



April 30, 2019

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

Dear Mr. Bean:

Members of the American Institute of Certified Public Accountants (AICPA) State and Local Government Expert Panel have reviewed the Governmental Accounting Standards Board (GASB) Exposure Draft (ED), *Leases Implementation Guide* and are pleased to offer our comments.

Overarching Comments

We suggest more linkages be made among questions and to illustrations to improve understanding of the concepts. We have made several recommendations in our comments on specific questions where improvements can be made in this area.

We also suggest the answers be made more explicit by starting with a Yes, No, or It Depends. When the answers lay out rationale first and then conclude with the answer, it makes the concepts more difficult to follow. We believe that GASB should be more explicit by starting with the answer to improve user comprehension. We have provided a few examples to consider (e.g., Question 4.17), however the entire document could benefit from this suggestion.

Significant Concerns

Question 4.6

We recommend the Board consider providing potential additional factors for cell phone tower or antenna placement agreements to be considered as leases. The answer provided to Question 4.6 is very specific as to how the control criterion may be met (i.e., the right to use the land or connection point). While these agreements are common, they vary tremendously, and may be silent on the right to use the land or connection point. Thus, users would benefit from elaboration of additional circumstances that would qualify cell phone towers as leases.

Question 4.7

We suggest the question be rephrased to explicitly state this arrangement is a lease of land between the government and an oil and gas company. This question makes a distinction between the underlying asset (i.e., the land) and the nature of the company's business (i.e., exploration for oil and gas). Therefore, we suggest the question be revised as follows:

Q: A government enters into [an agreement](#) with a company that engages in oil and gas exploration and production. [The agreement between the government and the oil and gas company conveys control of the right to use a parcel of land \(i.e., lease of land\)](#). Is this lease excluded from Statement 87?

Question 4.28

We suggest that the question be revised to provide an example that is not commonly carried as inventory. The question currently poses a scenario where a government leases tires for its transit fleet. In practice, many governments treat tires as inventory. Given leases of inventory are scoped out of Statement 87, we suggest using an item not commonly carried as inventory in the example to alleviate confusion and focus on the issue of variable payments.

Further, it is unclear how the facts in this scenario would constitute a lease since the expectation is for the government to consume all of the estimated service capacity of the asset. Since this question is focusing on the variable lease payments, we suggest simplifying the fact pattern focus on variable payments. For example,

Q - Lease payments are based entirely on *[insert a variable metric in lieu of miles driven]*. Should the government record an estimated liability for the expected total payments over the lease term?

Question 4.31

We suggest the question clarify that if payments are variable (e.g., based on usage or performance) that the relevant guidance is paragraph 22 of Statement 87. Based on the information provided in the question, it could be interpreted that the payments based on usage could meet the criteria of paragraph 21h of Statement 87 (i.e., "any other requirements of payments that are reasonably certain of being required based on an assessment of all relevant factors"). Clarifying that paragraph 22 of Statement 87 applies when the payments are based on usage or performance is an important distinction to make as an assessment of "reasonably certain" as discussed in paragraph 21 is not appropriate.

Other Comments

Question 4.14

We suggest an additional reference be added to explain the relevance of Question 4.35 referenced in the answer.

A-... (See also Question 4.35 [related to prepayments.](#))

Question 4.15

We suggest the question and answer explicitly state that in the holdover period both the lessor and the lessee have the right to cancel the lease. As stated, it is implied that a month-to-month lease is cancellable by both parties, but this is not always the case.

Q ...the end of the five years, [both the lessor and the lessee have the right to cancel the lease or](#) may continue the lease, using the same terms

Further, the question and answer use the terms renegotiation period, month-to-month holdover period, and holdover period. We suggest using one term for consistency and clarity.

Question 4.16

We suggest the question emphasize the original lease is at a market rental rate to clarify that the scenario posed is focused on the impact of the bargain renewal option.

Qsuch as a 20-year lease [at a market rental rate](#) with a \$1 option to renew....

Question 4.17

We suggest the answer to this question be more explicit to answer the question posed. We suggest the following:

A—[Yes, as](#) paragraph 12 of Statement 87 requires that periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party be excluded from the lease term as cancellable periods. The presence of cancellation penalties does not affect this conclusion. (See also Question 4.18.)

Question 4.24

We suggest the structure of Question 4.24 be aligned to Question 4.23 since the scenarios are similar and focus on nuances of ownership and transfer. We suggest question 4.24 ask the same question as 4.23 and make clear that no termination option exists and then adjust the answer to 4.24 to say that it is not a lease but a financed purchase.

