



Leases (GASB 87)
ACCOUNTING BRIEF #28

GOVERNING REGULATIONS AND GUIDANCE

1. Governmental Accounting Standards Board Statement (GASB) No. 87, Leases.
2. Financial Data Schedule Line Definition Guide (FYE 12/31/2013 and forward), updated July 2020
3. HUD Accounting Brief 11- Accounting and Financial Reporting for Nonexchange Transactions: GASB 33

SUMMARY

GASB 87, *Leases*, was adopted to better meet the information needs of financial statement users by improving accounting and financial reporting for leases. The goal of the new lease standard is to increase the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It also 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 requires a **lessee** (i.e., the entity that is lease is granted to) to recognize a lease liability and an intangible right-to-use lease asset, and a **lessor** (i.e., the entity that issues the lease) to recognize a lease receivable and a deferred inflow of resources.

This accounting brief aims to provide users with a framework to record and report leases on the financial statements and Financial Data Schedule (FDS) accurately and to provide implementation examples for common housing authority leasing arrangements. The goal of this brief is to:

1. Provide background information for the issuance of GASB 87 and discuss the key lease concepts and terminology.
2. Provide users with guidance on the entries to record the applicable lease asset, lease liabilities, deferred inflow of resources, lease revenues and lease expense, as applicable.
3. Provide users with guidance on implementation of GASB 87.

BACKGROUND: LEASES

In 2006, the FASB and the International Accounting Standards Board (IASB) started a joint project to reexamine their guidance for leases. In June 2007, the GASB issued Concepts Statement No. 4, Elements of Financial Statements. Because the FASB's leases guidance (as of November 30, 1989) is the basis for the GASB requirements in Statement 62, the FASB and IASB project presented an opportunity for the GASB to reconsider lease accounting in light of (a) definitions of financial statement elements (including assets and liabilities) that were not in place when the GASB leases guidance was established, and (b) the research and approaches considered by the FASB and IASB. In 2011, the GASB initiated pre-agenda research on leases. The pre-agenda research initially focused on monitoring the developments of the FASB and IASB project¹.

In June 2017, GASB 87 was issued, and the statement is effective for fiscal years beginning after June 15, 2021². Under this statement, the accounting for both the lessee and lessor is significantly different from prior GAAP. For instance, other than short-term and contracts that transfer ownership³, leases previously accounted for as operating and capital leases are now categorized as financing leases. Now under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.

KEY CONCEPTS AND TERMINOLOGY

There are several GASB 87 concepts and terminology associated with evaluating leases of nonfinancial assets such as buildings, land, vehicles, equipment, etc. For instance, GASB 87,

- Defines a lease as a contract that conveys control⁴ 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.⁵
- Establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset.⁶

¹ GASB 87 Paragraph A2

² This Accounting Brief does not incorporate any GASB statements or interpretive guidance issued subsequent to GASB 87. Users should exercise professional judgment when applying this Accounting Brief and consider incorporating any new authoritative lease guidance as applicable.

³ This Statement requires lessees to recognize and measure transactions as leases, including recognition of a lease liability, except for (a) leases outside the scope of this Statement, (b) contracts that transfer ownership of the underlying asset to the lessee and do not contain termination options (but may contain fiscal funding or cancellation clauses that are not reasonably certain of being exercised), and (c) short-term leases. (GASB 87 Paragraph B34)

⁴ To determine whether a contract conveys control of the right to use the underlying asset, a government should assess whether it has both of the following:

- a. The right to obtain the present service capacity from use of the underlying asset as specified in the contract, and
- b. The right to determine the nature and manner of use of the underlying asset as specified in the contract. [GASB 87 paragraph 5]

⁵ GASB 87 Summary, Definition of a Lease

⁶ GASB 87 Summary

- Discusses the concepts of exchange or exchange-like transactions.⁷
- Provides additional guidance to assist entities in determining short-term leases, contracts that transfer ownership and the noncancelable period of a lease.
 - A short-term lease is defined as 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. For a lease that is cancelable 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.⁸
 - A contract that transfers ownership of the underlying asset to the lessee by the end of the contract and does not contain termination options, but that may contain a fiscal funding or cancellation clause that is not reasonably certain of being exercised, should be reported as a financed purchase of the underlying asset by the lessee or sale of the asset by the lessor.⁹
 - The lease term is the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period¹⁰), plus the following periods, if applicable:
 - Periods covered by a lessee's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessee will exercise that option.
 - Periods covered by a lessee's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessee will not exercise that option.
 - Periods covered by a lessor's option to extend the lease if it is reasonably certain, based on all relevant factors, that the lessor will exercise that option.
 - Periods covered by a lessor's option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessor will not exercise that option.¹¹

