PURPOSE:
This policy provides guidance on accounting and financial reporting for capital leases by lessees and lessors.

AUTHORITY:
ORS 293.590
NCGA Statement No. 5
GASB Statement No. 34
GASB Statement No. 38
GASB Statement No. 62
GASB Statement No. 87

APPLICABILITY:
This policy applies to all state agencies included in the State’s annual financial statements, except for those agencies specifically exempted by OAM Policy 01.05.00.

George Naughton, Chief Financial Officer
Signature on file

OAM Policy 01.05.00

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DEFINITIONS:
For purposes of this policy, conveys control of the right to use an underlying asset includes 1) the right to obtain the present service capacity from use of the underlying asset as specified in the contract and 2) the right to determine the nature and manner of use of the underlying asset as specified in the contract.

A lease is a contractual agreement that conveys the right to use specific property for a specific period of time in return for stipulated, and generally periodic, cash payments. It 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. Leases include contracts that, although not explicitly identified as leases, meet the definition of a lease. This definition excludes contracts for services except those contracts that contain both a lease component and a service component.

As used in this policy, lease incentives are (a) payments made to, or on behalf of, the lessee, for which the lessee has a right of offset with its obligation to the lessor, or (b) other concessions granted to the lessee. A lease incentive is equivalent to a rebate or discount and includes assumption of a lessee's preexisting lease obligations to a third party, other reimbursements of lessee costs, rent holidays, and reductions of interest or principal charges by the lessor.

Lease term is the period during which a lessee has a noncancelable right to use an underlying asset (referred to as the noncancelable period), plus the following periods, if applicable:

a. 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.

b. 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.

c. 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.

d. 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.

For purposes of this policy, a lessee refers to an entity that leases a nonfinancial asset from another entity. A lessor refers to an entity that leases a nonfinancial asset to another entity.

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. 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.

Underlying asset – another entity's nonfinancial asset.

A lease agreement is classified as a capital lease (in-substance purchase) when substantially all the risks and benefits of ownership are assumed by the lessee.
A **capital lease** is a lease that meets any one of the following conditions in (a) through (d) and meets the condition in (e):

a. Ownership of the leased property transfers to the agency at the end of the lease.
b. The lease contains a **bargain purchase option**.
c. The lease term is 75% or more of the estimated useful life of the leased property.
d. The present value of the minimum future lease payments at the inception of the lease, excluding **executory costs**, is 90% or more of the fair value of the leased property.
e. In addition to one of the items above, the lease must be noncancellable.

A **bargain purchase option** is a provision in the lease agreement that allows the lessee to buy the leased property sometime during the term of the lease at a price considerably lower than the estimated fair value of the asset at the date the option becomes exercisable.

The lessee's **incremental borrowing rate** is the estimated interest rate the lessee would have had to pay if the lessee purchased the leased property and financed it over the period covered by the lease.

The lessor's **implicit borrowing rate** is the discounted interest rate that, when applied to the minimum future lease payments less executory costs of the lease and the unguaranteed residual value of the asset, causes the aggregate present value of the leased property to be equal to the fair value of the property to the lessor.

Click here for other definitions.

**EXCLUSIONS AND SPECIAL SITUATIONS**

This policy does not apply to:

a. Leases of intangible assets, including rights to explore for or to exploit natural resources such as oil, gas, and minerals and similar nonregenerative resources; licensing contracts for items such as motion picture films, video recordings, plays, manuscripts, patents, and copyrights; and licensing contracts for computer software. In sublease transactions, however, this policy does apply to the intangible right-to-use assets that are created by the original leases of tangible underlying assets.
b. Leases of biological assets, including timber, living plants, and living animals.
c. Leases of inventory.
d. Contracts that meet the definition of a service concession arrangement.
e. 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.
f. Supply contracts, such as power purchase agreements.

**POLICY**

101. Agency management is responsible to ensure proper accounting and reporting of capital leases.

101. Agency management must determine whether any of the agency’s contracts meet the definition of a lease and/or contain an embedded lease (e.g., a services contract that includes the lease of an underlying asset), apply the criteria above to determine if the transaction is a capital lease or an operating lease.
103. At lease commencement, a lessee should recognize a lease liability and an intangible right to use lease asset for leases in which the discounted present value of the minimum future lease payments exceed the state’s capitalization threshold of $5,000. This provision does not apply to short-term leases or contracts that transfer ownership (as described in paragraph 106).

Note: Recognize lease payments on contracts below the statewide capitalization threshold of $5,000 as outflows of resources (e.g. expense) based on the payment provisions of the lease contract.

104. At lease commencement, a lessor should recognize a lease receivable and deferred inflows of resources for leases in which the discounted present value of the minimum future lease payments exceed $250,000. This provision does not apply to short-term leases, contracts that transfer ownership (as described in paragraph 106), or leases of assets that are investments (as described in paragraph 132).

Note: Recognize lease payments on contracts below the statewide lease receivable threshold of $250,000 as inflows of resources (e.g. revenue) based on the payment provisions of the lease contract.

PROCEDURE

105. Leases that exceed the statewide capitalization threshold or the statewide lease receivable threshold are reportable regardless of the remaining balance of the lease. For example, at lease commencement, a lessor calculates the discounted present value of the minimum future lease payments as $275,000; at the end of year three, the balance remaining on the lease is $210,000. The lessor should continue to recognize a lease receivable and deferred inflows of resources until 1) the end of the lease or 2) the lease qualifies for remeasurement and the amended value of the lease is less than $250,000.

106. A contract that (a) transfers ownership of the underlying asset to the lessee by the end of the contract and (b) 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.

Lease term

107. Periods for which both the lessee and the lessor have an option to terminate the lease without permission from the other party (or if both parties have to agree to extend) are cancelable periods and are excluded from the lease term. For example, a rolling month-to-month lease, or a lease that continues into a holdover period until a new lease contract is signed, would not be enforceable if both the lessee and the lessor have an option to terminate and, therefore, either could cancel the lease at any time.

108. Provisions that allow for termination of a lease due to (1) purchase of the underlying asset, (2) payment of all sums due, or (3) default on payments, are not considered termination options.

109. A fiscal funding or cancellation clause allows governmental lessees to cancel a lease if the government does not appropriate funds for the lease payments. This type of clause should affect the lease term only if it is reasonably certain that the clause will be exercised.

110. At the commencement of the lease term, the lessee and the lessor should assess all factors relevant to the likelihood that the lessee or the lessor will exercise options to extend or terminate, whether these factors are contract based, underlying asset based, market based, or
government specific. The assessment often will require the consideration of a combination of these interrelated factors. Examples of factors to consider include, but are not limited to, the following:

a. A significant economic incentive, such as contractual terms and conditions for the optional periods that are favorable compared with current market rates.
b. A significant economic disincentive, such as costs to terminate the lease and sign a new lease (e.g., negotiation costs, relocation costs, abandonment of significant leasehold improvements, costs of identifying another suitable underlying asset, costs associated with returning the underlying asset in a contractually specified condition or to a contractually specified location, or a substantial cancellation penalty).
c. The history of exercising options to extend or terminate.
d. The extent to which the asset underlying the lease is essential to the provision of government services.

111. Lessees and lessors should reassess the lease term only if one or more of the following occur:

a. The lessee or lessor elects to exercise an option even though it was previously determined that it was reasonably certain that the lessee or lessor would not exercise that option.
b. The lessee or lessor elects not to exercise an option even though it was previously determined that it was reasonably certain that the lessee or lessor would exercise that option.
c. An event specified in the lease contract that requires an extension or termination of the lease takes place.

112. A lessee should recognize short-term lease payments as outflows of resources (e.g., expense) based on the payment provisions of the lease contract. The lessee should recognize an asset if payments are made in advance or a liability for rent due if payments are to be made subsequent to the reporting period. The lessee should not recognize an outflow of resources during any rent holiday period (e.g., one or more months free).

113. A lessor should recognize short-term lease payments as inflows of resources (e.g., revenue) based on the payment provisions of the lease contract. The lessor should recognize a liability if payments are received in advance or an asset for rent due if payments are to be received subsequent to the reporting period. The lessor should not recognize an inflow of resources during any rent holiday period (e.g., one or more months free).

Lessee recognition and measurement

Lease liability

103. The state's capitalization threshold is $5,000. Capitalize only leases for which the present value of the minimum future lease payments is at least $5,000. Record the capital leased asset in general ledger (GL) account 0863, Capital Leased Property.

