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Government Environment and Reporting Model + Deep Dive in GASB 87 (Leases)



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Topics Covered

- Government Financial Reporting Environment
- Applicable Reporting Framework for Local Governments
- GASB 87 - Leases

Government Reporting Environment

Financial Reporting

- Who Cares?
 - Constituents
 - Bond buyers and rating agencies
 - Other governments and groups for benchmarking
- Who's responsible?
 - Financial managers are responsible for the accuracy of the financials (even if the work is contracted to a third party)

Financial Reporting

- 3 types – Internal reports, special purpose reports, and general purpose reports
 - Internal financial reporting
 - Prepared for internal use only
 - May have any form or content
 - Used to monitor budgetary compliance
 - Not subject to external review or audit
 - Special purpose reports
 - Financial reports required by external parties to be prepared according to their form and content

Financial Reporting

- General purpose external financial reporting
 - Other Comprehensive Basis of Accounting (OCBOA) and GAAP reports
 - Form and content is governed by GAAP

Sources of Governmental GAAP

- General purpose financial reports are governed by GAAP and GASB
- Sources of GAAP
 - Private Sector – Financial Accounting Standards Board (FASB)
 - State and local governments – Governmental Accounting Standards Board (GASB)
 - Federal government – Federal Accounting Standards Advisory Board (FASAB)

About the GASB

- Why is independent standards setting important?
 - Free from inappropriate political pressures or commercial influence
 - GASB brings objectivity and integrity
 - Standards are neutral, unbiased and relevant in the government environment

About the GASB

- **Why are GASB Standards important?**
 - Yield information users need to make decisions about a government
 - Assist users to assess whether a government has been accountable for its resources
 - Sounds financial reporting = informed decisions

Sources of Governmental GAAP

- **Governmental GAAP Hierarchy**
 - Category A
 - Officially established accounting principles (GASB Statements)
 - Category B
 - GASB Technical bulletins
 - GASB Implementation Guides
 - AICPA Literature cleared by the GASB

GASB Standard Setting Process



Financial Reporting

- The financial statement audit
 - Auditor's goal is to provide reasonable assurance that the BFS are fairly presented
 - Unmodified audit opinions are rendered as long as BFS are in accordance with GAAP and the standards set by governing body (AOS)
 - BFS should be well supported with underlying documentation

Ohio Local Governments

- **The Ohio Auditor of State**

- Responsible for auditing all public offices in Ohio
- Independently elected statewide office established under Ohio's Constitution
- Other duties include:
 - Performance auditing
 - Fraud investigation in public agencies
 - Financial services to local governments
 - Promotes transparency in government

Ohio Local Governments

- **The Ohio Auditor of State**

- Provides Technical Bulletins which can assist in the implementation of GASB Standards
- Releases the financial audit of public entities on the website www.ohioauditor.gov
- Local governments must now file unaudited financial statements on the Ohio Auditor of State's Hinkle System
- Audited financial information is used online for the new Financial Health Indicators (cities and counties)

Ohio Local Governments

- **GFOA and Ohio GFOA**

- Government Finance Officers Association
- Promotes excellence in state and local government financial management
- Provides:
 - Best Practice Guidance
 - Consulting
 - Networking Opportunities
 - Publications
 - Recognition programs
 - Research
 - Training

Reporting Framework

Financial Reporting Entity

- **GAAP** requires governments to define their reporting entity in a way that fully reflect the financial accountability of that government's officials.
- Must include (at minimum) the government itself (primary government) but also any legally separate units that if excluded could render the financial statements misleading.

