March 6, 2015

David R. Bean, Director of Research and Technical Activities
Governmental Accounting Standards Board
Project No. 3-24P
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Preliminary Views-Leases, Project No. 3-24P

Dear Mr. Bean:

The following is the response of the Government Accounting and Auditing Committee of the Washington Society of Certified Public Accountants (WSCPA). The views expressed are the views of the Committee and not necessarily the views of the individual members or the WSCPA as a whole. We are pleased to have the opportunity to respond to the Governmental Accounting Standards Board’s (GASB) Preliminary Views (PV) Leases.

We support the mission of GASB, to establish and improve standards of state and local governmental accounting and financial reporting.

Overview of Our Response:

We generally support this PV to allow comparability of financial statements of lease transactions among governmental and non-governmental entities. However, we are concerned the provisions described for both the lessees and lessors could be burdensome for preparers, especially those with a large number of lease agreements. The accounting and financial reporting treatment for leases will be more aligned with financing/servicing a loan than processing as operating leases.

Specific PV Comments:

Issue 1 Definition of Lease Term (Chapter 3) and Short-Term lease (Chapter 6)

We agree that lease term should be defined as the period during which a lessee has a noncancellable right to use an underlying asset. However, perhaps better clarification with examples would be helpful. For example, for lease agreements, such as moorage agreements with over 1,800 customers managed by a marina owned by a governmental authority, the termination provision allows cancellation within 15 or 30 day notice by either
the lessor or lessee, without penalty, regardless of the lease term that has a specified
duration (over or under 12 months) or not. It appears such leases would fall under the
definition of Short-Term lease as it may be cancellable before or after 12 months
(paragraph 3 of Chapter 6).

**Issue 2 Lessor’s Accounting (Chapter 5)**

*Determining the present value of a receivable* - We agree that lessors should recognize a
lease receivable and a deferred inflow of resources at the beginning of a lease, unless it is
a short-term lease. For example, for concession agreements managed by an airport
authority, the minimum annual guarantee (“MAG”) is only fixed when the MAG exceeds
the variable payments that are based on the lessees’ performance (i.e. volume of sales).
This type of concession agreement further requires an annual true-up of annual MAG
versus annual variable payments. Using paragraph 4 and 5 of Chapter 5), the present value
of the lease receivable should include the MAG. However, what would be the appropriate
treatment of the amount of variable payments that exceeds the MAG in any given month?
Should the delta be recognized as revenue using paragraph 6 of Chapter 5)?

Similarly, for an airport authority, airline agreements may include both fixed and variable
payment components in a lease agreement. While the preparer can account for the fixed
and variable payments separately following the provisions within this PV, airline
agreement often called for annual cost recovery true-ups or settlement of all components
(both fixed and variable payments) based on the operating costs of the leased properties.
Due to the annual true-ups or settlement provision of this kind of agreement, should the
fixed payment considered fixed in-substance upon inception of the lease and incorporating
into the net present value of lease receivables?

*Determining the discount rate* - Per paragraph 8 of Chapter 5, although the Board believes
that the lessor would have the information to determine discount rate for the computation
of Lessor’s lease receivables, Washington State Law requires port authorities entering
leases of its real estate at “fair market rental value”. As such, the lessor, the port authority,
may not have information to determine the discount rate as it is not the factor to derive the
“fair market rental value”. This is very similar to the discussion of paragraph 236 of GASB
No. 62 regarding airport facilities.

“Because of special provisions normally present in leases involving terminal space
and other airport facilities owned by a governmental unit or authority, the
economic life of such facilities for purposes of classifying the lease is essentially
indeterminate. Likewise, the concept of fair value is not applicable to such leases.
Because such leases also do not provide for a transfer of ownership or a bargain
purchase option, they should be classified as operating leases. Leases of other
facilities owned by a governmental unit or authority wherein the rights of the
parties are essentially the same as in a lease of airport facilities described above
also should be classified as operating leases. Examples of such leases may be those involving facilities at ports and bus terminals." Excerpt of GASB No. 62

In such circumstances, should the lessor be permitted to use its own incremental borrowing rate as the discount rate, similar to the lessee’s treatment using paragraph 10 of Chapter 4?

Disclosure requirement - For disclosure requirement paragraph 16b, when leases involves only part of a building, such as a section of an airport terminal is used for internal operation not for lease, its costs (or carrying amount) may not be objectively and reasonably determinable to segregate the value of the assets held for leasing. How should the government address this issue? Are the perceived benefits of this disclosure outweighing the expected costs to generate it?

Issue 3 Leases with related parties and intra-entity leases (Chapter 9)

We agree that leases with or between blended component units, for which eliminations are required and made before the financial statements of the blended component units are aggregated with those of the primary government. We suggest the Board include the requirement of eliminations to include joint venture equity interest computation if there are leases among joint venture’s participants and the joint venture organization.

Other Comments

In public-private partnerships, the legislated lease agreement may be much less than the fair market value of the facility’s rent producing capability and might only be based on operating costs of the governmental oversight entity, which is substantially less than the market value of a lease of a similar facility. The lease payments may be very inconsequential to the overall private-public partnership agreement revenue and costs, because the legislation was designed to encourage the public-private partnership. Would such a situation require recording a lease receivable and related deferred item in the statement of net position or could such a situation allow for recording annual lease payments as “operating” as is currently allowed?

Thank you for the opportunity to respond. If you have any questions or need additional information regarding this response, please contact Lisa Lam at (206) 787-4334.

Sincerely,

SENT VIA E-MAIL to director@gasb.org

Olga A, Darlington, Chair
Government Accounting and Auditing Committee
Washington Society of Certified Public Accountants