For leases meeting the criteria in a. and b. above, record the liability for future lease payments in GL account 1715, Lease-purchase Contracts Payable. For leases meeting the criteria in c. and d. above, record the liability for future lease payments in GL account 1716, Obligations Under Capital Lease.
114. A lessee initially should measure the lease liability at the present value of payments expected to be made during the lease term. Measurement of the lease liability should include the following, if required by a lease:

   a. Fixed payments.
   b. Variable payments that depend on an index or a rate (such as the Consumer Price Index or a market interest rate), initially measured using the index or rate as of the commencement of the lease term.
   c. Variable payments that are fixed in substance (refer to paragraph 116).
   d. Amounts that are reasonably certain of being required to be paid by the lessee under residual value guarantees.
   e. The exercise price of a purchase option if it is reasonably certain that the lessee will exercise that option.
   f. Payments for penalties for terminating the lease, if the lease term reflects the lessee exercising (1) an option to terminate the lease or (2) a fiscal funding or cancellation clause.
   g. Any lease incentives receivable from the lessor (refer to paragraph 147).
   h. Any other payments that are reasonably certain of being required based on an assessment of all relevant factors.

115. Recognize a lease liability in GL account 1716, Lease Obligations-Noncurrent. Refer to Exhibit C – Lease Accounting Entries for Lessees.

116. Variable payments based on future performance of the lessee or usage of the underlying asset should not be included in the measurement of the lease liability. Rather, those variable payments should be recognized as expenses in the period in which the obligation for those payments is incurred. However, any component of those variable payments that is fixed in substance should be included in the measurement of the lease liability.

117. The future lease payments should be discounted using the interest rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the interest rate cannot be readily determined by the lessee, the lessee’s estimated incremental borrowing rate (an estimate of the interest rate that would be charged for borrowing the lease payment amounts during the lease term) should be used.

   a. When agencies are unable to determine the interest rate charged by the lessor, they should consider their agency’s recently issued debt, whether general obligation bond, revenue bond, or certificate of participation, to determine if one of those issuances would provide an incremental borrowing rate. If one is not available or is not suitable for the lease arrangement, agencies shall rely upon the Oregon Bond Index (https://www.oregon.gov/treasury/oregon-bonds/Documents/Public-Financial-Services-MDAC/undated/Bond-Index.pdf), State of Oregon columns, and select the rate that most closely matches the effective date and lease term.

118. In subsequent financial reporting periods, the lessee should calculate the amortization of the discount on the lease liability and report that amount as an outflow of resources (e.g. interest expense) for the period. Any payments made should be allocated first to the accrued interest liability and then to the lease liability.

119. The lessee should remeasure the lease liability at subsequent financial reporting dates if one or more of the following changes have occurred at or before that financial reporting date, based on the most recent lease contract before the changes, and the changes individually or in the
aggregate are expected to significantly affect the amount of the lease liability since the previous measurement:

a. There is a change in the lease term.
b. An assessment of all relevant factors indicates that the likelihood of a residual value guarantee being paid has changed from reasonably certain to not reasonably certain, or vice versa.
c. An assessment of all relevant factors indicates that the likelihood of a purchase option being exercised has changed from reasonably certain to not reasonably certain, or vice versa.
d. There is a change in the estimated amounts for payments already included in the measurement of the lease liability (except as provided in paragraph 120).
e. There is a change in the interest rate the lessor charges the lessee, if used as the initial discount rate.
f. A contingency, upon which some or all of the variable payments that will be made over the remainder of the lease term are based, is resolved such that those payments now meet the criteria for measuring the lease liability under paragraph 114. For example, an event occurs that causes variable payments that were contingent on the performance or use of the underlying asset to become fixed payments for the remainder of the lease term.

120. If a lease liability is remeasured for any of the changes in paragraph 119, the liability also should be adjusted for any change in an index or rate used to determine variable payments if that change in the index or rate is expected to significantly affect the amount of the liability since the previous measurement. A lease liability is not required to be remeasured solely for a change in an index or rate used to determine variable payments.

121. If a lease liability is remeasured for any of the changes in paragraph 119, the lessee also should update the discount rate as part of the remeasurement if one or both of the following changes have occurred and the changes individually or in the aggregate are expected to significantly affect the amount of the lease liability:

a. There is a change in the lease term.
b. An assessment of all relevant factors indicates that the likelihood of a purchase option being exercised has changed from reasonably certain to not reasonably certain, or vice versa.

122. A lease liability is not required to be remeasured, nor is the discount rate required to be reassessed, solely for a change in the lessee’s incremental borrowing rate.

123. If the discount rate is required to be updated based on the provisions in paragraph 121, the discount rate should be based on the revised interest rate the lessor charges the lessee at the time the discount rate is updated. If that interest rate cannot be readily determined, the lessee’s estimated incremental borrowing rate at the time the discount rate is updated should be used (refer to paragraph 117a).

*Lease Asset*

124. A lessee initially should measure the lease asset as the sum of the following:

a. The amount of the initial measurement of the lease liability (refer to paragraph 114).
b. Lease payments made to the lessor at or before the commencement of the lease term, less any lease incentives (refer to paragraph 147) received from the lessor at or before the commencement of the lease term.
c. Initial direct costs that are ancillary charges necessary to place the lease asset into service. Any initial direct costs that would be considered debt issuance costs under paragraph 12 of Statement No. 7, *Advance Refundings Resulting in Defeasance of Debt*, should be recognized as outflows of resources (e.g. expense) in the period in which they are incurred.

125. Recognize the lease asset in one of the following general ledger (GL) accounts:

- GL 0821, Leased Equipment and Machinery
- GL 0822, Leased Motor Vehicles
- GL 0823, Leased Data Processing Hardware
- GL 0824, Leased Tunnels and Bridges
- GL 0825, Leased Airports
- GL 0826, Leased Docks, Dikes, and Dams
- GL 0827, Leased Land
- GL 0828, Leased Buildings
- GL 0829, Leased Other Assets

Refer to Exhibit C – Lease Accounting Entries for Lessees.

126. A lease asset should be amortized in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset, except as provided in paragraph 127. The amortization of the lease asset should be reported as an outflow of resources (e.g. amortization expense). Refer to OAM 15.60.20, *Capital Assets-Depreciation and Amortization* for additional guidance.

127. If a lease contains a purchase option that the lessee has determined is reasonably certain of being exercised, the lease asset should be amortized over the useful life of the underlying asset. In that circumstance, if the underlying asset is nondepreciable, such as land, the lease asset should not be amortized.

128. A lease asset generally should be adjusted by the same amount as the corresponding lease liability when that liability is remeasured based on paragraphs 119-123. However, if that change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the resource flows statement (e.g. gain).

104.129. The presence of impairment indicators (described in OAM 15.60.25) with respect to the underlying asset may result in a change in the manner or duration of use of the lessee’s right to use asset. Such a change in the manner or duration of use of the lessee’s right to use asset may indicate that the service utility of that lease asset is impaired. The length of time during which the lessee cannot use the underlying asset, or is limited to using it in a different manner, should be compared to its previously expected manner and duration of use to determine whether there is a significant decline in service utility of the lease asset. If a lease asset is impaired, the amount reported for the lease asset should be reduced first for any change in the corresponding lease liability. Any remaining amount should be recognized as an impairment.

105. Record capital leases at an amount equal to the present value of the minimum future lease payments, however the amount must not exceed the fair value of the leased property.

106. If an agency leases property and accounts for it in a proprietary fund or fiduciary fund, they account for the capital lease within the
accounts of that fund. If an agency leases property for general government purposes (using resources from governmental funds), they account for the capital lease in the government-wide reporting fund. Record payments to reduce the liability in the governmental fund that originated the liability. Do not use a debt service fund to record payments on this type of liability unless legally mandated through an appropriation. Refer to Exhibit C – Lease Accounting Entries for Lessees.

130. An expenditure and other financing source should be reported in the period the lease is initially recognized. The expenditure and other financing source should be measured as provided in paragraphs 114-117. Subsequent governmental fund lease payments should be accounted for consistent with principles for debt service payments on long-term debt. Refer to Exhibit C – Lease Accounting Entries for Lessees.

131. Depreciate lease-purchase contracts payable (GL 1715) over the estimated useful life of the asset. Depreciate obligations under capital lease (GL 1716) over the length of the lease. Refer to OAM 15 60 20 on Depreciation and Amortization of capital assets for guidance on depreciation.