⁷ The scope of this Statement includes both exchange and exchange-like transactions. Footnote 1 of Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions, states that the difference between exchange and exchange-like transactions is a matter of degree. In contrast to a "pure" exchange transaction, an exchange-like transaction is one in which the values exchanged, though related, may not be quite equal or in which the direct benefits may not be exclusively for the parties to the transaction. Nevertheless, the exchange characteristics of the transaction are strong enough to justify treating the transaction as an exchange for accounting recognition. [GASB 87 footnote 1]

⁸ GASB 87 paragraph 16

⁹ GASB 87 paragraph 19 (Contracts that Transfer Ownership)

¹⁰ The noncancelable period is included in the lease term because it is the period for which the lessee and lessor are legally obligated without the possibility of cancellation. [GASB 87 Paragraph B19]

¹¹ GASB 87 Summary, Lease Term

FINANCIAL DATA SCHEDULE REPORTING UPDATES

In July 2020, the FASS Financial Data Schedule Line Definition Guide (FDS Guide) was updated to provide additional information, examples, and clarity for several new developments (e.g., RAD transactions, HOTMA regulations, and GASB 68, 75 and 87 reporting (see Table 1, Appendix A of the FDS Guide). The most significant reporting changes from GASB 87 are reporting for leased asset, liability, and deferred inflow of resources. This new lease standard also has significant implications for ground lease accounting and lease arrangements with obligations greater than twelve months. Although the definition of line 400, *Deferred Inflow of Resources*, has been updated to include lease revenue earned from leases greater than one year there were no other significant updates or new lines added to the FDS Guide for the new lease statement.

The tables below provide the FDS line reporting for both the lessor and lessee. Until the FASS-PH system is updated with new FDS lines to properly account for the lease transactions, PHAs should report their lease transactions in accordance with the FDS line reporting provided in the tables.

LESSOR ACCOUNTING	FDS LINE	FDS DESCRIPTION
Lease Receivable – Current	127	Notes, Loans, & Mortgages Receivable Current
Lease Receivable - Noncurrent	171	Notes, Loans, & Mortgages Receivable Non-Current
Deferred Inflows of Resources	400	Deferred Inflow of Resources
Interest Income	71100	Investment Income – Unrestricted
Lease Revenue	71500	Other Revenue

LESSEE ACCOUNTING	FDS LINE	FDS DESCRIPTION
Lease Asset	165	Leasehold Improvements
Accumulated Amortization	166	Accumulated Depreciation
Lease Liability	343 and 351	Current Portion of Long-Term Debt-Capital Projects/Mortgage Revenue Bonds Long-Term Debt, Net of Current-Capital Projects/Mortgage Revenue Bonds
Interest and Amortization Expense	96710, 96720, and 96730	Interest on Mortgage (or bonds) payable, Interest on Notes Payable (short and long term) Amortization of Bond Issue Costs
Lease Expense	91600 91900 Etc.	Office Expense (e.g., rental office expense) Other (e.g., office vehicle leases)
Amortization Expense	97400	Depreciation Expense

In the year of adoption, restatement of beginning equity, beginning net position, fund net position or fund balance may be required, where appropriate, for the cumulative effect of applying the new lease standards for the earliest year presented on the financial statements. Restatements should be reported on FDS Line 11040 – *Prior period adjustments, equity transfers, and corrections of errors*. FDS line detail links: 11040-010 to 11040-060, are explicitly used for prior period adjustments.

Lease Asset. GASB 87 requires that PHAs track the leases by asset type and provides for other required disclosures. For FDS reporting, total lease asset will be reported in FDS line 165. However, for financial statement and note disclosure purposes, PHAs are required to report their lease transaction under the requirements of GASB 87.

Some PHAs currently report activity in FDS line 165 – Leasehold Improvements. PHAs will continue to report the costs of improvements performed on leased property such as additions, alterations, remodeling, or renovations in this line as well as the total of the PHAs leased assets. PHAs that currently report activity in FDS line 165, should review this account to confirm that the reported is limited to only the costs of improvements performed on leased property and now leased assets.

Lease Expense. The table above provides two FDS line examples where a PHA could report their lease expense. However, when reporting, PHAs should review the FDS line definition guide and report the lease expense in the expense category that best classifies the expense. For example, a leased maintenance truck should be reported under FDS line 94200 “Ordinary maintenance and operations - materials and other”.