Primary Government

- All State Governments are primary
- General Purpose Governments are primary
- “Special” Purpose Governments are primary only if it meets 3 criteria:
 - Separate legal status (sue, be sued, hold property in own name)
 - Separately elected governing body (general election)
 - Fiscal independence (one that is **not** fiscally dependent on other government)

Component Units

- Legally separate organization that a primary government must include as part of its financial reporting entity for “fair presentation”
- Tests for financial accountability:
 - Board appointment (voting majority)
 - Fiscal dependence
 - Majority equity interest
 - Exclusion would result in misleading financial reporting

Reporting Entity Presentation

- Two ways that primary government reports component units. Method depends on nature of relationship that exists between the two units.
- Component that function as an integral part of primary are “blended”
- Component that function with autonomy are “discretely presented” (together with but separate from the primary government)

Criteria For Blending

- Two situations where blending is appropriate
 - Shared governing body (substantively the same or voting majority is the same)
 - Exclusive (or almost exclusive) benefit to the primary government
 - Provide services entirely (or almost entirely) or provide benefits exclusively (or almost exclusively) for primary government
 - (function like an internal service fund)
 - Don't mistake services to citizens/constituents as benefitting the government

Separate Reporting

- Component units that are “discretely presented” may also issue their own separate, stand-alone financial reports.
 - Should use all the applicable accounting rules that the primary government
 - Should include all of its component units as well
 - Relationship between component and primary government must be disclosed on the cover of the report and in the financial notes

Summary Reporting Entity

- Primary Government (elected board, separate legal status & fiscal independent)
- Component Units (legally separate unit that must be reported with primary government)

Government Wide Financial Statements

- Statement of Net Position
- Statement of Activities

Statement of Net Position

- Shows assets, deferred outflows, liabilities, deferred inflows, and net position of the government entity
- Columns for Governmental Activities, Business-type Activities, and Component Units (if discretely presented)
- Meant to show a snapshot of the entity at the end of the fiscal year

Statement of Net Position

- **Order of Accounts**

- Current Assets (in order of liquidity)
 - Liquidity is the amount of time to convert to cash
- Capital Assets
- Deferred outflows or resources
- Current Liabilities (in order of liquidity)
- Long-term liabilities
- Deferred inflows or resources
- Net Investment in Capital Assets
- Restricted Net Position
- Unrestricted Net Position

Statement of Net Position

- **Current Assets**
 - Must be listed in order of liquidity

| Assets: |
|---|
| Equity in pooled cash and cash equivalents. |
| Receivables (net allowance for uncollectibles): |
| Income taxes. |
| Property and other local taxes |
| Accounts. |
| Special assessments |
| Accrued interest |
| Due from other governments |
| Internal balance |
| Net pension asset |

Statement of Net Position

- **Capital Assets**
 - Capital assets should be separated by non-depreciable and depreciable capital assets
 - Below are two ways to disclose capital assets on the financials

Capital Assets:

| |
|---|
| Non-depreciable capital assets. . . . |
| Depreciable capital assets, net |
| Total Capital Assets, net. |

Capital Assets:

| |
|-------------------------------------|
| Land |
| Construction in progress |
| Buildings |
| Equipment |
| Vehicles |
| Less: Accumulated depreciation . . |
| Total Capital Assets, net |

Statement of Net Position

- **Deferred outflows of resources**
 - Defined as a consumption of net assets by the government for a future period

| |
|---|
| Deferred outflows of resources: |
| Pension/OPEB related |
| Unamortized deferred charges on refunding |
| Total deferred outflows of resources |

Statement of Net Position

- **Current Liabilities**

- Must be listed in order of liquidity

| |
|--|
| Accounts payable |
| Accrued wages and benefits payable |
| Due to other governments |
| Accrued interest payable |
| Claims payable. |

Statement of Net Position

- **Long-term liabilities**
 - Include debt obligations and net pension/OPEB liability of the entity
 - Amounts due within one year should be separated from other amounts

| |
|---|
| Long-term liabilities: |
| Due within one year |
| Due in more than one year: |
| Net pension liability |
| Other amounts due in more than one year |

Statement of Net Position

- **Deferred inflows of resources**
 - Defined as an acquisition of net assets by the government that is applied to a future reporting period

Deferred inflows of resources:

Property taxes levied for the next fiscal year

Pension/OBEP related

Total deferred inflows of resources

Statement of Net Position

- **Net Position**
 - Net investment in capital assets
 - Represents the current carrying value of capital assets less the amount of debt applicable to the acquisition of those assets
 - Remember unspent debt proceeds

Statement of Net Position

- **Net Position, continued**

- Restricted Net Position

- Represents amounts of Net Position restricted for a specific use resources - subject to *externally imposed* restrictions (creditors, grantors, contributors, laws/regulations of other governments, constitutional provisions)

