May 31, 2016

Mr. David R. Bean
Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Dear Mr. Bean:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments to the Government Accounting Standards Board (GASB) on its January 25, 2016 exposure draft entitled Leases. The FMSB is comprised of 23 members (list attached) with accounting and auditing backgrounds in federal, state and local government, as well as academia and public accounting. The FMSB reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately. We are also providing our notice of intent to present at the public hearing on June 29, 2016.

We commend the Board for closely following the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) lease projects. We firmly believe in having convergence amongst the standard setters for similar projects is important to users, preparers and auditors as there will be a consistency in the contracting, operation and auditing of leases. We also appreciate the decision tree included in Appendix C of the exposure draft. However, we have a few questions and suggested changes to the exposure draft.

Areas of Convergence to Consider

In our review we noted three major differences between the exposure draft and lease standards issued by the FASB and strongly encourage the Board to consider convergence on these points:

- The definition of a short term lease in paragraph 60, which is more restrictive than in ASC 842-10-15. We recommend to follow FASB’s definition of a short term lease.
- Requirements to account for lease and non-lease components separately as required in paragraph 53, which are more restrictive than ASC 842-10-15-29 and 37 provisions, which allow lessees to choose not to report separate components when effects are insignificant or based on accounting policy. We believe the FASB’s approach is more expedient and recommend the Board follow the FASB’s perspective by including paragraphs 29 and 37.
- Requirement for all leases over 12 months to be reported at net present value, which will require far more leases to be subject to these calculations than FASB standards, which only require discounting for capital leases (now termed “direct financing leases”) and allow
operating leases to be capitalized at the full amount of the lease and amortized on a straight-line basis.

We see no reason why governments should report differently on these points, especially since we believe these differences will result in higher cost and more complexity for preparers and auditors. We noted that it appears the Board was attempting to make reporting simpler for governments by avoiding extra considerations as required in the FASB standards, then perhaps the Board should eliminate discounting altogether or establish a more reasonable threshold for determining when discounting is necessary - such as all leases greater than 5 years.

In addition, we also suggest the following convergence:

- Paragraph 47: converging with ASC 842-10-55-37 guidance on obligations to return underlying assets to original condition, which we found to be clearer and more conceptually consistent than guidance in the exposure draft.
- Paragraph 69-70: requiring reporting of the original and sublease only if the sub-lease does not relieve the original lessee of the primary obligation under the original lease - and if it does then to consider it a termination in the same way as ASC 842-20-35-14 and 842-20-40-3.
- Paragraph 76: addressing interfund leases in addition to intra-entity leases with component units.

Other Comments and Concerns

We recommend the Board add “infrastructure” to the list of nonfinancial assets in paragraph 4. While leasing infrastructure usually involves a service concession arrangement in accordance with GASB Statement No. 60, we believe clarity is necessary on whether any infrastructure leases not falling under GASB 60 would be included in the scope of this standard or not. We also recommend the Board add historical works of art and historical treasures that a government may rent for display to the list of excluded items. Many works of art and historical treasures on loan from institutions for display have only a limited display right of usage, without an intent to transfer ownership. Furthermore, if there was a transfer of ownership via a donation, the provisions of GASB Statement No. 72 would apply requiring valuation at acquisition value, which may be completely different than the lease provisions.

We also recommend in paragraph 5, that the term “biological assets” be defined so as to avoid misunderstanding. For example, governments may own farmland that is leased to not for profit organizations to operate community farms or gardens. Furthermore, we understand the exclusion for software licenses as explained in paragraph B12 and in question Z.51.21 of Implementation Guide 2015-1. However, the issue of software licensing and so-called cloud computing is pervasive and has some of the characteristics of the foundational model that the Board has proposed. For example, if fees are not paid, data may be inaccessible. We suggest the Board deliberate this issue sooner rather than later.

Similarly, in paragraph 5(d), leases in which the underlying asset is financed with outstanding conduit debt are excluded unless both the underlying asset and the conduit debt are reported by the lessor, as further explained in paragraph B16. Many assets such as dormitories, hospitals, water and sewer are
financed by debt issued by state authorities that is secured by a financing document similar to a lease, in most cases mirroring the maturities of the debt and similar provisions. We suggest that these arrangements be reported as financed purchases in paragraph 14.

In paragraph 30 we request the board clarify the phrase which states: “When a lease results in the reporting of a lease asset...” In this context, the proposed standard has not established when a lease asset would result under the current financial resources measurement focus. Paragraph 13, which establishes the basis for recording a lease asset, is restricted to the economic resources measurement focus per paragraph 7. Therefore, we recommend paragraph 30 be changed to “when a lease asset would have resulted under the economic resources measurement focus, the expenditure and other financing source to record under the current financial resources measurement focus in the first year is...” We also recommend the Board to clarify that the amount to be recognized is only the liability portion of the lease asset and provide clarity to how a lease should be reported in the governmental funds.

In paragraph 36, we agree with the Board’s treatment of regulated leases such as those between airports and airlines. We believe this is relatively clear.

In various paragraphs in the basis for conclusion (particularly B104), the Board discusses the ability of governments to set policy thresholds for the capitalization of leases, similar to those commonly used for capital assets. We suggest the Board include similar language in the transition provisions, such as in paragraphs 79 or 80. We believe that most governments will align the threshold for leases to those used for capital assets.

In conclusion, the implementation of the lease standard will be a large and complex process. We encourage the Board to provide more detailed transition guidance and examples. We noted the FASB provided multiple pages of transition guidance and we believe this would be a great opportunity for the Board to provide this information. In particular, we recommend that one of the examples be a very long term lease (such as a 99 year ground lease) such as those common to states.

We appreciate the opportunity to comment on this document and will be pleased to discuss this letter with you at your convenience. If there are any questions regarding the comments in this letter, please contact me at (208)383-4756 or Lmiller@eidebailly.com

Sincerely,

Lealan Miller, CGFM, CPA
Chair- AGA Financial Management Standards Board

cc: John E. Homan, MBA, CGFM, CPA, CGMA
   AGA National President
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