PHA Comments – Reconciliation Schedule. Part of HUD’s submission review procedures is to compare the totals of the FDS to the amounts reported on the PHA’s financial statement and to the notes to the financial statements making sure the various amounts match. As previously discussed, the FDS does not have all the needed line items to separately report GASB 87 transactions and therefore the PHA’s reporting of these amounts are commingled with other transactions on the FDS. For example: Lease Receivable – Current is to be reported in FDS line 127 Notes, Loans, & Mortgages Receivable Current.

To minimize the risk that the PHA’s submission is rejected or that HUD may request additional information after submission, PHAs should provide comments and/or a reconciling schedule of the GASB 87 amounts shown in their audit and how the amounts are reported on the FDS.

Financial Policy. PHAs should create a financial policy and associated procedures for leases similar to a PHA’s capitalization asset and depreciation policy and procedures.

IMPLEMENTATION OF LEASE STANDARDS – EXAMPLE OF A BUILDING OPERATING LEASE

For ease of illustration, the following building lease example assumes first year implementation and the PHA has a calendar year end of December 31, 2022.

Building Operating Lease Example. The PHA entered into a one-year non-cancelable lease on 1/1/2022, with the lessee’s option to extend each year for the next three years. The lease has an annual interest rate of 5% and requires monthly payments of \$4,000 with the first payment due on

1/1/2022. The Lessor currently owns the building and has the building recorded as a capital asset on its books. The fair value of the building as of 1/1/2022 is \$300,000. The lessee's incremental borrowing rate is 5%.

GASB 87 Analysis. The GASB 87 analysis assumes both the lessor and lessee operate with enterprise fund accounting. Considering the lease term, it was noted that only the Lessee has an option to extend the lease for four years and neither the lessor nor lessee has an option to terminate the lease. It was determined that it is reasonably certain the lease options will be extended for all three-years. Consequently, the term of the lease was determined to be four years.

The lessor expects to receive lease payments over the lease term and no reserve provision is required¹².

Using the Excel present value formula, the present value of the building lease is \$174,415.54. The annualized receipt schedule for the present value of the lease payments is shown the table below.

CALENDAR YEAR	PRINCIPAL	INTEREST	TOTAL PAYMENTS
2022	\$40,952.73	\$7,047.27	\$48,000.00
2023	\$42,287.21	\$5,712.79	\$48,000.00
2024	\$44,450.71	\$3,549.29	\$48,000.00
2025	\$46,724.89	\$1,275.11	\$48,000.00
TOTAL	\$174,415.54	\$17,584.46	\$192,000.00

The lease revenue is recognized on a systematic and rational manner (this example use straight-line basis) and is amortized through the deferred inflow as shown in the table below.

CALENDAR YEAR	AMORTIZED DEFERRED INFLOWS
2022	\$43,603.88
2023	\$43,603.88
2024	\$43,603.89
2025	\$43,603.89
TOTAL	\$174,415.54

1. **Lessor Journal Entries – Record Lease Receivable and Deferred Inflow of Resources.** The lessor's initial journal entry upon implementation of GASB 87 to record the lease receivable and deferred inflow of resources. The lessor does not derecognize the leased asset, the asset remains on the lessor's books.

¹² A lessor should initially measure the lease receivable at the present value of lease payments expected to be received during the lease term, reduced by any provision for estimated uncollectible amounts. [GASB 87 paragraph 44]

LESSOR - JOURNAL ENTRY 1	DEBIT	CREDIT
Lease Receivable – Due Within One Year (FDS Line 127 - Notes, loans, & mortgages receivable – current)	\$40,952.73	
Lease Receivable – Due Beyond One Year (FDS Line 171 - Notes, Loans, & Mortgages Receivable Non-Current)	\$133,462.81	
Deferred Inflow of Resources (FDS Line 400 -Deferred Inflow of Resources)		\$174,415.54

The Lessor's journal entry to record annual lease payments received.

LESSOR - JOURNAL ENTRY 2	DEBIT	CREDIT
Cash (FDS Line 111 – Cash – Unrestricted)	\$48,000.00	
Interest Income (FDS Line 71100 – Investment Income - Unrestricted)		\$7,047.27
Lease Receivable (FDS Line 127-Notes, Loans, & Mortgages Receivable Non-Current)		\$40,952.73

The Lessor's journal entry to record amortized deferred inflows.

