

GASB 87 ACCOUNTING AND IMPLEMENTATION CONSIDERATIONS

June 14, 2021

HM2
MB46

Slide 1

HM3 Update the month/date.
Horaney, Michelle, 6/11/2021

MB46 Date Updated
Malinowski, Bob, 6/11/2021

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Agenda



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GASB 87 Overview	10
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- Upon completing this course, you will be able to:
 - Identify key technical requirements of the new lease accounting standard, GASB 87
 - Recognize GASB 87 issues related to lease term, payments, discount rate, and embedded leases
 - Distinguish the primary components and work streams involved with implementing GASB 87

GASB 87 OVERVIEW



"IT LOOKS LIKE THEY'RE BRINGING IN THE NEW REGULATIONS
MANUAL."

GASB 87 big picture



- GASB Statement No. 87 (GASB 87) is a significant change in lease accounting and financial reporting.
- The new standard impacts nearly all GASB reporting entities.
- Most leases will be recorded as a “right to use” asset on the Statement of Net Position.
- Information technology systems can be significantly impacted.
- Implementation requires involvement throughout an entire organization—not just within accounting and finance departments.



Effective date and transition



- GASB 87 is effective for periods beginning after June 15, 2021 and all reporting periods thereafter.
- Changes adopted should be applied retroactively by restating financial statements, if practicable, for all prior periods presented.
- Leases should be recognized and measured using the facts and circumstances that existed at the beginning of the implementation period.
- Lessors should not restate the assets underlying their existing sales-type or direct-financing leases.
 - Any residual assets for these leases should become the carrying values of the underlying assets.



Lessee accounting

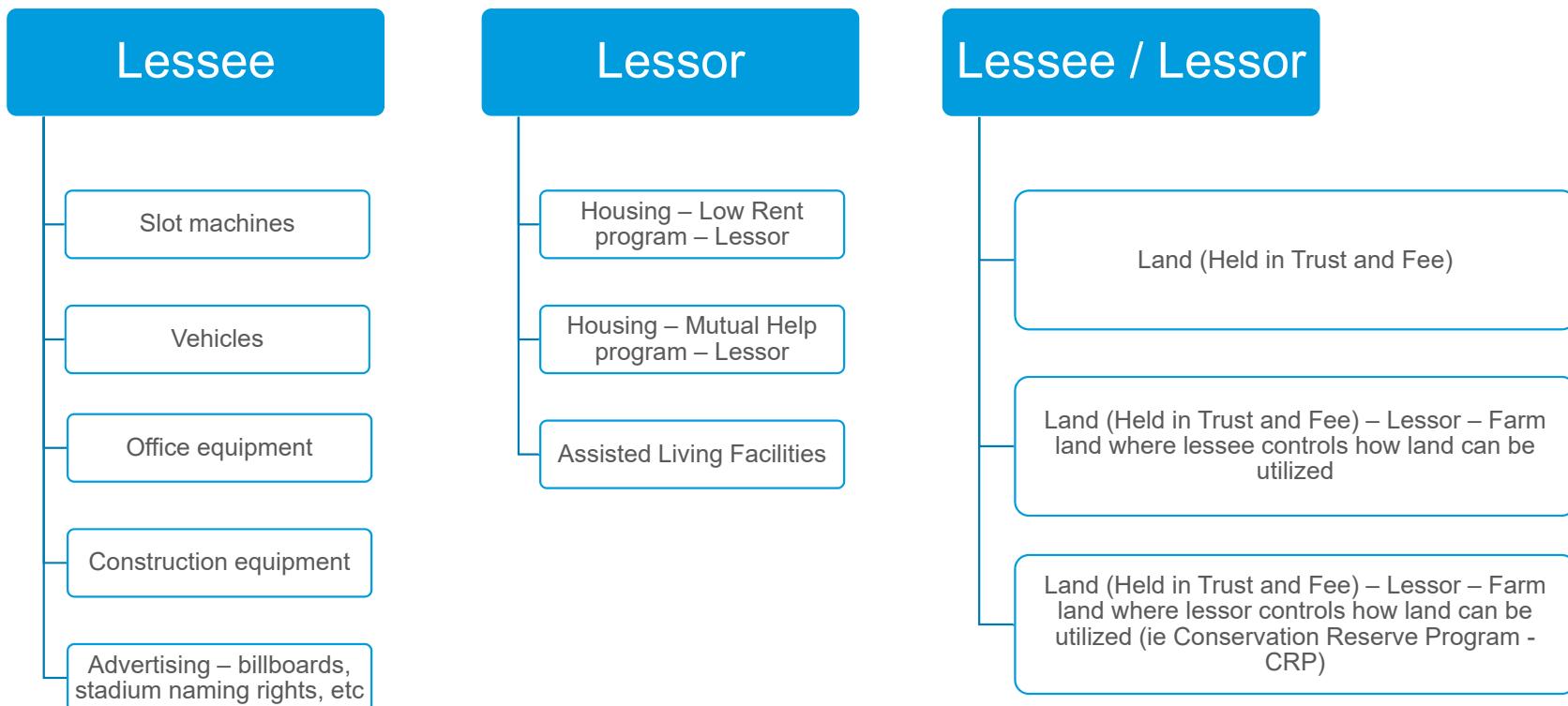
- At the commencement date, a **lessee** shall recognize a lease liability at the present value of the remaining lease payments and a lease asset based on the lease liability adjusted for certain items.
- Over the lease term the lessee recognizes interest expense and depreciation expense relating to amortization of the lease liability and asset.