- Unrestricted Net Position

- Amount of net position left over
 - Can be a deficit
 - $\text{Assets} + \text{Def Outflows} < \text{Liabilities} + \text{Def Inflows}$

Statement of Net Position

- **Net Position**
 - Example

| |
|--|
| Net position: |
| Net investment in capital assets |
| Restricted for: |
| Debt service |
| Capital projects |
| Security of persons and property. |
| Transportation projects. |
| Community development programs |
| Police and fire pension |
| Other purposes. |
| Unrestricted (deficit) |

Statement of Activities

- Shows changes in a government's net position over a length of time
- Includes Governmental activities, Business-type activities, and Component Units
- Net Position at the end of the year should match Net Position from the Statement of Net Position

Statement of Activities

- **Formatting and Order**
 - The Statement of Activities should be displayed in a matrix format.
 - Program specific revenues should offset the expenses associated with the revenues.
 - General revenues should be listed next
 - Extraordinary gains/losses
 - Special items
 - Transfers
- **Example on the following slide**

Statement of Activities

- **Program Revenues**

- Arise because the specific program with which they are identified exists
- Program revenues should be paired against the expenses that are used to generate them
- 4 types
 - Charges for services
 - Are charges for providing goods, services, and privileges directly from a governmental entity, charges are intended to cover the cost of the services they provide
 - Examples: services charges (water/sewer), license and permits, special assessment charges, intergovernmental charges

Statement of Activities

- **Program revenues**
 - Operating grants and contributions
 - Monies received from a government or individual that must be used for a particular purpose
 - Capital grants and contributions
 - Use the same criteria as operating grants except that monies are restricted to the purchase of capital assets rather than operating expenses
 - Offset to where depreciation will be charged

Statement of Activities

- **General Revenues**

- Includes items that are not specifically identified within a program, they include:
- Items that should be reported separately:
 - Income taxes
 - Sales taxes
 - Property taxes
 - Franchise taxes
- Non-tax sources of revenue will fall into the following categories:
 - Unrestricted grants and contributions
 - Unrestricted investment income
 - Miscellaneous

Statement of Activities

- **Other potential items**

- Extraordinary items

- Unusual in nature (possessing a high degree of abnormality *and* clearly unrelated the ordinary activities of the entity.
- Infrequent in occurrence (not reasonably expect to recur in the foreseeable future, taking into account the environment in which the entity operates.

- Special items

- Significant transactions or other events within the control of management that are unusual in nature or infrequent in occurrence

- Transfers

- This line item contains transfers not eliminated between governmental and enterprise funds

Nature & Purpose of Fund Accounting

- **Private Sector**
 - Accountable for resource utilization after the fact
- **Public Sector**
 - Assistance from higher levels of government
 - Legislative branch vs management
 - Accountability preempted

of Funds Principle

- Minimum number of funds to meet legal and administrative requirements
- Too many funds?
 - Complexity
 - Inefficient
 - Inflexible

Fund Defined

A fiscal and accounting entity with a *self balancing set of accounts* recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are *segregated* for the purpose of carrying on *specific activities* or attaining certain objectives *in accordance with* special regulations, *restrictions or limitations*.

Funds Categories

- **Governmental Funds**
 - Used to account for activities primarily supported by taxes, grants, and similar revenue sources
- **Proprietary Funds**
 - Used to account for activities that receive significant support from fees and charges
- **Fiduciary Funds**
 - Used to account for resources that a government holds as agent or trustee for an outside party

Fund Types

- **Governmental**
 - General
 - Account for everything not accounted for or reported in another fund
 - Special Revenue
 - Proceeds of *specific revenue sources* restricted or committed to expenditure for *specified purposes* other than debt service or capital projects

Fund Types

- **Governmental**
 - **Capital Projects**
 - To account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays
 - Prevent data distortion
 - **Debt Service**
 - To account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest
 - **Permanent funds**
 - Resources restricted to the extent that only earnings and not principal may be used to support government activities

