
Appendix A:

OSC Guide to Identifying Leases under GASB 87

The purpose of this document is to provide a guide to staff throughout the State in (1) identifying leases at their organization and (2) creating a central repository (i.e., an inventory) of leasing contracts with relevant information to aid in the implementation and reporting requirements for GASB 87, *Leases*. This document should be read in conjunction with completing the required elements of the GASB 87 Lease Inventory Template, sent to all state entities on May 17, 2019. A copy of the Lease Inventory Template can be found [here](#).

Current reporting guidance promulgated by the Governmental Accounting Standards Board (GASB) states that leases are either operating or capital. The issuance of GASB Statement 87, *Leases*, establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. GASB 87 is effective for the fiscal year ended June 30, 2022, including a restatement of beginning net position as of July 1, 2021.

The new standard requires each agency to examine its existing leasing and other contracts in their entirety to determine how they will be reported under the new guidance. **GASB 87 will require significant time, up-front effort, and coordination within each agency. Staff should be maintaining their lease repositories on an ongoing basis starting now.** This will require ongoing coordination among various business units or departments, such as Purchasing and Procurement, depending on the extent of decentralization of leasing contracts and the procurement process. The following is a general step-by-step guide for the identification of leases at your agency.

Step 1: Read GASB 87 and GASB Implementation Guide 2019-3, *Leases*

Begin by reading [GASB 87, *Leases*](#). Also refer to the [Implementation Guide 2019-3, *Leases*](#), which provides examples and clarification on the requirements contained within GASB 87. [Implementation Guide 2020-1](#) and [Implementation Guide 2021-1](#) also provide sections of further guidance specific to leases (scroll to Page 7 in the FRU for effective dates and specific paragraphs).

Step 2: Identify Leases at Your Organization

2a: **Examine your Procurement Process and Form a Leases Workgroup.** Examine your agency's process for entering into contracts. If several departments are involved in this process, form a leases workgroup to ensure that all types of current and potential leasing contracts can be identified. A leases workgroup should include members of the accounting team (Controller's Office) and any other business units/departments within your agency that have the authority to engage in contracts with parties both internal and external to the State. Gather all real property leases that are currently held with the State Property Office for your organization. ***At least one member of the accounting/ACFR team at your agency should be involved in this process*.**

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2b: Examine Existing and Known Leases. Begin the process of identifying leases by gathering contracts that are already reported as operating or capital leases. Examine your general ledger accounts for capital leases payable, rental expense, and rental income to ensure you are considering all existing and recorded leasing arrangements. **Use Appendix B: OSC Decision Guide for Lease Identification to help you identify if you have a leasing arrangement under GASB 87.** If the contract meets the definition of a lease under GASB 87, add it to the Lease Inventory Template on the correct tab depending on whether your agency is the lessee or lessor in the contract. **Focus on identifying and adding your largest dollar value leases first.** Convert any hard-copy lease agreements to electronic and readable/searchable (pdf) format and keep those documents in a central electronic drive/location. Do not include any leases or arrangements that should be excluded from GASB 87. See the FAQ and Glossary of Useful Terminology below and the Decision Guide tab in the template for leases that do not apply.

2c: Evaluate Other Contracts for Embedded Leases. Not every lease is labeled a “lease agreement,” and identifying embedded leases can involve considerable time and judgment as many of these contracts may not have been identified as leases in the past. Embedded leases are components within contracts that allow for the use of an asset, with the user having control over the right to use that asset. Such contracts (or components of such contracts) may be defined as leases under GASB 87 even if the contract does not use the word ‘lease’. One way to conduct a review of potential embedded leases is to analyze your agency’s payments made to outside vendors, and research what the vendor contracts underlying those payments contain. **Embedded leases may be found in advertising, service, transportation, or construction agreements as well as in related party charges. For example, related party charges could include renting pieces of land.**

Step 3: Analyze and Document Key Lease Terms, Evaluate Bond and Other Debt Covenants, Make Necessary Changes to Internal Controls and Processes

Analyze your lease agreements further, **focusing on your largest dollar value leases first.** The Lease Inventory Template contains key elements for the calculation of liabilities, assets, and deferred inflows of resources per GASB 87. Maintaining this information on a per lease basis will be essential to the accurate and complete reporting of leases statewide and for your entity. Note that lease agreements may not contain all the necessary data to comply with the new lease standards, such as fair values and discount rates. See [105.7 – Statewide Accounting Policy – Leases](#) for further guidance on capitalization thresholds for primary government entities. Also see [OSC GASB 87 Discount Rate Procedural Guidance](#) for more information on how to determine interest rates for leasing arrangements.