Lessor accounting

- At the commencement date, a **lessor** shall recognize a lease receivable and a deferred inflow of resources.
- Over the lease term, the lessor recognizes revenue related to interest earned on the receivable and amortization of the deferred inflow of resources

* For financial statements prepared using the current financial resources measurement focus, leases should be accounted for consistent with governmental fund accounting principles

Tribal considerations

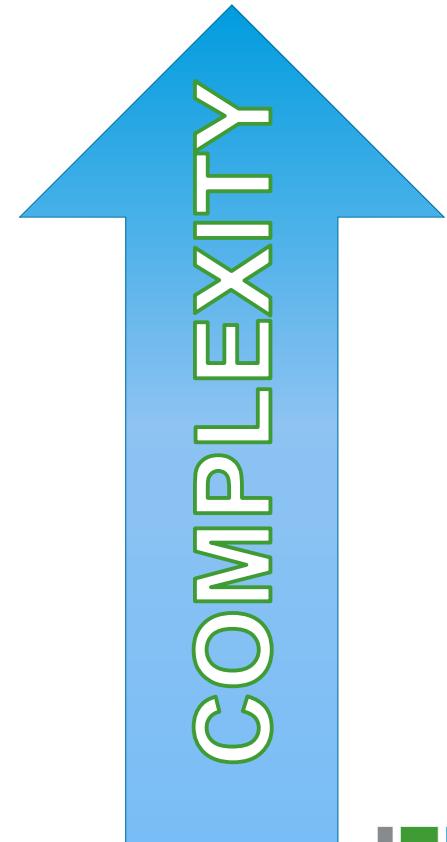


When the lessee or lessor is included as a blended component unit of the primary government, the reporting requirements of GASB 87 do not apply

Why is implementation difficult?



- Decentralized lease processes
- Volume of data and documents to manage
- Technical accounting requirements
- Determining discount rates
- Reassessment of lease assumptions upon transition
- Systems considerations
- Lease and nonlease components
- Identifying and accounting for embedded leases
- New controls
- Resource constraints