LESSOR - JOURNAL ENTRY 3	DEBIT	CREDIT
Deferred Inflow of Resources (FDS Line 400 – Deferred Inflow of Resources)	\$43,603.88	
Lease Revenue (FDS Line 71500 – Other Revenue)		\$43,603.88

2. **Lessee Journal Entries – Record Lease Payable and Building (Right-to-Use Asset).** The lessee's initial journal entry upon implementation of GASB 87 to record the lease payable and Building (right-to-use asset).

LESSEE – JOURNAL ENTRY 1	DEBIT	CREDIT
Intangible Lease Asset – Building (FDS Line 165 – Leasehold Improvements)	\$174,415.54	
Lease Liability – Due Within One Year (FDS Line 343 - Current Portion of Long-Term Debt-Capital Projects/Mortgage Revenue Bonds)		\$40,952.73
Lease Liability – Due Beyond One Year (FDS Line 351 - Long-Term Debt, Net of Current-Capital Projects/Mortgage Revenue Bonds)		\$133,462.81

The Lessee's journal entry to record annual lease payments made.

LESSEE – JOURNAL ENTRY 2	DEBIT	CREDIT
Lease Liability – Due Within One Year (FDS Line 343 - Current Portion of Long-Term Debt-Capital Projects/Mortgage Revenue Bonds)	\$40,952.73	
Interest Expense (FDS Line 96720 - Interest on Notes Payable (short and long term))	\$7,047.27	
Cash (FDS Line 111 – Cash – Unrestricted)		\$48,000.00

The Lessee's journal entry to record amortization expense.

LESSEE – JOURNAL ENTRY 3	DEBIT	CREDIT
Amortization Expense (FDS Line 97400 – Depreciation Expense)	\$43,603.88	
Accumulated Amortization (FDS Line 166 – Accumulated Depreciation)		\$43,603.88

GASB 87 requires that the lessee amortize the lease asset in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset. In this example, the systematic manner was a straight-line amortization basis.

IMPLEMENTATION OF GASB 87 – CONSIDERATION OF HUD PROGRAM REGULATIONS & TENANT LEASES

HUD federally subsidizes public and Indian housing units under the Low-Income Housing Program¹³ and program participants can receive HUD subsidies and tenant rental income. The lease agreements under the Low-Income Housing Program are different from normal financing of a right to use an underlying asset and may vary by HUD program. For example,

- For the Public Housing program, the initial and renewal lease terms are regulated by HUD as follows: The initial lease shall have a twelve-month term. Except as provided in paragraph (a)(2)(ii) of this section, the lease term must be automatically renewed for the same period. (24 CFR § 966.4 - Lease requirements)
- Rent payment charged to a tenant must be reasonable as determined by HUD in accordance with applicable regulations.¹⁴

¹³ 42 USC Ch. 8: Low-Income Housing

¹⁴ 42 USC §1437a. Rental payments

- Subsidies provided under the Low-Income Housing Programs either directly or indirectly subsidize rents charged to tenants and regulations and funding vary by program.
 - **Section 8** – Housing Act of 1937, as amended, P.L. 75-412, 42 U.S.C. 1401-1435, and the Indian Housing Act of 1988, P.L. 100-358. Regulations are found at 24 CFR 982 Housing Choice Voucher Program, 24 CFR 983 Project Based Voucher Program, 24 CFR 578 Project Based Rental Assistance, 24 CFR 92 Homes Investment Partnership Program, 24 CFR 574 Housing Opportunities for Persons with Aids, and 24 CFR 576 Emergency Solutions Grant Program. Additionally, terms and conditions of funding are included in the Consolidated Annual Contributions Contracts with PHAs and Housing Assistance Payment Contracts with private owners.
 - **Section 9** – Housing Act of 1937, as amended, P.L. 75-412, 42 U.S.C. 1401-1435, and the Indian Housing Act of 1988, P.L. 100-358. Regulations are found at 24 CFR 960. The Public Housing Operating Fund provides operating subsidies to housing authorities (HAs) to assist in funding the operating and maintenance expenses of their own dwellings and the Capital Fund provides funds to housing authorities to modernize public housing developments, in accordance with Section 9 of the U.S. Housing Act of 1937, as amended. The operating subsidies are also required to help maintain services and provide minimum operating reserves.
 - **Mutual Help and Turnkey III Projects** – Housing Act of 1937, as amended, P.L. 75-412, 42 U.S.C. 1401-1435, and the Indian Housing Act of 1988, P.L. 100-358. Regulations are found at 24 CFR 950 and Additional terms and conditions of funding are included in the Consolidated Annual Contributions Contract.

