Implementation of New GASB Standards Applicable to Utah School Districts (April 2019)

Compiled by Ray B. Bartholomew, CPA – Squire & Company, PC

GASB Statement Number	Topic	Issued	Effective RPBA	Fiscal Year Ending
75	Governments That Provide OPEB To Employees	Jun 2015	6/15/2017	6/30/2018
84	Fiduciary Activities	Jan 2017	12/15/2018	6/30/2020
85	Omnibus - 2017	Mar 2017	6/15/2017	6/30/2018
86	Certain Debt Extinguishment Issues	May 2017	6/15/2017	6/30/2018
87	Leases	Jun 2017	12/15/2019	6/30/2021
88	Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements	Apr 2018	6/15/2018	6/30/2019
89	Accounting for Interest Costs Incurred before the End of a Construction Period	Jun 2018	12/15/2019	6/30/2021
90	Majority Equity Interests-an amendment of GASB Statements No. 14 and No. 61	Aug 2018	12/15/2018	6/30/2020

RPBA = Reporting Periods Beginning After

Projects

	Financial Reporting Model	(Feb 2022)
	Revenue and Expense Recognition	(Mar 2023)
	Disclosure Framework	(May 2022)
	Subscription-Based Information Technology Arrangements	(June 2021)
	Compensated Absences	
	Prior-Period Adjustments, Accounting Changes, and Error Corrections	

GASB 84, *Fiduciary Activities*, issued January 2017, effective for reporting periods beginning after December 15, 2018, earlier application is encouraged.

Provides guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The focus is on whether a government is controlling the assets of the fiduciary activity, and the beneficiaries with whom a fiduciary relationship exists.

An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements (a statement of fiduciary net position and a statement of changes in fiduciary net position).

There are four types of fiduciary funds, namely,

1. Pension (and other employee benefit) trust funds,
2. Investment trust funds,
3. Private-purpose trust funds, and
4. Custodial funds (resources that are not held in a trust or equivalent arrangement).

A government controls the assets of an activity if the government 1) holds the assets or 2) can direct the use, exchange, or employment of the assets in a manner that provides benefits to the specified or intended recipients.

Paragraph 11 of GASB 84 a defines other fiduciary activities:

> 11. For activities not addressed in paragraphs 6−10, the activity is a fiduciary activity if all of the following criteria are met:
>
> a. The assets associated with the activity are controlled by the government (as described in paragraph 12).
>
> b. The assets associated with the activity are *not* derived either:
>
> (1) Solely from the government's own-source revenues (as described in paragraph 13) or
>
> (2) From government-mandated nonexchange transactions or voluntary nonexchange transactions with the exception of pass-through grants for which the government does not have administrative involvement or direct financial involvement.
>
> c. The assets associated with the activity have one or more of the following characteristics:
>
> (1) The assets are
> (a) administered through a trust in which the government itself is *not* a beneficiary,
> (b) dedicated to providing benefits to recipients in accordance with the benefit terms, and
> (c) legally protected from the creditors of the government.
>
> (2) The assets are for the benefit of individuals and the government does *not* have administrative involvement with the assets or direct financial involvement with the assets.[3] In addition, the assets are *not* derived from the government's provision of goods or services to those individuals.
>
> (3) The assets are for the benefit of organizations or other governments that are *not* part of the financial reporting entity. In addition, the assets are *not* derived from the government's provision of goods or services to those organizations or other governments.
>
> [3]For purposes of this provision, a government has administrative involvement with the assets if, for example, it (a) monitors compliance with the requirements of the activity that are established by the government or by a resource provider that does not receive the direct benefits of the activity, (b) determines eligible expenditures that are established by the government or by a resource provider that does not receive the direct benefits of the activity, or (c) has the ability to exercise discretion over how assets are allocated. A government has direct financial involvement with the assets if, for example, it provides matching resources for the activities.