Those entities that are statutorily permitted to issue debt in their own name should examine their bond and other debt covenants to determine how a lease liability will affect the requirements contained therein.

GASB 87 introduces additional considerations around an entity’s internal control structure. In order to ensure accurate and complete reporting of leases, there will be an increased focus on internal controls related to identification of leasing transactions, ongoing maintenance of leasing information, and robust management review of leasing information for financial reporting at an agency level.

FAQ and Glossary of Useful Terminology*

*Note: The Implementation Guide 2019-3, Leases contains further examples, illustrations, and clarification on terminology.

Why is New Leasing Guidance Necessary?

New guidance is needed because the existing leasing standards have been in effect for decades without being changed or reconsidered. They do not take the definitions of assets and liabilities as defined by the GASB into consideration. Previous standards have been criticized for creating an artificial distinction between capital and operating leases when the economic impact is the same for the lessee.

Is OSC acquiring a statewide contract for lease software?

No. OSC recommends individual state entities consider procuring lease maintenance software if that entity has a large volume of leases (for example, greater than 15 leases). Due to the ongoing maintenance required in developing amortization schedules for each lease, accounting for lease additions, terminations, and modifications, as well as many other moving parts to the overall lease liability and lease asset calculations, entities with a large volume of leases or very decentralized operations should consider procurement of a lease maintenance software to ensure compliance with GASB 87.

What is a "Lease" under GASB 87?

Entities enter into leasing arrangements within the normal course of business. With the new standard, 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. Examples of nonfinancial assets include buildings, land, vehicles, and equipment.

What arrangements are NOT subject to GASB 87?

GASB 87 does NOT apply to:

- a.) Leases of intangible assets, biological assets, and inventory (e.g., software subscriptions, animals/plants, and finished goods inventory)
- b.) Service concession arrangements
- c.) Leases in which the underlying asset is financed with conduit debt
- d.) Supply contracts: such contracts convey access to output of assets, not control of right to use asset
- e.) Leases of financial assets reported as investments
- f.) Short term leases, as defined in GASB 87 paragraph 16 (see definition below)
- g.) Contracts that transfer ownership of the underlying asset by the end of the lease term and do not contain termination options (such contracts are considered financed purchases). If

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termination options exist, regardless of the probability of exercising the options, the transaction should be reported as a lease if all other requirements of GASB 87 are met.

Short-term lease - (outside scope of GASB 87) – 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. Options to terminate the lease are excluded. For a lease that is cancellable by either the lessee or the lessor, such as a rolling month-to-month lease or a year-to-year lease, the maximum possible term is the noncancelable period, including any notice periods. For example, if an agency has a year-to-year lease on a machine but must give at least 90-days' notice to cancel the lease, the lease term is the 12-month non-cancellable period, PLUS the notice period of 90 days. As such, the total lease term is 15 months and would not be considered a short-term lease. However, in this example, if there is no required notice period, the lease term would be 12 months, and as such a short-term lease is not subject to the requirements of GASB 87. See Questions 4.17-4.20 in the Implementation Guide 2019-3, Leases for additional examples.

Lease term - the period during which a lessee has a non-cancellable right to use an underlying asset.

Lease-leaseback transaction - an asset is leased by one party (first party) to another party and then leased back to the first party.

Sublease - a lease by a lessee of part or all leased assets to another person but with the original lessee retaining rights or interest under the original lease.

Sale-leaseback transaction – involves the sale of an underlying asset by the owner, and a lease of the property back to the seller.

Fiscal Funding/Cancellation Clause - A government agency may place a fiscal funding clause in a lease, which states that the government agency has the option to break the lease if it does not receive the money to make the lease payment through the appropriation process. The fiscal funding clause provides the government agency with a safety measure that eliminates the risk that it will have to pay high cancellation fees.

Incremental Borrowing Rate – The rate that, at the inception of the lease, the lessee would have incurred to borrow over a similar term, the resources necessary to purchase the leased asset.

Present Value - The discounted value of a future amount or amounts of cash, assuming a given rate of interest.

Regulated Lease - Leases that are subject to external laws, regulations, or legal rulings. For example, the U.S. Department of Transportation and the Federal Aviation Administration regulate aviation leases between airports and air carriers and other aeronautical users.