4.24. Q – A school district leases computers. At the end of the lease term, students are given the option to purchase their computers. There is no termination option.....Is this transaction a lease for financial reporting purposes?

A – No, it should be reported as a financed purchase of the computers by the school district.
Paragraph 19 of Statement 87....

Question 4.25

While we agree with the answer in 4.25 we suggest it be restructured to state that lease liabilities, either individually or in the aggregate, be recognized. We also suggest adding a linkage to question 7.9.8 which addresses assets that may not meet the capitalization policy on an individual basis, yet might be considered material collectively. Clarity is needed on this point as detaching the materiality of lease liabilities from a government's capitalization policy is an issue frequently discussed between auditors and their clients.

A—Significant lease liabilities, either individually or in the aggregate, should be recognized, regardless of the government's capitalization policy. A government's capitalization threshold applies only to assets (See also Question 7.9.8 for materiality considerations). While authoritative pronouncements do not provide specific guidance related to a capitalization threshold, governments often use capitalization thresholds in practice so that limited resources are not spent accounting for insignificant items. When applying a capitalization threshold to leases, lessees should consider the significance of the lease liability in addition to the significance of the lease asset in accordance with the guidance provided in Question 7.4.1 of *Implementation Guide No. 2015-1*, as amended.

Question 4.26

We suggest Question 4.26 include an assumption that the criteria in paragraph 12a of Statement 87 is met so that the answer can focus on the point of this question, to estimate the payment amounts when not specified in the contract.

4.26. Q—.....The lessee has an ongoing relationship with the lessor and is reasonably certain that it will exercise its option to extend (thus, assume for this example that the criteria in paragraph 12a of Statement 87 are met). How should the lessee measure the lease liability if the payment amount for the optional period is not specified in the contract?

Question 4.27

We suggest more specificity in the question to link the first year's payment to the lease commencement Consumer Price Index (CPI) factor. We understand that this question is clarifying the difference between subsequent changes to CPI and the current CPI balance and how that amount impacts the lease liability. The answer provides a good explanation of how the CPI impacts the lease liability, but it does not link why the lease liability is calculated using \$5,000 per month and does not take into account the CPI balance of 251 at lease commencement. Thus, we suggest the following:

Q....for the first year at \$5,000 per month, which was calculated using the lease commencement CPI factor.

In addition, GASB should consider adding in a fact pattern for the year 2 calculation to further the reader's understanding and share consistency with illustration B3 in appendix B. We believe further clarity is needed as our experience is that questions are being raised on this topic.

Questions 4.37 and 4.38

We suggest switching the order of Questions 4.37 and 4.38. Question 4.38 is a more straight-forward fact pattern of an amortizing asset that the government subsequently decides purchase. Discussing the non-amortizing asset in Question 4.37 provides additional nuances that build upon concepts included in 4.38.

Additionally, we believe it is likely that the government's timing of becoming reasonably certain will occur later in the lease term. In addition to the edits proposed below, GASB should revise the answer to address any additional factors to consider when a significant portion of the lease term has passed

Q—A government leases land and amortizes the lease asset because it is not reasonably certain that it will purchase the land at the time the lease is entered into. If the government subsequently becomes reasonably certain that it will purchase the land, should the lease asset be remeasured to the amount of the initial measurement before the lease asset was amortized?

A—No. If a lease contract includes a purchase option and the lessee determines that it is reasonably certain of being exercised, paragraph 32 of Statement 87 requires that the lease asset be amortized over the useful life of the underlying asset, unless the underlying asset is nondepreciable. If the government is not reasonably certain that it will purchase the land when the lease is entered into, but later becomes reasonably certain, the government should cease amortizing....

Question 4.44

We suggest the question be rephrased to ask whether leased assets be presented in the disclosure of changes in capital assets and to avoid the term "included." As proposed, we have concerns that users may improperly infer that leased assets be *included* with other capital assets when paragraph 37c of Statement 87 requires lease assets be disclosed *separately* from other capital assets.

Question 4.46

The fact pattern presents two transactions, a non-exchange transaction and a lease. For clarity, we suggest modifying the language to eliminate references to a sublease. In the first transaction, the state donates the right-to-use the land to the school district

and it is considered a nonexchange transaction (i.e., does not qualify as a lease). The second transaction is equivalent to leasing the intangible right-to-use asset created by a **sublease** (emphasis added). If the first transaction does not qualify as a lease, how can the second transaction qualify as a sublease? We suggest the following edits to the final sentence of the answer:

A....The second transaction is equivalent to leasing the intangible right-to-use asset created by the [school district's right to use the land](#).

