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Proposed Changes to Federal Lease Accounting Standards

The Federal Accounting Standards Advisory Board (FASAB) has proposed amendments to federal lease accounting standards found within Statement of Federal Financial Accounting Standard (SFFAS) 5, 'Accounting of Liabilities of the Federal Government,' and SFFAS 6, 'Accounting for Property, Plant, and Equipment,' promulgated by FASAB. The proposals would require entities leasing property to the federal government, such as private landlords, to recognize a lease receivable and deferred revenue at the beginning of the lease term (except on intragovernmental or short-term leases). The proposals are slated to take effect in reporting periods following September 30, 2018.

PUBLIC COMMENTS ARE DUE JANUARY 6, 2017.

The federal government is one of the largest tenants in the country. The General Services Administration (GSA) alone leases space to house over 600,000 government workers. GSA has over 8,000 leases throughout the U.S.

Federal government leases, such as those for commercial office buildings, are subject to numerous reporting requirements aimed at fulfilling the government's duty of accountability for federal funds and their expenditure. FASAB is the entity responsible for promulgating accounting standards for the U.S. government.

FASAB's current lease accounting standards, SFFAS 5 and 6, have received criticism for failing to make meaningful distinctions between lease types, and for providing insufficient guidance to the federal community. The current standards were premised on FASAB's notion that some leases are akin to financed purchases of the underlying asset (classified as capital leases) while other leases (classified as operating leases) are not, the distinction depending on whether a lease meets any of four tests used to determine whether most of the risks and benefits of ownership of the underlying asset (i.e. a building) are transferred to the lessee. The bright-line nature of those tests received criticism for resulting in similar leases being accounted for in different ways.

FASAB's proposed amendments seek to improve SFFAS 5 and SFFAS 6 by providing (i) relevant and meaningful financial information needed by federal financial statement users and (ii) comprehensive lease standards that better address various lease transactions of the federal community.

While the public may comment on any aspect of the proposed amendments, FASAB has solicited responses from the public on twelve specific proposals. Several key proposals include the following:

- Proposing lessor recognition of a lease receivable and deferred revenue at the beginning of the lease term, except for intragovernmental and short-term leases.

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- Proposing lessee recognition of lease liability at the beginning of the lease term, except for intragovernmental and short-term leases.
- Proposing a lessee measure the lease asset as the sum of (i) the amount of the initial measurement of the lease liability, (ii) lease payments made to the lessor at or before the beginning of the lease, less any lease incentives received from the lessor, and (iii) initial direct costs that are ancillary charges necessary to place the lease asset into service.
- Proposing the lessee re-measure lease liability at subsequent financial reporting dates if certain changes have occurred and are expected to significantly affect the amount of the lease liability, and to adjust the lease asset by such amount accordingly. If the change reduces the lease's carrying value to zero, any remaining amount should be reported in the flows statement as a gain.
- Proposing to establish distinct standards for intragovernmental leases – a contract conveying the right to use an asset for a period of time in exchange for consideration occurring within a consolidation entity or between two or more consolidation entities.

The information provided in this Bulletin does not, nor is it intended to, constitute legal advice. Readers should not take or refrain from taking any action based on any information contained in this Bulletin without first seeking legal advice.