accommodation, if elected by the reporting entity, would apply to contracts or agreements that meet both of the following criteria: (a) the contracts or agreements contain nonlease components(s) and may contain lease component(s), and (b) the purpose of the contracts or agreements is primarily attributable to the nonlease component(s), such as service components.

Please provide feedback on paragraphs 3-4 and paragraph 5 (96A criteria), which are intended to provide criteria for the scope of the transitional accommodation for “embedded leases.” Respondents are encouraged to refer to the basis for conclusions and provide feedback on the design of these proposals and the extent to which they effectively scope in “embedded leases,” and the level of effort for applying such criteria.

VA believes one of the most burdensome, onerous, and costly piece of SFFAS 54 as it relates to embedded leases is the analysis of service contracts. SFFAS 54 brings heightened focus and audit scrutiny to contracts and agreements with lease and nonlease components, requiring a more comprehensive and deliberate analysis of service contracts to identify the presence of lease components. Depending on the criteria and factors an agency needs to consider when evaluating contracts and agreements to determine primary purpose, the real need for transitional accommodation is the time to perform an evaluation of service contracts and agreements to determine “primary purpose.” Criteria dependent, this analysis could require considerable review, professional judgement, and documentation to support VA’s conclusion.

We believe the language should be revised to affirm that the scope of SFFAS 54 applies to contracts or agreements with the purpose of conveying the right to control the use of property, plant, and equipment (PP&E) for a period of time in exchange for consideration. The transitional accommodation applies to all other contracts or agreements that contain lease and nonlease components.

This language would eliminate the risk that has been cited that agencies would inappropriately apply the transitional accommodation to all leases, including leases such as real estate leases, which a lessee agency clearly enters into with the intent of receiving the right to control the property but has both a lease component (shell rent) and nonlease component (operating expenses).

If the 96A language is retained, recommend the following clarifying edits to 96A. The transitional accommodation applies only to contracts or agreements that meet both of the following criteria:

- a. The contracts or agreements contain nonlease component(s) and [remove phrase - may contain] lease component(s).
- b. The purpose of the contracts or agreements is [remove phrase – primarily] attributable to the nonlease component(s), such as service components, based on management’s assessment of the nature of the contracts or agreements and professional judgment. The [remove phrase – primary] purpose attribution to the nonlease component(s) should not appear to be unreasonable based on the nature of the contracts or agreements and professional judgment.

- QFR 3** Please provide feedback on the proposed transitional accommodation provisions under paragraphs 96B-96C, which are intended to allow practitioners to reduce implementation time by not reporting certain “embedded leases” during the accommodation period. Please describe any alternative views or approaches, suggestions for improvements, and the reasons for your views. Respondents are encouraged to refer to the basis for conclusions and provide feedback on (1) the design of these proposals, (2) the expected effectiveness of the transitional accommodation, and (3) and the expected level of effort for applying the accommodation.

We agree with the provision to recognize contracts or agreements, including the lease components, as nonlease components in their entirety. We suggest adding language to clearly state that the provisions of paragraphs 96B-96C do not change measurement of Short-Term, Intragovernmental, or Right-To-Use Leases. For example, we would not want there to be any misinterpretation that the nonlease components of a Real Property Lease would need to be included with the lease components in the measurement of the lease liability and asset value.

- QFR 4** Proposed paragraph 96B provides that reporting entities may elect an accommodation period for up to two years prior to the prospective application requirements described in paragraph 96C. Please also refer to paragraphs A1-A13 of the basis for conclusions, including paragraph A10, which discusses the Board’s intent that this proposal would provide additional time to prepare for prospective implementation of paragraph 73 for new or modified “embedded leases.”

Please provide your views on the length and sufficiency of the proposed accommodation period and any views with respect to making the accommodation permanent. Please describe the reasons for your views and relevant considerations to facilitate the Board’s analysis of your comments.

VA believes the proposal should be revised to become a practical expedient. VA agrees with views expressed by Mr. Bell, Ms. Johnson, and Messrs. McNamee and Vicks in that “the transitional accommodation the Board proposes would provide some relief from the challenges inherent in implementing paragraph 73 of SFFAS 54, which addresses accounting by lessors and lessees for contracts that contain both a lease and a nonlease component. Such relief would be limited, however, in that it would be temporary and would apply only to contracts or agreements whose purpose is primarily attributable to their nonlease components. These members believe that making available broader and permanent relief from the requirements of paragraph 73 would substantially reduce the cost of implementing SFFAS 54 without substantially diminishing the quality of financial reporting of leases.”

- QFR 5** Proposed paragraph 96D provides that reporting entities may apply the provisions of paragraphs 96A-96C to groups of contracts or agreements that are reasonably similar in nature. A reporting entity may select different accommodation periods under paragraph 96B for different groupings of contracts or agreements.

Please provide feedback on the proposed criteria. Please describe any alternative views or approaches, suggestions for improvements, and the reasons for your views.

VA agrees allowing reporting entities to apply the provisions of 96A-96C to apply groups of contracts or agreements instead of applying the provisions of 96A-96C on a contract by contract basis, but VA does not agree with the provision providing reporting entities to apply different accommodation periods under paragraph 96B. VA agrees with proposed paragraph 96E regarding the transitional accommodation disclosure and would not want the disclosure requirement expanded, which seems necessary when allowing different accommodation periods.

QFR 6 Proposed paragraph 96E provides that reporting entities electing the transitional accommodation would disclose the election of the transitional accommodation during the reporting period(s) covered by the accommodation period and the reporting period immediately following the accommodation period. The disclosure would not need to be repeated during subsequent reporting periods.

Please provide feedback on the proposed disclosure requirement. Please describe any alternative views or approaches, suggestions for improvements, and the reasons for your views.

VA agrees with proposed paragraph 96E.

QFR 7 Four Board members provided an alternative view, which is documented under the basis for conclusions (appendix A), paragraphs A15-A26. Please refer to these paragraphs to review the alternative view as presented.

Do you agree, partially agree, or disagree with the alternative view? Please provide the rationale for your answer.

VA strongly agrees with the alternate view expressed by Mr. Bell, Ms. Johnson, and Messrs. McNamee and Vicks. VA requests that language added to the alternate view that clearly states that the provisions of paragraphs 96B-96C do not change measurement of Short-Term, Intragovernmental, or Right-To-Use Leases. For example, we would not want there to be any misinterpretation that the nonlease components of a Real Property Lease would need to be included with the lease components in the measurement of the lease liability and asset value.