Question 4.51

We suggest the answer be expanded to add clarification on how an additional lease receivable is reported and whether amortization is retrospectively or prospectively applied.

Question 4.61

We suggest adding a reference to Illustration B1 to the answer to improve understanding of the accounting for installation costs.

A-...in accordance with paragraph 30c of Statement 87. [\(See Illustration B1 in nonauthoritative Appendix B for an example of how installment costs considered in the lease asset\)](#)

Question 4.62

We suggest the discussion about the components of the contract be consistently referenced as components rather than assets as not all lease components are assets (e.g., services). As drafted, the answer sometimes refers to assets and sometimes refers to components.

A- Yes. If a lease contains multiple underlying [components](#), the lease components should be separated if the accounting treatment for each underlying [component](#) would be different. Statement 87 does not apply to software licenses but does apply to the use of the equipment. Therefore, in this example, the components of the lease should be separated.

Question 4.63

We suggest the scenario in the question be changed to illustrate a component that could potentially be difficult to reasonably estimate to provide a more realistic scenario. The example in Question 4.63 gives utilities and janitorial costs for a portion of the building as a component for which costs need to be estimated. We believe a government could reasonably estimate and separate the cost for those services and are unclear why the answer infers they could not.

Question 4.70

We suggest the question and answer be revised as follows to eliminate the dollar amounts as we found the scenario unrealistic (i.e., 200 computers leased resulting in a \$200,000 liability and an additional 30 computers leased added only \$2,500 to the liability).

4.70. Q—Three years into a 4-year lease, a school district modifies its lease from 200 computers to 230 computers due to an increase in enrollment. The school district has determined that the increase in the lease payments appears to be unreasonable based on the advertised list price of the computers. How should the school district account for the amendment to the lease?

A—Because the school district has determined that the increase in the lease payments appears to be unreasonable based on the advertised list price of the computers, the school district should account for this as a lease modification. Paragraph 73 of Statement 87 states that unless a modification is reported as a separate lease as provided by paragraph 72, a lessee should account for a lease modification by remeasuring the lease liability. The lease asset should be adjusted by the difference between the remeasured liability and the liability immediately before the lease modification. Thus, the lease asset should be increased by the difference between the remeasured liability and the liability immediately before the lease modification.

Illustration B1

We suggest adding language to clarify that both the lessor and lessee have a right to cancel (similar to the language in paragraph 12 of Statement 87). Our comment is similar to Question 4.15 where it implies that a month-to-month lease is cancellable by both parties, but this is not always the case.

Facts and Assumptions

....After the end of the 60 months (if the city does not extend the lease) or 84 months (if the city does not extend the lease), the lease may be continued on a month-to-month basis where both the lessee and lessor have the right to cancel the lease.

Illustration B3-Example 2

For completeness, we suggest addressing what happens when the prime interest rate decreases.

Accounting and Financial Reporting

If the prime interest rate at January 1, 20X2 is 5.1 percent, a 2 percent increase, the school district's payment on January 1, 20X2, will be \$25,500. The additional \$500 will be recognized as an inflow of the period.

If the prime interest rate at January 1, 20X2 is 4.9 percent, a 2 percent decrease, the school district's payment on January 1, 20X2, will be \$24,500. The \$500 reduction will be recognized as an inflow of the period.

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Letter of Comment No. 021
File Reference: Leases2-IG87
Date Received: 04/30/2019

Additional Example – Capital Asset Disclosure

We suggest the Board include an illustration of a capital asset disclosure to emphasize the nuances to the disclosure requirements.

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The AICPA appreciates the opportunity to comment on the ED. As the nature of this ED is to further clarify and illustrate existing GASB Statements, this comment letter was prepared by members of the AICPA's State and Local Government Expert Panel and was not reviewed by the AICPA's Financial Reporting Executive Committee. Therefore, this response represents only the views of individual members of the State and Local Government Expert Panel and is not an official position of the AICPA. Representatives of the State and Local Government Expert Panel would be pleased to discuss these comments with you at your convenience.

Sincerely,



Heather S. Acker
Chair
AICPA State and Local Government
Expert Panel



Mary M. Foelster
Director
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cc: State and Local Government Expert Panel
Dan Noll