Fund Types

- **Proprietary**
 - Enterprise
 - *May be used for any activity for which a fee is charged to external users for goods or services*
 - *Must be used if :*
 - *Outstanding debt backed by revenue*
 - *Laws or regs. require fees to recover cost*
 - *Pricing policy in place to recover cost*

Fund Types

- **Proprietary**
 - Internal Service
 - To report any activity that provides goods or services to other funds, departments, or agencies of the primary government or its component units
 - Always optional
 - Limitations:
 - Government must be predominant participant
 - Fund must operate on breakeven over time

Fund Types

- **Fiduciary**
 - Pension/OPEB Trust
 - Investment Trust
 - External portion of investment pools
 - Private-purpose Trust
 - All other trust arrangements
- Custodial Fund
 - Government controls the assets
 - Assets are NOT own-source revenues or from government mandated nonexchange transactions
 - Assets are held for the benefit of others

Presentation of Funds

- **Too many funds to present individually**
 - Not feasible
 - Confusing
- **2 Categories**
 - Major – presented separately
 - Nonmajor – aggregated into single column

Major Fund Determination

- **Test financial statement elements**
 - Assets + deferred outflows
 - Liabilities + deferred inflows
 - Revenues (exclude other financing sources)
 - Expenditures/expenses (exclude other financing uses)

Major Fund Determination

- **Exclusions from calculation**
 - Governmental
 - Extraordinary items
 - Other financing sources and uses
 - Enterprise
 - Extraordinary items
 - Transfers in or out

Major Fund Determination

- **How to calculate**
 - Compute 10% of each element for governmental funds
 - Compute 5% of each element for governmental funds + enterprise funds
 - Use highest amount for each element threshold

Major Fund Determination

- **How to calculate**
 - Compare each element for each fund to the figures from previous slide
 - If any fund element exceeds the threshold, then it is a major fund and must be presented in its own column
- **Qualitative major fund**
 - Management believes it should be shown even if threshold is not met each year
 - Often used for consistency purposes

What Are Government Fund Statements?

- Governmental fund balance sheet
- Governmental fund statement of revenues, expenditures and changes in fund balances
- Budgetary comparison (optional as basic financial statement or RSI)

What is the GF Balance Sheet?

- Financial assets
- Deferred outflows of resources
- Liabilities to be paid from available expendable resources
- Deferred inflows of resources
- Difference = fund balance
 - Non spendable
 - Spendable
 - *Restricted*
 - *Committed*
 - *Assigned*
 - *Unassigned*

Components of Fund Balance

- **5 Categories**
 - Non-spendable
 - Restricted
 - Committed
 - Assigned
 - Unassigned
- Not all will always be present

Non-spendable fund balance

- **Not in spendable form**
 - Cannot ever be spent (e.g. supplies inventories and prepaid items)
 - Cannot currently be spent (e.g. the long term portion of loans receivable and nonfinancial assets held for resale)
- Legally or contractually required to be maintained intact (principal of an endowment or revolving loan fund)

Non-spendable, continued

- Resources that cannot currently be spent
 - If constraints on the purpose for which the proceeds can be used, classify based on constraint
- Only long-term loans receivable would be classified as non-spendable fund balance
- Other long-term receivables offset by liability for deferred revenue (thus no fund balance)

Spending constraints

- Restricted
 - Committed
 - Assignment
-
- No requirement that constraint be narrower than the purpose of the fund (except for general fund assigned fund balance)

Restricted fund balance

- **Amounts subject to externally enforceable legal restrictions**
 - Externally imposed by creditors, grantors, contributors, or laws or regulations of other governments
 - Imposed by law through constitutional provisions or enabling legislation

Committed fund balance

- Amounts whose use is constrained by limitations that the government imposes upon itself
 - Imposed at the government's highest level of decision making
 - Normally the governing body, with consent of the executive
 - Binding unless removed in the same manner
 - Action taken no later than the close of the reporting period

Assigned fund balance

- **Intended use of resources**
 - Established by the governing body itself, or
 - Established by a body or an official delegated by the governing body
- Never in excess of total fund balance less its non-spendable, restricted and committed components

Committed v. Assigned

- **Level at which action must be taken**
 - Committed requires highest level of decision-making
 - Assigned allows delegation to some other body or official
- **Action necessary**
 - Formal action to impose, remove, or modify a constraint reflected in committed
 - Less formal for assigned

Unassigned fund balance

- Excess of total fund balance over non-spendable + restricted + committed + assigned components
 - Positive balance only possible in the general
 - Deficit balance possible in any governmental fund
 - Deplete general fund assigned before reporting deficit unassigned

What is the GF Operating Statement?