Lessor recognition and measurement

132. Leases of Assets That Are Investments - If the underlying asset in a lease meets the requirements to be reported as an investment measured at fair value, the lessor should not apply the recognition and measurement provisions of this policy. The lessor should disclose the information in paragraph 186d of this policy but is not required to make the other disclosures in paragraph 186.

Certain regulated leases

133. Certain leases 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. Lessors should not apply the provisions in paragraphs 135-146 and 186 of this policy to leases that meet the provisions of paragraph 134.

134. Lessors should recognize inflows of resources (e.g. revenue) based on the payment provisions of the lease contract and provide the disclosures in paragraph 189 for leases for which external laws, regulations, or legal rulings establish all of the following requirements:

a. Lease rates cannot exceed a reasonable amount, with reasonableness being subject to determination by an external regulator.

b. Lease rates should be similar for lessees that are similarly situated.

c. The lessor cannot deny potential lessees the right to enter into leases if facilities are available, provided that the lessee’s use of the facilities complies with generally applicable use restrictions.

Lease receivable

135. A lessor initially should 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. Measurement of the lease receivable should include the following, if required by a lease:
a. Fixed payments.
b. Variable payments that depend on an index or a rate (such as the Consumer Price Index or a market interest rate), initially measured using the index or rate as of the commencement of the lease term.
c. Variable payments that are fixed in substance (as discussed in paragraph 136).
d. Residual value guarantee payments that are fixed in substance (as discussed in paragraph 137).
e. Any lease incentives (as discussed in paragraph 147) payable to the lessee.

136. Variable payments based on future performance of the lessee or usage of the underlying asset should not be included in the measurement of the lease receivable. Rather, those variable payments should be recognized as inflows of resources (e.g. revenue) in the period to which those payments relate. However, any component of those variable payments that is fixed in substance should be included in the measurement of the lease receivable.

137. Amounts to be received under residual value guarantees (that are not fixed in substance) should be recognized as a receivable and an inflow of resources if (a) a guarantee payment is required (as agreed to by the lessee and lessor) and (b) the amount can be reasonably estimated. Amounts to be received for the exercise price of a purchase option or penalty for lease termination should be recognized as a receivable and an inflow of resources (e.g. revenue) when those options are exercised.

138. The future lease payments to be received should be discounted using the interest rate the lessor charges the lessee, which may be the interest rate implicit in the lease.

139. In subsequent financial reporting periods, the lessor should calculate the amortization of the discount on the lease receivable and report that amount as an inflow of resources (e.g. interest revenue) for the period. Any payments received should be allocated first to the accrued interest receivable and then to the lease receivable.

140. The lessor should remeasure the lease receivable at subsequent financial reporting dates if one or more of the following changes have occurred at or before that financial reporting date, based on the most recent lease contract before the changes, and the changes individually or in the aggregate are expected to significantly affect the amount of the lease receivable since the previous measurement:
   a. There is a change in the lease term.
   b. There is a change in the interest rate the lessor charges the lessee.
   c. A contingency, upon which some or all of the variable payments that will be received over the remainder of the lease term are based, is resolved such that those payments now meet the criteria for measuring the lease receivable under paragraph 135. For example, an event occurs that results in variable payments that were contingent on the performance or use of the underlying asset becoming fixed payments for the remainder of the lease term.

141. If a lease receivable is remeasured for any of the changes in paragraph 140, the receivable also should be adjusted for any change in an index or rate used to determine variable payments if that change in the index or rate is expected to significantly affect the amount of the receivable since the previous measurement. A lease receivable is not required to be remeasured solely for a change in an index or rate used to determine variable payments.
142. The **lessor** also should update the discount rate as part of the remeasurement if one or both of the following changes have occurred and the changes individually or in the aggregate are expected to significantly affect the amount of the **lease** receivable:
   
   a. There is a change in the **lease term**.
   b. There is a change in the interest rate the lessor charges the **lessee**.

143. If the discount rate is updated based on the provisions in paragraph 142, the receivable should be remeasured using the revised discount rate.

**Deferred Inflow of Resources**

144. A **lessor** initially should measure the deferred inflow of resources as follows:
   
   a. The amount of the initial measurement of the **lease** receivable.
   b. Lease payments received from the **lessee** at or before the commencement of the **lease** term that relate to future periods (e.g. the final month's rent), less any **lease incentives** (refer to paragraph 147) paid to, or on behalf of, the **lessee** at or before the commencement of the **lease** term.

145. A **lessor** subsequently should recognize the deferred inflow of resources as inflows of resources (e.g. revenue) in a systematic and rational manner over the **term** of the **lease**. The deferred inflow of resources generally should be adjusted by the same amount as any change resulting from the remeasurement of the **lease** receivable.

**Underlying Asset**

A **lessor** should not derecognize the **asset underlying** the **lease**. A lessor should continue to apply other applicable guidance to the underlying asset, including depreciation and impairment. However, if the lease contract requires the **lessee** to return the asset in its original or enhanced condition, a lessor should not depreciate the asset during the **lease term**.

146. **Lease Incentives**

147. **Lease incentives** reduce the amount that a **lessee** is required to pay for a **lease**. Lease incentives that provide payments to, or on behalf of, a lessee at or before the commencement of a **lease term** are included in initial measurement by directly reducing the amount of the **lease** asset. Lease incentive payments to be provided after the commencement of the **lease** term should be accounted for by lessees and lessors as reductions of lease payments for the periods in which the incentive payments will be provided. Those payments should be measured by lessees consistently with the lessee’s lease liability and by **lessors** consistently with the lessor’s **lease** receivable. Accordingly, lease incentive payments to be provided after the commencement of the **lease** term are included in initial measurement and any remeasurement if they are fixed or fixed in substance, whereas variable or contingent lease incentive payments are not included in initial measurement.

**Contracts with Multiple Components**

148. **Lessees** and **lessors** may enter into contracts that contain multiple components, such as a contract that contains both a **lease** component and a nonlease component, or a lease that contains multiple **underlying assets**.
149. If a lessee or lessor enters into a contract that contains both a lease component (such as the right to use a building) and a nonlease component (such as maintenance services for the building), the government should account for the lease and nonlease components as separate contracts unless the contract meets the exception in paragraph 152.

150. If a lease involves multiple underlying assets and the assets have different lease terms, the lessee and the lessor should account for each underlying asset as a separate lease component. In addition, the lessee should account for each underlying asset as a separate lease component if the underlying assets are in different major classes of assets for disclosure purposes under paragraph 182c. The provisions of this paragraph should be applied unless the contract meets the exception in paragraph 152.

151. To allocate the contract price to the different components, lessees and lessors first should use any prices for individual components that are included in the contract, as long as the price allocation does not appear to be unreasonable based on the terms of the contract and professional judgment, maximizing the use of observable information (e.g. using readily available observable stand-alone prices). Stand-alone prices are those that would be paid or received if the same or similar assets were leased individually or if the same or similar nonlease components (such as services) were contracted individually. Some contracts provide discounts for bundling multiple leases or lease and nonlease components together in one contract. Those discounts may be taken into account when determining whether individual component prices do not appear to be unreasonable. For example, if the individual component prices are each discounted by the same percentage from normal market prices, the discount included in those component prices would not appear to be unreasonable.

152. If a contract does not include prices for individual components, or if any of those prices appear to be unreasonable as provided in paragraph 151, lessees and lessors should use professional judgment to determine their best estimate for allocating the contract price to those components, maximizing the use of observable information. If it is not practicable to determine a best estimate for price allocation for some or all components in the contract, a government should account for those components as a single lease unit.

153. If multiple components are accounted for as a single lease unit as provided for in paragraph 152, the accounting for that unit should be based on the primary lease component within that unit. For example, the primary lease component’s lease term should be used for the unit if the lease components have different lease terms.

Contract Combinations

154. Contracts that are entered into at or near the same time with the same counterparty should be considered part of the same contract if either of the following criteria is met:

   a. The contracts are negotiated as a package with a single objective.
   b. The amount of consideration to be paid in one contract depends on the price or performance of the other contract.

155. If multiple contracts are determined to be part of the same contract, that contract should be evaluated in accordance with the guidance for contracts with multiple components in paragraphs 148-153.

Lease Modifications and Terminations
156. The provisions of a **lease** contract may be amended while the contract is in effect. Amendments modify the provisions of the lease contract. Examples of amendments to lease contracts include changing the contract price, lengthening or shortening the **lease term**, and adding or removing an **underlying asset**. An amendment should be considered a lease modification unless the **lessee’s** right to use the underlying asset decreases, in which case the amendment should be considered a partial or full lease termination. By contrast, exercising an existing option, such as an option to extend or terminate the lease, is subject to the guidance for remeasurement.

