May 13, 2016

Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Proposed Statement of the Governmental Accounting Standards Board, “Leases”
Project No. 3-24E

Dear Sir:

The Michigan Government Finance Officers Association (MGFOA) has reviewed the Proposed Statement of the Governmental Accounting Standards Board on Leases, dated January 25, 2016. We offer the following comments and observations:

We agree that additional guidance on Leases is necessary in order to more consistently account for and report such activities within governmental financial statements. We agree that Lessors reporting a receivable in the financial statements helps define the financial strength of the entity. Also we agree that Lessees have entered into a financing agreement that should be reported as such showing the financial obligation.

We believe the exposure draft could be improved to provide clearer guidance on some of the more common transactions that local units deal with. Specifically, we offer the following comments:

Clarification is needed on definition of intangible assets in paragraph 5a:

Paragraph 5 provides examples of types of leased assets that this statement does not apply to. However, we feel the definition could be expanded and more examples are needed.

- Many local units of government in Michigan enter into lease agreements with cell phone service providers. These governmental entities become a lessor, providing an easement of a section of land for a cell phone tower. In this case, the governmental unit is giving up the right to use the land in the lease transaction.
- In another example, the governmental entity is leasing the top of a water tower to cell phone providers as a means to create a cell phone “tower”. This leasing agreement does not change the original use of the water tower, so it seems this would be considered an intangible asset.

Some members of our committee are looking for clarification on the intangible nature of these two types of leases to cell phone providers. We request clarity in paragraph 5a in this regard.
More details are needed in paragraph 29 and 30 related to the current financial resources measurement focus:

Paragraph 29 and 30 summarize reporting of leases within governmental funds. The final sentence in paragraph 30 reads “Subsequent governmental fund lease payments should be accounted for consistent with principles for general obligation debt.” Currently, outflows related to capital leases are commonly reported as functional expenses, rather than as debt service principal and interest. If the GASB is intentionally directing that the outflows related to leases be reported as debt service principal and interest, perhaps the basis for conclusions could provide more specific direction.

Reporting the lease asset in the financial statements

Paragraph 13 or 24 should clarify whether the lease asset may be reported as a component of capital assets in the financial statements, or rather should it be reported as a separate item in the statement of net position.

Amortization Recognition rationale in paragraph’s B46 – B48

Paragraph 25 requires the lease asset to be amortized in a systematic and rational manner. However, paragraph B48 states: “A calculation that results in a constant total lease expense (interest plus amortization) could be considered systematic and rational in some cases”. This implies two things that we are concerned about:

a) That in some cases a total of interest and amortization could be recorded on one line in the financials as if it were an operating lease. When interpreted this way, the last sentence in B48 contradicts the information given in paragraph B46. If our interpretation of the last sentence in paragraph B48 is correct, clarification and examples of cases in which reporting total lease expense on one expense line could be considered systematic and rational.

b) That it could be rational to calculate the amortization as being equal to the principal amortization on the related financing. Since this has no relation to the use of the asset, it cannot be considered to be rational. The only rationale we can see is to force an expense measurement that is consistent with the cash basis of accounting, which would frustrate the purposes of accrual accounting.

These comments represent the consensus opinion of the Accounting Standards Committee and have been approved by our Board of Directors. Thank you for your consideration and the opportunity to express our points of view.

Respectfully,

Christa McLellan, President
Michigan Government Finance Officers Association