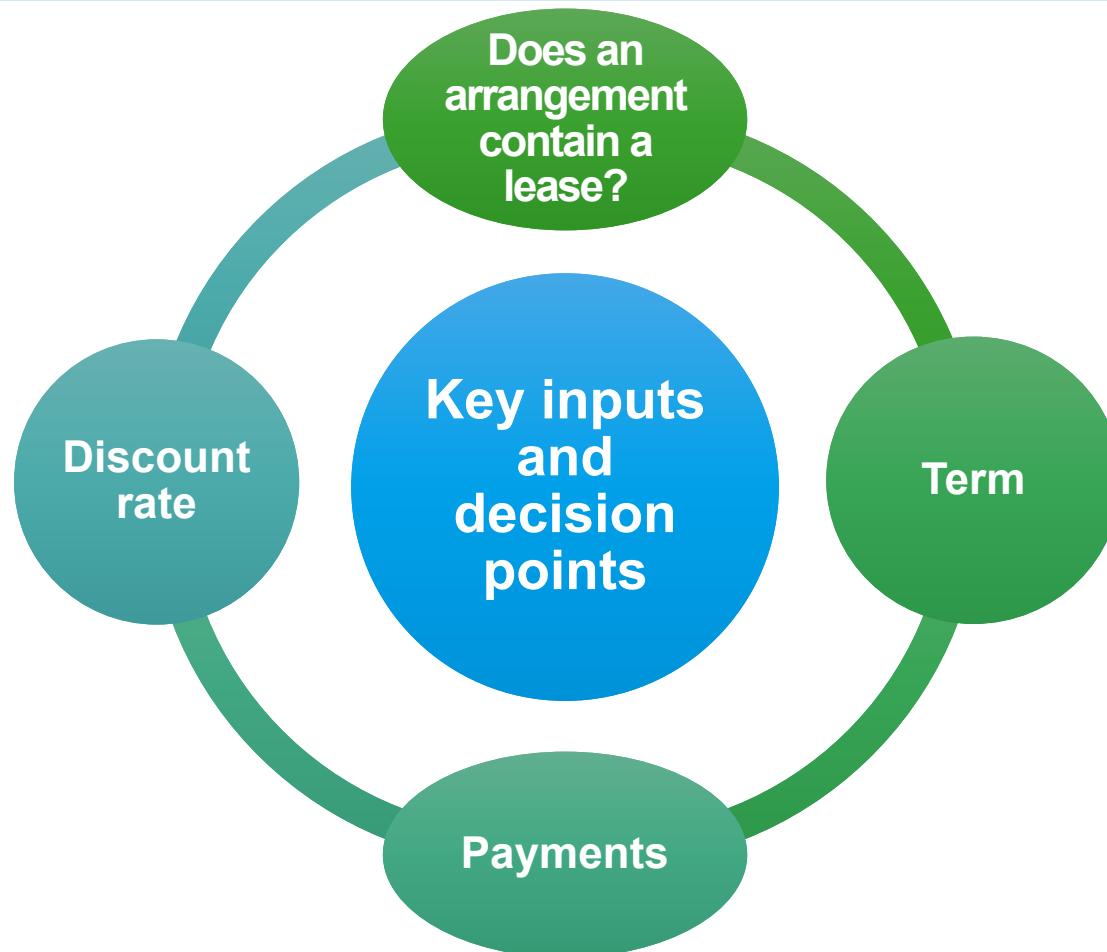


TECHNICAL ACCOUNTING CONSIDERATIONS

- A lease is defined as a contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction.
- GASB 87 does not apply to:
 - Leases of intangible assets
 - Leases of biological assets, including timber, living plants, and living animals
 - Leases of inventory
 - Contracts that meet the definition of a service concession arrangement
 - Leases in which the underlying asset is financed with outstanding conduit debt, unless both the underlying asset and the conduit debt are reported by the lessor.
 - Supply contracts, such as power purchase agreements.



Primary considerations



Short-term leases

- A short-term lease is a lease that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised.
- Short-term leases are not recorded on the statement of financial position as a right to use asset and lease liability.

Case Study: Slot machine lease

Facts:

- Casino leases a slot machine
- Rent: 20% of daily coin-in, subject to \$100 daily minimum
 - Based on similar slot machines, lessee is reasonably certain that the slot machine will generate at least \$500 in receipts per day
- Term: month-to-month, lessee can cancel the lease anytime or can continue to lease the slot machine indefinitely

Questions:

- What is the lease term?
- How is the lease asset and liability calculated?

Case Study: Slot machine lease continued

What if:

- Lease could be terminated by either party upon 30 days notice?

What if:

- No minimum lease payments are required?