**Lease Modifications**

157. The **lessee** and **lessor** should account for an amendment during the reporting period resulting in a modification to a **lease** contract as a separate lease (that is, separate from the most recent lease contract before the modification) if both of the following conditions are present:

a. The lease modification gives the lessee an additional lease asset by adding one or more **underlying assets** that were not included in the original lease contract.

b. The increase in lease payments for the additional lease asset does not appear to be unreasonable based on (1) the terms of the amended lease contract and (2) professional judgment, maximizing the use of observable information (e.g. using readily available observable stand-alone prices).

**Lessees**

158. Unless a modification is reported as a separate **lease** as provided in paragraph 157, a **lessee** should account for a lease modification by remeasuring the lease liability. The lease asset should be adjusted by the difference between the remeasured liability and the liability immediately before the lease modification. However, if the change reduces the carrying value of the lease asset to zero, any remaining amount should be reported in the resource flows statement (e.g. a gain).

159. If prior to the expiration of the **lease term** a change to the provisions of a **lease** results from a debt refunding by the **lessor**, including an advance refunding, in which the perceived economic advantages of the refunding are passed through to the **lessee**, the change should be accounted for as follows:

a. If a change to the provisions of a lease results from a debt refunding by the lessor, including an advance refunding that results in a defeasance of debt, the lessee should adjust the lease liability to the present value of the future lease payments under the revised lease using the effective interest rate applicable to the revised lease contract. The resulting difference should be reported as a deferred outflow of resources or a deferred inflow of resources. The deferred outflow of resources or the deferred inflow of resources should be recognized as an adjustment to an outflow of resources (e.g. as an increase or decrease to interest expense) in a systematic and rational manner over the remaining life of the old debt or the life of the new debt, whichever is shorter.

b. If (1) the provisions of a lease are changed in connection with an advance refunding by the lessor that results in a defeasance of debt and (2) the lessee is obligated to reimburse the lessor for any costs related to the refunded debt that have been or will be incurred (such as an unamortized discount or a call premium), the lessee should recognize those costs in a systematic and rational manner over the remaining life of the old debt or the life of the new debt, whichever is shorter.

**Lessors**
160. Unless a modification is reported as a separate lease as provided in paragraph 157, a lessor should account for a lease modification by remeasuring the lease receivable. The deferred inflow of resources should be adjusted by the difference between the remeasured receivable and the receivable immediately before the lease modification. However, to the extent that the change relates to payments for the current period, the change should be recognized as an inflow of resources (e.g. revenue) or an outflow of resources (e.g. expense) for the current period.

161. If prior to the expiration of the lease term a change to the provisions of a lease results from a debt refunding by the lessor, including an advance refunding, in which the perceived economic advantages of the refunding are passed through to the lessee, the change should be accounted for as follows:

   a. If a change to the provisions of a lease results from a debt refunding by the lessor, including an advance refunding that results in a defeasance of debt, the lessor should adjust the lease receivable to the present value of the future lease payments based on the interest rate applicable to the revised lease contract and also should adjust the deferred inflows of resources. The adjustment to the deferred inflow of resources should be recognized as inflows of resources or outflows of resources (for example, gain or loss) over the remaining life of the old debt or the life of the new debt, whichever is shorter.

   b. If a change to the provisions of a lease results from an advance refunding that results in a defeasance of debt, the lessor also should systematically recognize, as inflows of resources (e.g. revenue), any reimbursements to be received from the lessee for costs related to the refunded debt (such as an unamortized discount or a call premium) over the remaining life of the old debt or the life of the new debt, whichever is shorter.

Lease Terminations

162. The lessee and lessor should account for an amendment during the reporting period resulting in a decrease in the lessee’s right to use the underlying asset (e.g. the lease term is shortened or the number of underlying assets is reduced) as a partial or full lease termination.

Lessees

163. A lessee generally should account for the partial or full lease termination by reducing the carrying values of the lease asset and lease liability, and recognizing a gain or loss for the difference. However, if the lease is terminated as a result of the lessee purchasing an underlying asset from the lessor, the lease asset should be reclassified to the appropriate class of owned asset.

Lessors

164. A lessor should account for the partial or full lease termination by reducing the carrying values of the lease receivable and related deferred inflow of resources, and recognizing a gain or loss for the difference. However, if the lease is terminated as a result of the lessee purchasing an underlying asset from the lessor, the carrying value of the underlying asset should be derecognized and included in the calculation of any resulting gain or loss.

Subleases

165. A sublease involves three parties: the original lessor, the original lessee (who also is the lessor in the sublease), and the new lessee. The original lessor should continue to apply the general
lessor guidance. The government that is the original lessee and becomes the lessor in the sublease should account for the original lease and the sublease as two separate transactions, as a lessee and a lessor, respectively. Those two separate transactions should not be offset against one another. The new lessee should apply the general lessee guidance.

166. The original lessee (now the lessor in the sublease) should include the sublease in its disclosure of the general description of lease arrangements. Its lessor transactions related to subleases should be disclosed separately from its lessee transactions related to original leases.

Sale-Leaseback Transactions

167. Sale-leaseback transactions involve the sale of an underlying asset by the owner and a lease of the property back to the seller (original owner). A sale-leaseback should include a transaction that qualifies as a sale (refer to GASB Statement No. 62, paragraphs 287-319 and 321-323) to be eligible for sale-leaseback accounting. A sale-leaseback transaction that does not include a qualifying sale should be accounted for as a borrowing activity by the seller-lessee and a lending activity by the buyer-lessor.

168. The sale and lease portions of a sale-leaseback transaction should be accounted for in financial statements prepared using the economic resources measurement focus as two separate transactions—a sale transaction and a lease transaction—except that the difference between the carrying value of the capital asset that was sold and the net proceeds from the sale should be reported as a deferred inflow of resources or a deferred outflow of resources and subsequently recognized in the resource flows statements in a systematic and rational manner over the term of the lease. However, if the lease portion of the transaction qualifies as a short-term lease, any difference between the carrying value of the capital asset that was sold and the net proceeds from the sale should be recognized immediately.

169. A sale-leaseback transaction is considered to have off-market terms if there is a significant difference between (a) the sale price and the estimated fair value of the asset or (b) the present value of the contractual lease payments and the estimated present value of what the lease payments for that asset would be at the market price, whichever of the two differences is more readily determinable. That difference should be reported based on the substance of the transaction (e.g. as a borrowing, a nonexchange transaction, or an advance lease payment) rather than as part of the sale-leaseback transaction.

170. A seller-lessee should disclose the terms and conditions of sale-leaseback transactions in addition to the disclosures required of a lessee in paragraph 182. A buyer-lessor should provide the disclosures required of a lessor in paragraph 186.

171. For entities that elect to apply the regulated operations guidance of GASB Statement No. 62, and that meet the criteria in paragraphs 476–500 of that Statement, as amended, the difference between (a) the amount of inflows of resources or outflows of resources (e.g. revenue or expense) recognized for a transaction that is accounted for as a sale-leaseback and (b) the amount of inflows of resources or outflows of resources included in allowable cost for rate-making purposes should be recognized as a separate regulatory-created asset or regulatory-created deferred inflow of resources, as appropriate.

Lease-Leaseback Transactions

172. In a lease-leaseback transaction, an asset is leased by one party (first party) to another party and then leased back to the first party. The leaseback may involve an additional asset (such as leasing a school building that has been constructed by a developer on land owned by and
leased back to a school district) or only a portion of the original asset (such as leasing back only one floor of a building to the owner). A lease-leaseback transaction should be accounted for as a net transaction. Both parties to a lease-leaseback transaction should disclose the amounts of the lease and the leaseback separately in the notes to financial statements.

Intra-Entity Leases

173. When the lessee or lessor is included as a blended component unit of the primary government, the reporting requirements of this policy do not apply. Instead, when the lessor is a blended component unit, the debt and assets of the lessor should be reported as if they were the primary government’s debt and assets. For example, the capital assets leased from a blended component unit would be reported as capital assets, and related debt would be reported as a long-term liability in the reporting entity’s government-wide financial statements. The debt service activity of the lessor would be reported as a debt service activity of the reporting entity. With respect to leases with or between blended component units, for which eliminations are required, these eliminations should be made before the financial statements of the blended component units are aggregated with those of the primary government. The remaining cash payments between component units should be reported as inflows of resources and outflows of resources.

