



Lease Policy

Updated for GASB 87

City of Foley, Alabama

Adopted _____ Resolution _____

Rescinds Resolution 16-1097 Policy for Capital and Operational Equipment Lease as a result of GASB 87

Sec 1. Summary

The Governmental Accounting Standards Board (GASB) issued Standard 87, to improve accounting and financial reporting for leases by governments. This standard requires recognition of certain lease assets and liabilities for leases previously reported as operating leases; therefore establishing a single model of lease accounting based on the foundational principal that leases are financing of the right to use an underlying asset. This standard creates new asset categories referred to as Intangible Right to Use Assets, which can be Buildings, Land, Vehicles or Equipment.

Sec 2. Capitalization Threshold for Intangible Right to Use Assets

Intangible right-to-use assets associated with leases of the City should be capitalized if the future lease payments remaining in the lease term are \$15,000 or greater.

If the primary government is a lessee in a leasing arrangement, the intangible right-to-use lease asset should be capitalized if greater than or equal to the threshold above. Assets with remaining lease payments below the threshold should be expensed as payments are made. This threshold should only be applied once upon entering into a lease agreement as defined by GASB Statement 87.

Example: The City has an equipment lease with a lease term of five years. Payments per the lease contract are \$255 per month. At the time of implementing GASB Statement 87, Leases, the entire five years of payments were left on the lease. The City would capitalize this lease because the remaining payments on the lease are greater than or equal to \$15,000.

Example: The City has an equipment lease with a lease term of five years. Payments per the lease contract are \$255 per month. At the time of implementing GASB Statement 87, Leases, only one year of payments were left on the lease. The City would not capitalize this lease because the remaining payments on the lease are less than \$15,000. Instead, payments would be expensed for the remainder of the lease term (one year).

Sec 3. Lease Term

The lease term is the period in which there is a noncancelable right to use the underlying asset, plus all following periods (if applicable):

- Periods covered by a lessee's (or lessor'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 (or lessor's) option to terminate the lease if it is reasonably certain, based on all relevant factors, that the lessee will not exercise that option.

A fiscal funding or cancellation clause should affect the lease term only when it is reasonably certain that the clause will be exercised.

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

- 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.
- 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.
- An event specified in the lease contract that requires an extension or termination of the lease takes place

Sec 4. Short-Term Leases

A short-term lease is a lease that, at the commencement of the lease term, has a maximum possible term of 12 months (or less), including any options to extend, regardless of their probability of being exercised. Short term leases will be recognized as revenues (or expenses) as they occur.

Sec 5. Lessee Accounting

A Lessee should recognize a lease liability and a lease asset at the beginning of the lease term, unless the lease is a short term lease or it transfers ownership of the underlying asset. The lease liability should be measured at the present value of payments expected to be made during the lease term (less any lease incentives). The lease asset should be measured at the amount of the initial measurement of the lease liability, plus any payments made to the lessor at or before the commencement of the lease term and certain direct costs.

A lessee should reduce the lease liability as payments are made and recognize an outflow of resources (for example, expense) for interest on the liability. The lessee should 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. The notes to the financial statement should include a description of all leasing arrangement, the amount of lease asset recognized, and a schedule of future lease payments to be made.

Sec 6. Lessor Accounting

A Lessor should recognize a lease receivable and a deferred inflow of resources at the beginning of the lease term, with certain exceptions for leases of assets held as investments, certain regulated leases, short-term leases, and leases that transfer ownership of the underlying asset. A lessor should not derecognize the asset underlying the lease. The lease receivable should be measured at the present value of lease payments expected to be received during the lease term. The deferred inflow of resources should be measured at the value of the lease receivable plus any payments received at or before the commencement of the lease term that relate to future periods.

A lessor should recognize interest revenue on the lease receivable and an inflow of resources (for example, revenue) from the deferred inflows of resources in a systematic and rational manner over the term of the lease. The notes to financial statements should include a description of leasing arrangements and the total amount of inflows of resources recognized from leases.

Sec 7. Lease Modifications and Subleases

An amendment to a lease contract should be considered a lease modification, unless the lessee's right to use the underlying asset decreases, in which case it would be a partial or full lease termination. A lease termination should be accounted for by reducing the carrying values of the lease liability and lease asset by a lessee, or the lease receivable and deferred inflows of resources by the lessor, with any difference being recognized as a gain or loss. A lease modification that does not qualify as a separate lease should be accounted for by remeasuring the lease liability and adjusting the related lease asset by a lessee and remeasuring the lease receivable and adjusting the related deferred inflows of resources by a lessor.

Subleases should be treated as transactions separate from the original lease. The original lessee that becomes the lessor in a sublease should account for the original lease and the sublease as separate transactions, as a lessee and lessor, respectively.