- Statement of revenues, *expenditures* and changes in fund balances
- Other financing sources and uses reported separately to avoid distorting trend data
 - Issuance of debt (including capital leases)
 - Sale of capital assets (if not “special item”)
 - Transfers
 - Refunding transactions

What is the Format of Operating Statement?

- Revenues
- Expenditures
- Excess (Deficiency)
- Other financing Uses
- Special & Extraordinary Items
- Net change in Fund Balance
- Beginning Fund Balance
- Ending Fund Balance

How do we report?

- Revenues
 - By major source
- Expenditures
 - By function or program (at minimum)
- What about capital outlay?

What is the Budgetary Comparison?

- **Compare**
 - Original budget to final amended budget
 - Final amended budget to actual (presented on the budgetary basis)
- **Options**
 - Basic financial statement (GFOA recommended practice consistent with current practice)
 - Required supplementary information

Why GF Financial Statements?

- Most decisions in public sector made in context of operating budget
 - Focus on near-term inflows and outflows of spendable resources
 - Includes budgeted items not otherwise reported in operating statement (e.g., capital outlay)
 - Excludes from operating statement items not typically budgeted (e.g., the incurrence of liabilities payable in future years, depreciation)

Reconciliation of Fund Balances to Net Position

- Shows the change in measurement focus from the current financial resources focus (modified accrual) to economic resources focus (full accrual)
- Presentation
 - May be located at the bottom of the Balance Sheet or on a separate page
 - Should start with governmental fund balances and show reconciling items to Net Position

Reconciliation of Fund Balances to Net Position

- **Common reconciling items**

- Capital Assets
- Long-term unmatured principal
- Unmatured interest payable
- Accrued liabilities (such as compensated absences)
- Unamortized premiums/discounts on long-term debt
- Deferred charges on debt refundings
- Net pension/OPEB liability related items
- Internal service fund (discussed later)

Reconciliation of Changes in Fund Balance to Changes in Net Position

- Shows how the change in accounting basis affects the changes in fund balance and net position
- Presentation
 - May be located at the bottom of the Statement of Revenues, Expenditures, and Changes in Fund Balances or on a separate page
 - Should start with Change in Fund Balances and show reconciling items to Change in Net Position

2 Types of Proprietary Funds

- **Enterprise**
 - Services to non-government customers
- **Internal Service**
 - Services to other funds, departments or agencies of the primary government

What are Proprietary Statements?

- Statement of net position
- Statement of revenues, expenses and changes in fund net position
- Statement of cash flows

Measurement Focus and Basis of Accounting

- **Economic Resources**
- **Full Accrual**
 - Revenues recognized when earned
 - Expenses recognized when incurred

Statement of Net Position/ Balance Sheet

- Must use classified format (classifying assets and liabilities as current and noncurrent)
- Major fund reporting same as governmental funds; except internal service funds never major and 10 and 5 percent criteria should be applied to all enterprise funds and total of all governmental and enterprise funds, respectively
- Separate aggregated column for internal service funds immediately following the total column for all enterprise funds (non-major by definition)

3 Classifications of Net Position

- Net investment in capital assets
- Restricted net position
- Unrestricted net position

What is the PF Statement of Changes?

- **Operating items distinguished from nonoperating items**
 - Demonstrates the degree to which a fund recovers the costs of the services it provides
- **Nonoperating items**
 - Capital grants
 - Operating subsidies
 - Taxes
 - Interest
 - Other
- **Reconcile operating income to net cash**

Order of Presentation

- Operating revenues
- Operating expenses
- Operating income (loss)
- Nonoperating revenues (expenses)
- Capital contributions; special and extraordinary items; transfers
- Net position, Beginning of year
- Net position, End of year

What is the PF Statement of Cash Flows?