174. Lease arrangements between the primary government and discretely presented component units (or between discretely presented component units) should be treated in the same manner as any other lease under the provisions of this policy. However, related receivables and payables should not be combined with other amounts due to or due from discretely presented component units or with lease receivables and payables with organizations outside the reporting entity.

Leases between Related Parties

175. In the separate financial statements of the related parties, the classification and accounting should be the same as for similar leases between unrelated parties, except in cases in which it is clear that the terms of the transaction have been significantly affected by the fact that the lessee and lessor are related. In such cases, the classification and accounting should be modified as necessary to recognize the substance of the transaction rather than merely its legal form. For example, if the lease contract is structured to meet the definition of a short-term lease but the related parties have a mutual understanding that the lease contract will stay in effect for several more years, that lease should not be accounted for as a short-term lease. The nature and extent of leasing transactions with related parties should be disclosed.

176. In financial statements for which an interest in an investee is accounted for using the equity method, any inflow of resources or outflow of resources (e.g. gain or loss) on a leasing transaction with the related party should be accounted for in accordance with the investment in common stock principles set forth in GASB Statement No. 62, paragraphs 202–210 the equity interests in common stock principles set forth in GASB Statement No. 72, paragraph 77.

PROCEDURE:

Examination of Capital Lease Criteria
108. For each lease agreement entered into, consider the criteria for capital leases to determine whether to classify the lease as a capital lease.

a. Transfer of ownership should be apparent in the terms of the lease.

b. Bargain purchase option. Use professional judgment in determining whether the purchase option price will be a bargain price at the option date. The difference between the option price and the expected fair value must be large enough to make exercise of the option reasonably assured. If there is reasonable assurance at the start of the lease that the agency will exercise the purchase option, or it is the agency's intention at the start of the lease to exercise the purchase option, consider the option a bargain purchase option.

c. Lease term at least 75% of useful life. The lease term is normally the fixed, noncancellable term of the lease. The lease term is at least 75% of the estimated economic life of the leased asset if, for example, an agency has a lease contract for a motor vehicle that extends for 48 months and the agency estimates the useful life of the vehicle at 60 months. In this case, the term of the lease runs for 80% of the normal life of the asset, meeting the criteria. If the term of the lease had been less than 45 months, the lease would not have qualified under this criterion since 45 months is 75% of the useful life of the asset.

In addition, if the beginning of a lease term falls within the last 25% of the total estimated useful life of the leased asset, including earlier years of use, consider the lease an operating lease.

d. Lease payments at least 90% of fair value of leased asset. Lease payments include minimum rental payments based on the term of the lease and exclude executory costs such as payments for insurance, maintenance and taxes. The lease payments include any residual value guaranteed by the lessee at the end of the term of the lease as well as any penalties that the lessee must pay for failure to renew or extend the lease. If the lease contains a bargain purchase option, the lease payments include only the minimum future lease payments over the term of the lease and the bargain purchase option.

When determining the present value of lease payments, the lessee uses its incremental borrowing rate. The lessee uses the lessor's implicit interest rate if that rate can be determined and it is less than the lessee's incremental borrowing rate.

The lessee then compares the present value amounts to the fair value of the asset to determine if the present value of minimum future lease payments exceeds 90% of the fair value of the leased asset.

For example, the lessee:

Leases equipment for a 5-year period
Will make 5 annual payments of $50,000
Will make the first payment upon signing the lease on 6/30/X1

Both the lessee's incremental borrowing rate and the lessor's implicit borrowing rate are 10%.
Fair value of the property is $230,000

Annual lease payments $ 50,000
From PV tables: Present value of an annuity due x =
Interest rate 10% and number of periods is 5 = 4.16986
Present value of minimum future lease payments $208,493
Present value of minimum future lease payments $208,493
Divided by fair value of the property $230,000
Percentage of fair value 90.65%

Capitalize the lease at $208,493 and report interest per the following schedule:

<table>
<thead>
<tr>
<th>Date</th>
<th>Lease Payment</th>
<th>Interest @ 10%</th>
<th>principal liability</th>
<th>remaining liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>6/30/X1</td>
<td></td>
<td>1</td>
<td></td>
<td>208,493</td>
</tr>
<tr>
<td>6/30/X2</td>
<td>50,000</td>
<td>5,000</td>
<td>45,000</td>
<td>158,493</td>
</tr>
<tr>
<td>6/30/X3</td>
<td>50,000</td>
<td>5,000</td>
<td>45,000</td>
<td>124,342</td>
</tr>
<tr>
<td>6/30/X4</td>
<td>50,000</td>
<td>5,000</td>
<td>45,000</td>
<td>86,777</td>
</tr>
<tr>
<td>6/30/X5</td>
<td>50,000</td>
<td>5,000</td>
<td>45,000</td>
<td>(0)</td>
</tr>
</tbody>
</table>

109. If the lease does not meet any one of the above criteria in (a) through (d) and the condition in (e), record the lease as an operating lease in the agency’s accounting records. See OAM 15.80.00 on Commitments for more information on operating leases.

Accounting Transactions

110. When a lease meets the criteria of a capital lease, use the following entry to record an asset and liability in either a proprietary fund or the government-wide reporting fund:

T-code 466: Establish asset and liability for capital lease

DR 0863 Capital Leased Property xxx
DR 3074 Change in Capital Assets xxx
CR 3018 Invested in Capital Assets xxx
CR 1715 Lease-Purchases Contracts Payable xxx
or CR 1716 Obligations Under Capital Lease

111. After making payment, reduce the liability for the principal portion of the payment only. Charge the interest portion to comptroller object 7400, Interest-Loans.

T-code 459: Reduce capital lease liability for principal payment only

DR 1715 Lease-Purchases Contracts Payable xxx
or DR 1716 Obligations Under Capital Lease
CR 3600 GAAP Expenditure Offset-Capital Outlay xxx
112. When capital leased property is disposed of, record an entry as follows:

______ **T-code 535**: Disposition of capital leased property

- **DR 0871 Accumulated Amortization-Capital Leased Property** xxx
- **CR 0863 Capital Leased Property** xxx

If the capital leased property has any unamortized balance, make the following entry:

______ **T-code 537**: Remove unamortized balance of capital leased asset

- **DR 3200 GAAP Revenue Offset Gain/(loss) on Disposition** xxx
- **DR 3018 Invested in Capital Assets** xxx
- **CR 0863 Capital Leased Property** xxx
- **CR 3074 Change in Capital Assets** xxx

113. At fiscal year end, reclassify the current portion of the capital lease liability (the principal amount that the agency must pay in the coming fiscal year) out of the noncurrent portion of the liability. For **Lease-Purchase Contracts Payable**, reclassify from GL account 1715 into GL account 1280. For **Obligations Under Capital Lease**, reclassify from GL account 1716 into GL account 1281. This reclassification ensures appropriate reporting of the current and noncurrent portions of the liability on the face of the statement of net assets.

**Financial Statement Reporting**

114. In the year an agency acquires a new lease purchase in governmental funds, SARS reports both capital outlay expenditures and another financing source to properly report leases incurred on the statement of revenues, expenditures, and changes in fund balances, as required by GAAP. SARS obtains the necessary information from agency year-end disclosure forms.

115. For **lease-purchase contracts payable** (GL 1715), agencies report payments on capital leases entered into for general government purposes as capital outlay (for principal amount) and debt service (for interest expenditure) in R*STARS. For governmental fund financial statement reporting, SARS reclassifies the capital outlay expenditures to debt service principal expenditures. This eliminates the expenditures for reporting in the government-wide financial statements. SARS obtains the necessary information from agency year-end disclosure forms.

116. For **obligations under capital lease** (GL 1716), agencies report expenditures for payments on a capital lease entered into for general government purposes as capital outlay expenditures. For governmental fund financial statement reporting, SARS reclassifies the capital outlay expenditures to debt service principal and interest expenditures, as applicable. This eliminates the principal expense for reporting in the government-wide financial statements. SARS obtains the necessary information from agency year-end disclosure forms.

117. The SARS reports **capital leased property assets** as part of Buildings, Property, and Equipment by major asset class within the capital asset section of the proprietary fund statement of net assets position, the statement of fiduciary net assets position, and the government-wide statement of net assets position.
SARS reports lease liability-current and lease liability-noncurrent both lease-purchase contracts payable and obligations under capital lease as part of Obligations Under Capital Lease on the proprietary fund statement of net assets position, the statement of fiduciary net assets position, and the government-wide statement of net assets position.

