

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.

DHS supports the transitional accommodation proposal to prospectively apply the provisions of SFFAS 54 to lease components of new or modified contracts or agreements meeting the “embedded leases” eligibility criteria beginning October 1, 2023; October 1, 2024; or October 1, 2025. Our main reason for supporting this proposal is the additional time it allows us to prioritize implementing contracts or agreements with a primary purpose attributable to non-lease components, as well as additional time to prepare for prospective implementation of embedded leases DHS would begin reporting embedded leases October 1, 2025.

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.

DHS agrees with the scope of the proposed transitional accommodation for embedded leases. In addition, DHS requests more specific guidance on how to assess whether the primary purpose of a contract or agreement is attributable to its non-lease or lease component(s).

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) the expected level of effort for applying the accommodation.

DHS agrees with the alternative view proposed by Mr. McNamee at the June board meeting. See our response to QFR 7 for additional feedback on this alternative view.

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.

DHS agrees with the proposed two-year deferment. Based on a recent survey with DHS components, it was determined that it would take approximately 8,500-man hours at a cost over \$400,000 to review all DHS contracts for embedded leases. A two-year deferment would allow more efficient allocation of staff resources and significantly reduce our financial statement audit risk. The additional time will allow DHS to fully implement SFFAS 54 for our right-to-use and intra-

governmental lease population prior to shifting resources to searching for and reporting on embedded 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.

DHS supports applying the provisions to groups of contracts or agreements that are reasonably similar in nature. Allowing this provision will streamline contract identification and the assessment process. DHS would report groups of contracts or agreements that are similar in nature through the end of the accommodation period.

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.

DHS agrees with the requirement to disclose the election of the transitional accommodation. DHS would disclose the election of the transitional accommodation through FY 2027 reporting. DHS also requests examples based on different accommodation selections, so that our disclosures meet the intent of 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.

DHS supports the alternative view proposed by Mr. McNamee at the June 2023 FASAB board meeting. We believe this approach would substantially reduce the cost of implementing SFFAS 54 without materially diminishing the quality of financial reporting of leases. The alternative view proposed that a reporting entity may elect to account for contracts or agreements according to their primary purpose, as either lease or non-lease. Therefore, a contract whose purpose is primarily attributable to its lease components could be accounted for as a lease in its entirety. If a contract or agreement's purpose is primarily attributable to its non-lease components, it could be accounted for using the standards applicable to the non-lease components. This would significantly decrease the administrative burden to separate lease and non-lease components of a contract and likely result in immaterial differences to the Balance Sheet.