Lease payments

Lease payments should be consistent with the lease term



- Fixed (including in-substance fixed) payments, less any lease incentives paid or payable to lessee
- Variable payments based on an index or rate
- Exercise price of a purchase option*
- Payments for penalties for terminating lease**
- Amounts it is probable will owe under residual value guarantees (lessees only)***

* Including only if reasonably certain of exercise

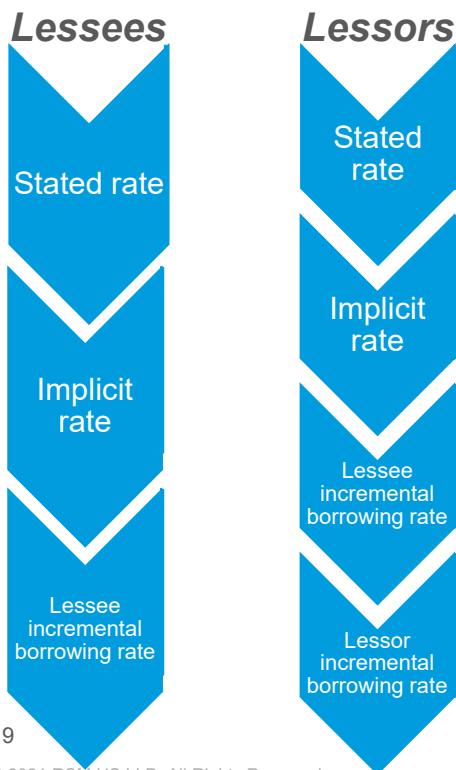
** Include only if the lease term reflects the lessee exercising an option to terminate the lease

*** Change from existing US GAAP under which full amount is included

Variable payments that are performance or usage-based are not included in the measurement of the lease liability

Discount rate

Lease payments should be discounted using the interest rate the lessor charges the lessee. Lessees and lessor should consider the following in this analysis:



- If the lease contract contains a stated interest rate, the stated rate generally is the charges the lessee.
- If there is no stated rate (or if the stated rate is not the rate the lessor charges the lessee), the lessor should determine whether the rate implicit in the lease can be estimated.
- Lessees and lessors should use professional judgment to determine their best estimate for the interest rate, maximizing the use of observable information; for example, using the lessee's estimated incremental borrowing rate or published market rates for similar instruments.
- If there is no stated rate, and neither the implicit rate, nor the lessee's incremental borrowing rate are determinable, the lessor may use the its own incremental borrowing rate.

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Embedded leases

- Certain arrangements that are not structured as leases may contain **embedded leases**.
- Examples of types of contracts that often may contain embedded leases include:



IT and office equipment



Miscellaneous equipment



Advertising



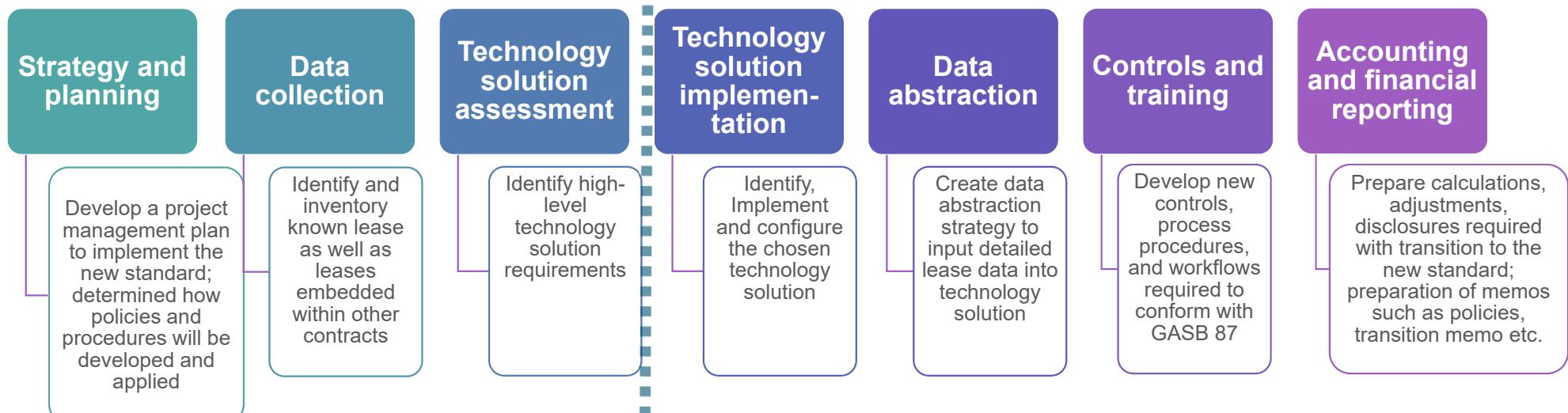
Cell towers / antennas

- If a contract *contains* a lease, it does not automatically indicate that the entire contract *is* a lease, i.e., it may also contain nonlease components.

IMPLEMENTATION CONSIDERATIONS

GASB 87 Assessment and Implementation

Key workstreams required to implement GASB 87 usually involve:

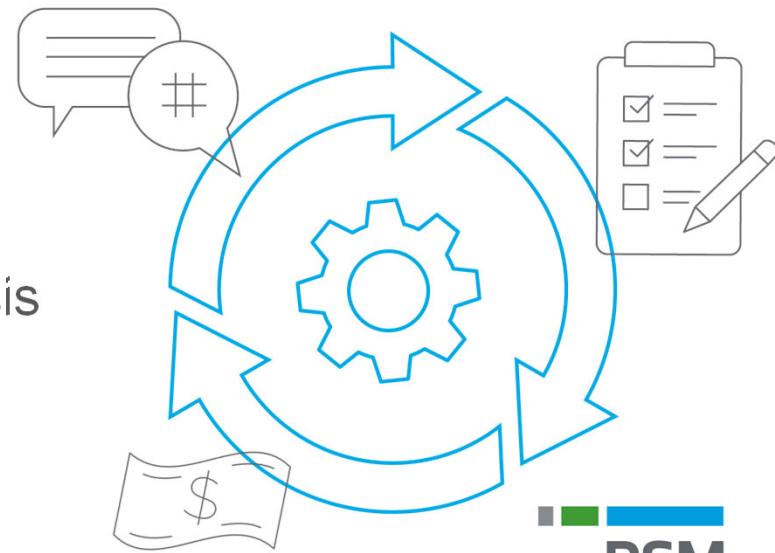


Assessment

Implementation

Data collection – ensuring lease completeness

- Have you identified all of your leases?
- Ensuring completing of the lease portfolio is critical under GASB 87.
- Procedures to verify completeness include:
 - Review of footnote disclosures
 - Review of board / meeting minutes
 - Surveys to business units
 - Cash disbursement / recurring payments analysis



Data abstraction and review

Key components of the abstraction process involve:

ABSTRACT

- Abstract data from lease documents and prepare templates to be imported into the technology solution
- Apply all judgments made in the preparation phase to the data being abstracted
- Ensure all documents are reviewed and abstracted into the system by checking the most current lease documents against the expenses being recorded in the GL

VALIDATE

- Validate the completeness of information entered into the system
- Validate the accuracy of data entered into the system
- Validate the GASB 87 calculations tie back to the current GL

REVIEW

- Perform reviews to ensure accuracy of the information inputted
- Review of information inputted into the abstraction templates or lease technology solution
- Review the accounting calculations under GASB 87
- Provide population to you for review prior to finalizing the abstracts

Need for a technology solution

A technology solution can help centralize all leases onto a single platform, perform calculations, assist with lease administration and provide necessary information for reporting:

- **Calculate future lease liability** based on net present value (NPV) of future payments based on interest rates which could differ by contract. Systems will store appropriate data and calculate the liability
- **Calculate the right to use asset** with adjustments
- **Create amortization schedules** for lease assets and liabilities as for lessee and lessors
- **Track terms including renewals, options, expirations, etc.**; terms can be stored within the system and notifications can be generated
- **Facilitate efficient financial reporting including** compilation of required quantitative disclosures
- **Centralize and store lease information**, process payments and assist in establishing controls over lease procurement

THANK YOU FOR
YOUR TIME AND
ATTENTION



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