SARS reports depreciation expense, including that associated with capital leased assets, as a separate line item within operating expenses in the proprietary fund statement of revenues, expenses, and changes in fund net assets position. SARS reports depreciation expense as administrative expense on the statement of changes in fiduciary net assets position. SARS reports depreciation expense in the applicable function/program for governmental or business-type activities in the government-wide statement of activities.

SARS reports accumulated depreciation for capital assets, including that associated with capital leased assets, as a contra account to capital assets on both the proprietary funds statement of net assets position and the government-wide statement of net assets position. SARS nets accumulated depreciation for capital leased assets against Buildings, Property, and Equipment the applicable major asset class in the statement of fiduciary net assets position.

Disclosure Requirements

SARS includes disclosure information for capital leased assets along with disclosure information for all other capital assets as described in OAM 15.60.10.

Lessees

A lessee should disclose the following about its lease activities other than short-term leases:

a. A general description of its leasing arrangements, including (1) the basis, terms, and conditions on which variable payments not included in the measurement of the lease liability are determined and (2) the existence, terms, and conditions of residual value guarantees provided by the lessee not included in the measurement of the lease liability.

b. The total amount of lease assets, and the related accumulated amortization, disclosed separately from other capital assets.

c. The amount of lease assets by major classes of underlying assets, disclosed separately from other capital assets.

d. The amount of outflows of resources recognized in the reporting period for variable payments not previously included in the measurement of the lease liability.

e. The amount of outflows of resources recognized in the reporting period for other payments, such as residual value guarantees or termination penalties, not previously included in the measurement of the lease liability.

f. Principal and interest requirements to maturity, presented separately, for the lease liability for each of the five subsequent fiscal years and in five-year increments thereafter.

g. Commitments under leases before the commencement of the lease term.

h. The components of any loss associated with an impairment (the impairment loss and any related change in the lease liability).

A lessee also should provide relevant disclosures for the following transactions, if applicable:

a. Sublease transactions.

b. Sale-leaseback transactions.

c. Lease-leaseback transactions.

A lessee is not required to disclose collateral pledged as a security for a lease if that collateral is solely the asset underlying the lease.
122. SARS discloses the following information specific to capital leases:

a. a description of the general leasing arrangements
b. the gross amount of assets recorded under capital leases
c. minimum future lease payments for each of the next five fiscal years and for each five year increment thereafter, presenting a deduction for the amount of imputed interest to reduce the net minimum future lease payments to their present value
d. depreciation of leased assets

SARS gathers the detail for this disclosure on agency year-end disclosure forms.

185. SARS gathers the lease disclosure for lessees detail on agency year-end disclosure forms.

Lessors

186. A lessor should disclose the following about its lease activities other than short-term leases and certain regulated leases:

a. A general description of its leasing arrangements, including the basis, terms, and conditions on which any variable payments not included in the measurement of the lease receivable are determined.
b. The total amount of inflows of resources (e.g. lease revenue, interest revenue, and any other lease-related inflows) recognized in the reporting period from leases, if that amount cannot be determined based on the amounts displayed on the face of the financial statements.
c. The amount of inflows of resources recognized in the reporting period for variable and other payments not previously included in the measurement of the lease receivable, including inflows of resources related to residual value guarantees and termination penalties.
d. The existence, terms, and conditions of options by the lessee to terminate the lease or abate payments if the lessor government has issued debt for which the principal and interest payments are secured by the lease payments.

187. A lessor also should provide relevant disclosures for the following transactions, if applicable:

a. Leases of assets that are investments.
b. Certain regulated leases.
c. Sublease transactions.
d. Sale-leaseback transactions.
e. Lease-leaseback transactions.

188. Additionally, if a lessor’s principal ongoing operations consist of leasing assets to other entities, the government should disclose a schedule of future payments that are included in the measurement of the lease receivable, showing principal and interest separately, for each of the five subsequent fiscal years and in five-year increments thereafter.

189. A lessor with one or more regulated leases should disclose the following about those lease activities, other than short-term leases:

a. A general description of its agreements.
b. The extent to which capital assets are subject to preferential or exclusive use by counterparties under agreements, by major class of assets and by major counterparty.
c. The total amount of inflows of resources (e.g. lease revenue, interest revenue, and any other lease-related inflows) recognized in the reporting period from these agreements, if
that amount cannot be determined based on the amounts displayed on the face of the financial statements.

d. A schedule of expected future minimum payments under these agreements for each of the subsequent five years and in five-year increments thereafter.

e. The amount of inflows of resources recognized in the reporting period for variable payments not included in expected future minimum payments.

f. The existence, terms, and conditions of options by the lessee to terminate the lease or abate lease payments if the lessor government has issued debt for which the principal and interest payments are secured by the lease payments.

190. SARS gathers the lease disclosure for lessors detail on agency year-end disclosure forms.
EXHIBIT A – Lease Accounting Decision Tree for Lessees

Is the lease for an asset excluded from the scope of GASB 87?

YES
Record an expense as payments are made.

NO
Will the state own the asset at the end of the lease term?

YES
Follow requirements for reporting financing agreements (OAM 15.65.10).

NO
Does the government have control of the right to use the asset?

YES
Is the maximum lease term greater than 12 months?

NO
Record an expense as payments are made.

YES
Does the lease have any fixed or fixed in-substance lease payments?

NO
Record an expense as payments are made.

YES
Are the lease payments significantly lower than the "market rate"?

NO
Record an expense as payments are made.

YES
Record an expense as payments are made.

NO
Do total lease payments exceed the capitalization threshold of $5,000?

YES
Calculate the lease liability and leased asset.

NO
Record an expense as payments are made.
EXHIBIT B – Lease Accounting Decision Tree for Lessors

Is the lease for an asset excluded from the scope of GASB 87?

YES
Record a revenue as payments are received (OAM 15.35.00).

NO
Does the lessee have control of the right to use the asset?

YES
Is the maximum lease term greater than 12 months?

NO
Record a revenue as payments are received (OAM 15.35.00).

YES
Does the lease have any fixed or fixed in-substance lease payments?

NO
Record a revenue as payments are received (OAM 15.35.00).

YES
Are the lease payments significantly lower than the "market rate"?

NO
Record a revenue as payments are received (OAM 15.35.00).

YES
Do total lease payments exceed the reporting threshold of $250,000?

NO
Record a revenue as payments are received (OAM 15.35.00).

YES
Calculate the lease receivable and deferred inflows.

NO
Record a revenue as payments are received (OAM 15.35.00).
EXHIBIT C – Lease Accounting Entries for Lessees
### Lessee entries at lease commencement

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of Transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>CoB</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Recognize lease proceeds (complete lease purchase-exp)</td>
<td>908R</td>
<td>1551:Deposit Liability</td>
<td>5200:GAAP Revenue Offset</td>
<td>3700</td>
<td>X</td>
</tr>
<tr>
<td>2.</td>
<td>Recognize acquisition of asset (complete lease purchase-exp)</td>
<td>908R</td>
<td>5200:GAAP Expenditure Offset</td>
<td>1551:Deposit Liability</td>
<td>5770</td>
<td>X</td>
</tr>
<tr>
<td>3.</td>
<td>Establish lease liability (eliminate 1700)</td>
<td>402</td>
<td>3200:GAAP Revenue Offset</td>
<td>1710:Lease Oblig</td>
<td>1700</td>
<td>X</td>
</tr>
<tr>
<td>4.</td>
<td>Establish lease asset (eliminate 504X)</td>
<td>154 or 154X-Leased Asset</td>
<td>3600:GAAP Exp. Offset</td>
<td>5770</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(FO) 3074-Change in Cap. Assets</td>
<td>3015-Net Inv. in Cap. Assets</td>
<td>8010-Change in Cap. Assets</td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