- Positive or negative cash flow? Not evident from operating statement (unlike governmental funds)
- What are the sources and uses of cash?
 - Operating activities
 - Noncapital financing activities
 - Capital and related financing activities
 - Investing activities
- Must use direct method

Internal Service Fund Consolidation

- **Definition**

- Used to report any activity that provides goods or services to other funds, departments, or agencies of the primary government and its component units, or to other governments on a cost-reimbursement basis

- **Consolidation**

- For government wide reporting, internal service funds must be incorporated into either governmental or business-type activities
- Based on predominant users

Internal Service Fund Consolidation

- **Consolidation**

- Operating profits/losses are allocated
- Use reasonable basis for allocation
- Assets/liabilities should be reported with the predominant user of the goods and/or services
- Amounts owed between governmental and business-type activities show up on the Statement of Net Position as “Internal Balance Receivable/Payable”

GASB 87 - Leases

Scope and Definition of Lease

- **Effective for reporting periods beginning after 6/15/21 (thank you GASB 95!)**
- **Applicable to “leases”**
 - Contract
 - Right to Use an Asset
 - Period of Time

Definition of Lease Term

- **Lease Term = Noncancelable period of lease, plus the following if reasonably certain:**
 - Periods covered by lessee's option to extend
 - Periods covered by lessee's option to terminate
 - Periods covered by lessor's option to extend
 - Periods covered by lessor's option to terminate
 - Fiscal funding or cancellation clause

Certain Regulated Leases

- **Lessors should recognize revenue based on payment provisions when external sources establish:**
 - Lease rates cannot exceed a reasonable amount determined by external regulator
 - Lease rates are required to be similar for similar lessees
 - Lessor cannot deny lessees if facilities are available
- **Example** = Aviation leases governed by U.S. Department of Transportation and Federal Aviation Administration

Certain Regulated Leases

- **Lessors with one or more regulated leases must disclose:**
 - General description of agreements
 - Extent to which capital assets are used under these agreements
 - Total amount of revenue recognized in reporting period
 - Schedule of future minimum payments
 - Amount of revenue recognized in current period related to variable payments not included in future minimum payments
 - Terms and conditions where lessee could terminate

Short-Term Leases

- Short-term leases are excluded from the reporting requirements of GASB 87
- Short-term means maximum possible term under the lease contract is 12 months (or less)
- Recognize lease payments as revenue (lessor) and expense (lessee)
- Do not recognize revenues or expenses for rent holidays

Contracts that Transfer Ownership

- **Report a transaction as a finance purchase (lessee) and sale of asset (lessor) if:**
 - Contract transfers ownership of the asset to the lessee by the end of the contract period and
 - Contract does not include termination options

Lessee Accounting

- Lease Liability
- Lease Asset
- Disclosures

Lease Liability

- **Liability is measured at the present value of payments expected to be made during lease term, including:**
 - Fixed payments
 - Variable payments based on an index or rate
 - Variable payments that are fixed in substance
 - Reasonably certain residual value guarantees
 - Reasonably certain purchase options
 - Termination penalties if factored into the lease term
 - Lease incentives
 - Any other payments that are reasonably certain

Lease Liability

- **Discount rate used for present value of liability should be:**
 - Interest rate the lessor charges the lessee, which could be implicit
- If interest rate cannot be readily determined the lessee's incremental borrowing rate can be used
- The discount on the lease is amortized and reported as interest expense

Lease Liability

- **Remeasure lease liability if:**
 - Change in lease term
 - Likelihood of residual value being paid changes
 - Likelihood of a purchase option change
 - Change in estimated payment amounts
 - Change in interest rate being charged by lessor
 - A contingency occurs that triggers variable payments
- If a remeasurement occurs, you should adjust any index rate relating to variable payments. However, a change in index rate does not require remeasurement.