PHAs should consider implementing GASB 87 based on the steps and in the order provided below. It is HUD's position that if HUD subsidized rental unit leases are appropriately evaluated under the standard, including the standard's intent, and properly documented¹⁵, HUD subsidized rental units would likely be outside of the scope of GASB 87.

- The first step is to review the terms of each lease and identify any short-term leases that are outside the scope of GASB 87.
- The second step is to consider if the monthly tenant rent amount to be paid for a housing unit is an exchange or exchange like transaction¹⁶. Nonexchange transactions are outside the scope of GASB 87.
- The third step is to consider if any of the remaining leases are regulated leases under GASB 87 paragraph 42 and 43. Certain regulated leases are outside the scope of GASB 87.

¹⁵ PHAs and auditor workpapers should show the rationale on how / why HUD subsidized rental units are outside of the scope of GASB 87.

¹⁶ The scope of this Statement includes both exchange and exchange-like transactions. Footnote 1 of Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions, states that the difference between exchange and exchange-like transactions is a matter of degree. In contrast to a "pure" exchange transaction, an exchange-like transaction is one in which the values exchanged, though related, may not be quite equal or in which the direct benefits may not be exclusively for the parties to the transaction. Nevertheless, the exchange characteristics of the transaction are strong enough to justify treating the transaction as an exchange for accounting recognition.

Absent specific guidance from GASB, HUD will allow the PHA and their auditor to determine whether GASB 87 applies to tenant leases.

IMPLEMENTATION OF GASB 87 – EXAMPLES OF NONEXCHANGE TRANSACTIONS

The scope of GASB 87 includes both exchange and exchange-like transactions, in which each party receives and gives up essentially equal values. GASB 87 excludes nonexchange transactions, in which an entity gives (or receives) value without directly receiving (or giving) equal value in exchange. GASB acknowledges that the existing guidance for nonexchange transactions in Statement 33 does not specifically address the right to use nonfinancial assets in nonexchange transactions, such as the free use of office space. GASB noted that nonexchange transactions are expected to be addressed as part of the GASB's project on revenue and expense recognition.

Land Lease Example 1. A PHA has a ground lease with the City for the property on which its apartment building is located. The lease term is from January 1, 2022, to December 31, 2072. Under the terms of the lease, PHA is to pay the City \$10 annually for the land. PHA is responsible for utilities and insurance on the property. The premises may be used only to construct, operate, and maintain housing for lower and very-low-income persons. The land has a lease market value of \$15,800 per year at the time of the lease.

GASB 87 is applicable to exchange and exchange-like transactions. In this example, the PHA's right to use the land for \$10 per year is a nominal value and does not meet the definition of an exchange or exchange-like transaction¹⁷. This lease does not meet the requirement of GASB 87¹⁸. Transactions resulting from this lease should be considered as Nonexchange transactions under HUD Accounting Brief #11 and GASB 33.

Land Lease Example 2. A Low-Income Housing Tax Credit (LIHTC), Apollo 1 LLP, has a ground lease with a PHA for the property on which its project will be located. The lease term is from March 1, 2022, to February 31, 2072. Under the terms of the lease, the LIHTC is to pay the PHA \$100 annually for the land. The LIHTC is responsible for utilities and insurance on the property. The premises may be used only to construct, operate, and maintain housing for lower and very-low-income persons. The land has a lease market value of \$20,000 per year at the time of the lease.

GASB 87 is applicable to exchange and exchange-like transactions. In this example, the LIHTC's right to use the land for \$100 per year is a nominal value and does not meet the definition of an exchange or exchange-like transaction. This lease does not meet the requirement of GASB 87. Transactions resulting from this lease should be considered as Nonexchange transactions under HUD Accounting Brief #11 and GASB 33.

¹⁷ The definition of a lease in this Statement also specifies that a lease should be an exchange or exchange-like transaction. Some governmental contracts that transfer the right to use an asset require only a nominal amount, such as one dollar per year, to be exchanged for the right to use the underlying asset. The Board believes that the substance of that type of arrangement represents a nonexchange transaction (such as a donation or grant), which is addressed within the scope of Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions. [GASB 87 Paragraph B9]

¹⁸ See GASB Comprehensive Implementation Guide, Chapter 12, question 12.2.1 for additional guidance.