### Measurement Focus

- **Economic Resources**: X
- **Financial Resources**: X

### Lessee entries throughout the fiscal year

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of Transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>CoB</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.</td>
<td>Record accumulated amortization of lease</td>
<td>342 or 341</td>
<td>3600:GAAP Exp. Offset</td>
<td>0006-Amort. of Lease</td>
<td>3074-Change in Cap. Assets</td>
<td>7000</td>
</tr>
<tr>
<td></td>
<td>(FO) 3015-Net Inv. in Cap. Assets</td>
<td>3074-Change in Cap. Assets</td>
<td>7003</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td>te.</td>
<td>Record lease payment (principal portion)</td>
<td>222</td>
<td>3500:Expenditure Control Cash</td>
<td>0170-Cash on Deposit w/ OCM</td>
<td>2201</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Record lease payment (interest portion)</td>
<td>222</td>
<td>3500:Expenditure Control Cash</td>
<td>0170-Cash on Deposit w/ OCM</td>
<td>2201</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Record total lease payment</td>
<td>222</td>
<td>3500:Expenditure Control Cash</td>
<td>0170-Cash on Deposit w/ OCM</td>
<td>2201</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Record interest portion of lease payment</td>
<td>406</td>
<td>0170-Cash on Deposit w/ OCM</td>
<td>3500:Expenditure Control Cash</td>
<td>7003</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Record interest portion of lease payment</td>
<td>415</td>
<td>3500:Expenditure Control Cash</td>
<td>0170-Cash on Deposit w/ OCM</td>
<td>2201</td>
<td>X</td>
</tr>
<tr>
<td>7.</td>
<td>Reduce lease liability by principal lease payments</td>
<td>480</td>
<td>1714-Lease Oblig</td>
<td>3600:GAAP Exp. Offset</td>
<td>7000</td>
<td>X</td>
</tr>
</tbody>
</table>

### Lessee entries at fiscal year end

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of Transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>CoB</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>8a.</td>
<td>Reduce current portion of lease liability</td>
<td>473R</td>
<td>1714-Lease Oblig, Noncurrent</td>
<td>2951-System Clearing GL</td>
<td>N/A</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Establish/adjust lease liability-current</td>
<td>476</td>
<td>2051-System Clearing GL</td>
<td>1210-Lease Oblig, Current</td>
<td>N/A</td>
<td>X</td>
</tr>
</tbody>
</table>

### Lessee entries at lease remeasurement or modification

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of Transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>CoB</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>9a.</td>
<td>Recognize lease proceeds</td>
<td>908R</td>
<td>1551:Deposit Liability</td>
<td>5200:GAAP Revenue Offset</td>
<td>3700</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Recognize acquisition of asset</td>
<td>908R</td>
<td>5200:GAAP Expenditure Offset</td>
<td>1551:Deposit Liability</td>
<td>5770</td>
<td>X</td>
</tr>
<tr>
<td>9c.</td>
<td>Adjust lease liability (eliminate amount from 9a)</td>
<td>402</td>
<td>3200:GAAP Revenue Offset</td>
<td>1710:Lease Oblig</td>
<td>1700</td>
<td>X</td>
</tr>
<tr>
<td>9d.</td>
<td>Adjust lease asset (eliminate amount from 9b)</td>
<td>545 or 555</td>
<td>3600:GAAP Exp. Offset</td>
<td>5770</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>10.</td>
<td>Recognize gain/(loss) on leased asset only if the change reduces the carrying value of the leased asset to zero</td>
<td>557 or 558</td>
<td>3200:GAAP Revenue Offset</td>
<td>0006-Leased Asset</td>
<td>2551</td>
<td>X</td>
</tr>
</tbody>
</table>

### Lessee entries at lease termination or at the end of the lease

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of Transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>CoB</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>11a.</td>
<td>Reduce current portion of lease liability to noncurrent lease liability</td>
<td>473R</td>
<td>1210-Lease Oblig, Current</td>
<td>2951-System Clearing GL</td>
<td>N/A</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Adjust lease liability-noncurrent</td>
<td>476</td>
<td>2051-System Clearing GL</td>
<td>1710-Lease Oblig, Noncurrent</td>
<td>N/A</td>
<td>X</td>
</tr>
<tr>
<td>12a.</td>
<td>Eliminate asset asset value, record gain/(loss)</td>
<td>336 or 335</td>
<td>3300:GAAP Revenue Offset</td>
<td>0006-Leased Asset</td>
<td>2251</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Reduce accumulated amortization</td>
<td>573</td>
<td>0006-Leased Asset</td>
<td>3074-Change in Cap. Assets</td>
<td>N/A</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Reduce asset value</td>
<td>574</td>
<td>3200-System Clearing GL, GL</td>
<td>0006-Leased Asset</td>
<td>N/A</td>
<td>X</td>
</tr>
<tr>
<td>15a.</td>
<td>Eliminate lease proceeds</td>
<td>908</td>
<td>3200:GAAP Revenue Offset</td>
<td>1551:Deposit Liability</td>
<td>3700</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Eliminate acquisition of leased asset</td>
<td>900</td>
<td>1551-Leased Liability</td>
<td>3600:GAAP Exp. Offset</td>
<td>5770</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Adjust lease liability (eliminate amount from 11a)</td>
<td>462R</td>
<td>1714-Lease Oblig</td>
<td>3200:GAAP Revenue Offset</td>
<td>1700</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Adjust lease asset (eliminate amount from 11b)</td>
<td>545J or 555J</td>
<td>3600:GAAP Exp. Offset</td>
<td>0006-Leased Asset</td>
<td>5770</td>
<td>X</td>
</tr>
<tr>
<td>Lessee entries at lease commencement</td>
<td>Measurement Focus</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-----------------------------------</td>
<td>------------------</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Step</strong></td>
<td><strong>Description of transaction</strong></td>
<td><strong>T.Code</strong></td>
<td><strong>DR</strong></td>
<td><strong>CR</strong></td>
<td><strong>Cob</strong></td>
<td><strong>Economic Resources</strong></td>
</tr>
<tr>
<td>1.</td>
<td>Recognize lease proceeds (complete lease purchase-roy)</td>
<td>906R</td>
<td>1551-Deposit Liability</td>
<td>3200-GAAP Revenue Offset</td>
<td>1700</td>
<td>X</td>
</tr>
<tr>
<td>2.</td>
<td>Recognize acquisition of asset (complete lease purchase-exp)</td>
<td>906R</td>
<td>3600-GAAP Expenditure Offset</td>
<td>1551-Deposit Liability</td>
<td>5770</td>
<td>X</td>
</tr>
<tr>
<td>3.</td>
<td>Establish lease liability (eliminate 1700)</td>
<td>462</td>
<td>3200-GAAP Revenue Offset</td>
<td>1716-Lease Oblig.</td>
<td>1700</td>
<td>X</td>
</tr>
<tr>
<td>4.</td>
<td>Establish lease asset (eliminate 5770)</td>
<td>545 or 555 08XX-Leased Asset (FID)</td>
<td>3074-Change in Cap. Assets</td>
<td>3600-GAAP Exp. Offset</td>
<td>5770</td>
<td>X</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lessee entries throughout the fiscal year</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Step</strong></td>
<td><strong>Description of transaction</strong></td>
</tr>
<tr>
<td>5.</td>
<td>Record accumulated amortization of lease</td>
</tr>
<tr>
<td>5a.</td>
<td>Record lease payment (principal portion)</td>
</tr>
<tr>
<td>5b.</td>
<td>Record lease payment (interest portion)</td>
</tr>
<tr>
<td>5c.</td>
<td>Record total lease payment</td>
</tr>
<tr>
<td>6b.</td>
<td>Reclassify interest portion of lease payment</td>
</tr>
<tr>
<td>7.</td>
<td>Reduce lease liability by removal lease payments</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lessee entries at fiscal year end</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Step</strong></td>
<td><strong>Description of transaction</strong></td>
</tr>
<tr>
<td>8.</td>
<td>Reclass current portion of lease liability</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lessee entries at lease remeasurement or modification</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Step</strong></td>
<td><strong>Description of transaction</strong></td>
</tr>
<tr>
<td>9.</td>
<td>Recognize lease proceeds</td>
</tr>
<tr>
<td>10.</td>
<td>Recognize gain/(loss) on leased asset only if the change reduces the carrying value of the leased asset to zero.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lessee entries at lease termination or at the end of the lease</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Step</strong></td>
<td><strong>Description of transaction</strong></td>
</tr>
<tr>
<td>11.</td>
<td>Move current portion of lease liability to noncurrent lease liability</td>
</tr>
<tr>
<td>12.</td>
<td>Eliminate excess asset value, record gain/(loss)</td>
</tr>
<tr>
<td>13.</td>
<td>Eliminate lease proceeds</td>
</tr>
<tr>
<td>14.</td>
<td>Eliminate acquisition of leased asset</td>
</tr>
<tr>
<td>15.</td>
<td>Adjust lease liability (eliminate amount from 13a)</td>
</tr>
</tbody>
</table>
EXHIBIT D – Lease Accounting Entries for Lessors