Lease Asset

- **Lease asset is initially measured as the sum of:**
 - Initial measurement of lease liability
 - Lease payments made before commencement of lease term, less incentives received
 - Initial direct costs necessary to place the asset into service

Lease Asset

- Lease asset is amortized over the shorter of the lease term or useful life of the asset
- Amortization will be an expense that can be combined with depreciation expense for reporting purposes
- If a purchase option is reasonably certain, the asset should always be amortized over the useful life of the asset

Notes to Financial Statements

- Description of leasing arrangements including info on variable payments, residual value guarantees, etc.
- Total amount of lease assets and accumulated amortization (separate from other capital assets)
- Amount of lease assets by major class (separate from other capital assets)
- Expense recognized for variable payments not included in lease liability
- Expense for other payments not included in lease liability

Notes to Financial Statements

- Principal and interest requirements to maturity for the lease liability
- Commitments under the leases before the start of the lease term
- Impairment losses, if any
- Sublease, Sale-Leaseback, Lease-Leaseback, if applicable

Information to Collect

- Lease Term – Including reasonably certain events
- Explicit or implicit interest rates
- Summary of variable payments reasonably certain to happen
- Annual status updates on leases and underlying assets

Lease Accounting

- Lease Receivable
- Deferred Inflow of Resources
- Underlying Asset
- Notes to Financial Statements

Lease Receivable

- Receivable is initially measured at the present value of lease payments expected to be received, including:
 - Fixed payments
 - Variable payments that depend on an index rate
 - Variable payments that are fixed in substance
 - Residual value guarantee payments that are fixed in substance
 - Any lease incentives payable to the lessee

Lease Receivable

- Discount rate used for present value of receivable should be:
 - Interest rate the lessor charges the lessee, which could be implicit
- The discount on the lease is amortized and reported as interest revenue

Lease Receivable

- Remeasure lease receivable if:
 - Change in lease term
 - Change in interest rate being charged by lessor
 - A contingency occurs that triggers variable payments
- If a remeasurement occurs, you should adjust any index rate relating to variable payments. However, a change in index rate does not require remeasurement.

Deferred Inflow of Resources

- Deferred inflow is initially measured as the sum of:
 - Initial measurement of lease receivable
 - Lease payments received before commencement of lease term, less incentives paid
- Deferred inflows are recognized as revenue over the term of the lease

Underlying Asset

- Lessor does not derecognize the underlying asset
- Normally, the lessor continues to depreciate and evaluate asset for impairment
- If the contract requires the lessee to return the asset in its original or enhanced condition, lessor would not depreciate the asset during the lease term

Notes to Financial Statements

- Description of leasing arrangements including information on variable payments
- Total amount of revenue recognized from leases during the year
- Amount of revenue recognized from variable payments not included in the lease receivable
- Existence of options by the lessee to terminate the lease
- Leases of assets that are investments, regulated leases, subleases, sale-leaseback, lease-leaseback, if applicable

Information to Collect

- Lease term – including reasonably certain events
- Explicit or implicit interest rates
- Summary of variable payments reasonably certain to happen
- Termination events able to be exercised by lessee
- Annual status updates on leases and underlying assets

Other Important Information

- Contracts with Multiple Components
- Lease Modifications
- Lease Terminations

Contracts with Multiple Components

- Lease and non-lease components of contracts should be accounted for separately
 - For example, right to use a building and maintenance of the building
- If a lease includes the lease of multiple assets with different lease terms or asset classes, each leased asset should be accounted for separately

Contracts with Multiple Components

- Allocate lease components based on:
 - Prices stated in the contract, as long as deemed reasonable
 - If no stated prices, then use professional judgement while maximizing use of observable input
- If not practical to determine allocation for some or all components, account for all components as a single lease
- If accounting for as a single lease, accounting should be based on the primary lease component

Lease Modifications

- Lessee and Lessor account for lease modifications as a separate lease if:
 - Modification gives the lessee an additional lease asset and
 - Increase in lease payments for the additional asset is not unreasonable
- If lease modification doesn't require separate lease accounting, then remeasure lease liability (lessee) or receivable (lessor)

Lease Termination

- Lessee and lessor account for a decrease in the lessee's right to use underlying assets as a partial or full termination
- Generally, reduce balance sheet items based on the termination and recognize a gain or loss for the difference
- If termination is due to the lessee purchasing the assets:
 - Lessee would reclassify asset
 - Lessor would derecognize asset and report gain or loss



CLARK SCHAEFER HACKETT
BUSINESS ADVISORS

QUESTIONS?