### Lessor entries at lease commencement

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>Cod</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Establish lease receivable-nonnear</td>
<td>486</td>
<td>0841-Lease Receivable-nonnear</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>2.</td>
<td>Establish allowance for uncollectible lease receivable-nonnear</td>
<td>486</td>
<td>0841-Lease Receivable-nonnear</td>
<td>0442-Allow for Doubt. Lease Rec NC</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>3.</td>
<td>Record payments received before lease commencement</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a.</td>
<td>Recognize cash transaction</td>
<td>1500</td>
<td>0070-Cash on Deposit w/o OST</td>
<td>3100-Revenue Control Cash</td>
<td>0667</td>
<td>X X</td>
</tr>
<tr>
<td>b.</td>
<td>Recognize deferred inflow receivable</td>
<td>522</td>
<td>3200-GAAP Revenue Offset</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>0667</td>
<td>X X</td>
</tr>
</tbody>
</table>

### Lessor entries throughout the fiscal year

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>Cod</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>4a.</td>
<td>Record receipt of monthly lease principal payment</td>
<td>486</td>
<td>0070-Cash on Deposit w/o OST</td>
<td>3100-Revenue Control Cash</td>
<td>0667</td>
<td>X X</td>
</tr>
<tr>
<td>4b.</td>
<td>Record receipt of monthly lease interest payment</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Reduce lease receivable by lease payments (principal)</td>
<td>560</td>
<td>3200-GAAP Revenue Offset</td>
<td>0441-Lease Receivable-nonnear</td>
<td>0667</td>
<td>X X</td>
</tr>
<tr>
<td>6.</td>
<td>Record accumulated amortization of deferred inflow</td>
<td>522</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>3200-GAAP Revenue Offset</td>
<td>2347</td>
<td>X X</td>
</tr>
</tbody>
</table>

### Lessor entries at fiscal year end

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>Cod</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>7a.</td>
<td>Reduce lease receivable-nonnear</td>
<td>474</td>
<td>2951-System Clearing GL</td>
<td>0441-Lease Receivable-nonnear</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>7b.</td>
<td>Record payment of lease receivable-nonnear</td>
<td>521</td>
<td>0000-Lease Receivable-nonnear</td>
<td>2951-System Clearing GL</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>8.</td>
<td>Adjust allowance for uncollectible lease receivable-nonnear</td>
<td>498</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>0442-Allow for Doubt. Lease Rec NC</td>
<td>N/A</td>
<td>X X</td>
</tr>
</tbody>
</table>

### Lessor entries at lease remeasurement or modification

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>Cod</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>9.</td>
<td>Adjust lease receivable-nonnear</td>
<td>486</td>
<td>0841-Lease Receivable-nonnear</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>10.</td>
<td>Adjust allowance for uncollectible lease receivable-nonnear</td>
<td>498</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>0442-Allow for Doubt. Lease Rec NC</td>
<td>N/A</td>
<td>X X</td>
</tr>
</tbody>
</table>

### Lessor entries at lease termination or at the end of the lease

<table>
<thead>
<tr>
<th>Step</th>
<th>Description of transaction</th>
<th>T-Code</th>
<th>DR</th>
<th>CR</th>
<th>Cod</th>
<th>Measurement Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>11a.</td>
<td>Move current portion of lease receivable to noncurrent</td>
<td>474</td>
<td>2951-System Clearing GL</td>
<td>0000-Lease Receivable-nonnear</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>11b.</td>
<td>Adjust lease receivable-nonnear</td>
<td>474</td>
<td>0841-Lease Receivable-nonnear</td>
<td>2951-System Clearing GL</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>12.</td>
<td>Eliminate allowance for uncollectible lease receivable-nonnear</td>
<td>486</td>
<td>0442-Allow for Doubt. Lease Rec NC</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>N/A</td>
<td>X X</td>
</tr>
<tr>
<td>13.</td>
<td>Record gain/(loss) on lease (calculation = rec receivable balance less deferred inflow on lease receivable balance)</td>
<td>522</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>3200-GAAP Revenue Offset</td>
<td>2347</td>
<td>X X</td>
</tr>
<tr>
<td>14.</td>
<td>Eliminate lease receivable-nonnear</td>
<td>498</td>
<td>1561-Def. Inflow Lease Rec</td>
<td>0441-Lease Receivable-nonnear</td>
<td>N/A</td>
<td>X X</td>
</tr>
</tbody>
</table>
**EXHIBIT E – Lease Measurement Example**

Agency A enters into a contract with Contractor B to lease equipment. The lessee then compares the present value amounts to the fair value of the asset to determine if the present value of minimum future lease payments exceeds 90% of the fair value of the leased asset.

For example, the lessee:

- Leases equipment for a 5-year non-cancellable period
- Will make 5 annual payments of $50,000
- The interest rate implicit in the lease is 3%
- Will make the first payment upon signing the lease on 6/30/X1

Both the lessee's incremental borrowing rate and the lessor's implicit borrowing rate are 10%

Fair value of the property is $230,000

<table>
<thead>
<tr>
<th>Year</th>
<th>Net cash flow</th>
<th>(1 + discount rate) ^ time</th>
<th>Present value of minimum future lease payments</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>50,000.00</td>
<td>1.03</td>
<td>50,000</td>
</tr>
<tr>
<td>2</td>
<td>48,543.69</td>
<td>1.03</td>
<td>48,543.69</td>
</tr>
<tr>
<td>3</td>
<td>47,129.80</td>
<td>1.03</td>
<td>47,129.80</td>
</tr>
<tr>
<td>4</td>
<td>45,757.08</td>
<td>1.03</td>
<td>45,757.08</td>
</tr>
<tr>
<td>5</td>
<td>44,424.35</td>
<td>1.03</td>
<td>44,424.35</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>XXXXXXXXX</td>
<td>235,854.92</td>
</tr>
</tbody>
</table>

Annual lease payments $50,000

From PV tables: Present value of an annuity due $50,000 x Interest rate 10% and number of periods is 5 $4,19686

Present value of minimum future lease payments $2208,493 $35,854.92
Present value of minimum future lease payments $208,493
Divided by fair value of the property $230,000
Percentage of fair value 90.65%

Capitalize the lease at $208,493 and report interest per the following schedule:

<table>
<thead>
<tr>
<th>Date</th>
<th>Lease Payment</th>
<th>Interest @ 10%</th>
<th>remaining liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>6/30/X1</td>
<td>-</td>
<td>-</td>
<td>208,493</td>
</tr>
<tr>
<td>6/30/X1</td>
<td>50,000</td>
<td>50,000</td>
<td>158,493</td>
</tr>
<tr>
<td>6/30/X2</td>
<td>50,000</td>
<td>15,849</td>
<td>124,342</td>
</tr>
<tr>
<td>6/30/X3</td>
<td>50,000</td>
<td>12,434</td>
<td>86,777</td>
</tr>
<tr>
<td>6/30/X4</td>
<td>50,000</td>
<td>8,678</td>
<td>45,454</td>
</tr>
<tr>
<td>6/30/X5</td>
<td>50,000</td>
<td>4,545</td>
<td>(0)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Lease Payment</th>
<th>Interest @ 3%</th>
<th>Principal</th>
<th>Remaining Liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>06/30/20x1</td>
<td>$</td>
<td>$</td>
<td>$</td>
<td>$ 235,854.92</td>
</tr>
<tr>
<td>06/30/20x1</td>
<td>50,000.00</td>
<td>-</td>
<td>50,000.00</td>
<td>185,854.92</td>
</tr>
<tr>
<td>06/30/20x2</td>
<td>50,000.00</td>
<td>5,575.65</td>
<td>44,424.35</td>
<td>141,430.57</td>
</tr>
<tr>
<td>06/30/20x3</td>
<td>50,000.00</td>
<td>4,242.92</td>
<td>45,757.08</td>
<td>95,673.48</td>
</tr>
<tr>
<td>06/30/20x4</td>
<td>50,000.00</td>
<td>2,870.20</td>
<td>47,129.80</td>
<td>48,543.69</td>
</tr>
<tr>
<td>06/30/20x5</td>
<td>50,000.00</td>
<td>1,456.31</td>
<td>48,543.69</td>
<td></td>
</tr>
</tbody>
</table>

* Applies to measurement of lease liability or lease receivable.