Illustrative financial statements of a custodial fund of a school district that receives grants for other governments:

Bonneville School District
Statement of Fiduciary Net Position
Western Utah Educational Services Custodial Fund
June 30, 2019

Assets:		
Cash	$	329,814
Receivable for other governments		150,227
Other assets		361
Total assets		480,402
Liabilities:		
Accounts payable and other liabilities		1,200
Due to other governments		413,656
Total liabilities		414,856
Net position:		
Restricted for other governments	$	65,546

Bonneville School District
Statement of Changes in Fiduciary Net Position
Western Utah Educational Services Custodial Fund
Year Ended June 30, 2019

Additons:		
Grant collections for other governments	$	1,654,523
Investment earnings:		
Interest		2,150
Investment costs		(682)
Net investment earnings		1,468
Total additions		1,655,991
Deductions:		
Grants distributed to other governments		1,597,322
Administrative costs		15,000
Total deductions		1,612,322
Net increase in fiduciary net position		43,669
Net position - beginning		21,877
Net position - ending	$	65,546

[GASB 87, *Leases*, issued June 2017, effective for reporting periods beginning after December 15, 2019; earlier application is encouraged]

This Statement requires reporting certain lease liabilities that currently are not reported. The accounting is based on the substance of the arrangement rather than the label on the contract. The terms *capital lease* and *operating lease* are discontinued.

Leases – Leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset. A lessor is required to recognize a lease receivable and a deferred inflow of resources.

A *lease* is a contract that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Any contract that meets this definition is accounted for as a lease, unless specifically excluded, such as:

- A short-term lease is defined as a lease that, at the beginning of the lease, has a maximum possible term under the contract of 12 months or less, including options to extend, regardless of its probability of being exercised. Lessees and lessors should recognize short-term payments as expenditures/expenses or revenues, respectively, based on the payment provisions of the contract.

- Contracts that transfer the right to use an asset that require only a nominal amount, such as one dollar per year, are nonexchange transactions and should be accounted for according to the provisions of GASB 33.

- Licensing agreements for computer software should not be treated as leases.

- Leases that transfer ownership before or at the end of the lease and do not contain termination options are accounted for as financed purchases rather than as leases. The substance of a lease that transfers ownership is a purchase of the underlying asset with payments financed over time. Therefore, assuming there is no possibility of termination before the transfer occurs, such a contract follows guidance for acquisition of capital assets with related long-term liabilities instead of guidance for leases. Provisions that allow for termination of a lease due to fiscal funding or cancellation clauses, purchase of the underlying asset, payment of all sums due, or default are not considered termination options and, therefore, do not disqualify the transactions from being treated as a financed purchase.

The *lease term* is the period during which a lessee has a noncancelable right to use an underlying asset, plus the following periods, if applicable, covered by a *lessee's* option to:

- Extend the lease if it is reasonably certain that the lessee will exercise that option
- Terminate the lease if it is reasonably certain that the lessee will not exercise that option.

Fiscal funding clauses should be evaluated in the same manner as other termination options. That is, it is not considered in determining the lease term unless it is reasonably certain that the option will be exercised (funds will not be appropriated).

The lease term is to be reassessed only when it is reasonably certain that the lessee changes its determination to exercise or not to exercise an option.

Lessee Accounting **–** A lease liability and a lease asset is recognized as the beginning of a lease, unless the lease is a short-term lease or transfers ownership of the underlying asset.

The *lease liability* is the present value of payments expected to be made for the lease term.

The *lease asset* is the amount of the lease liability, plus any payments made to the lessor at or before the beginning of the lease and certain indirect costs less any lease incentives received from the lessor. The lease asset is the right to use the underlying asset rather than the underlying asset itself.

The lessee reduces the lease liability as payments are made and recognize an expense for interest on the liability. The lessee amortizes the lease asset (usually straight-line) over the shorter of the lease term or the useful life of the underlying asset. The notes to the financial statements are to include a description of leasing arrangements, the amount of lease assets recognized, and a schedule of future lease payments to be made.

Lessor Accounting **–** A lessor recognizes a lease receivable and a deferred inflow of resources at the beginning of a lease, with certain exceptions (including a short-term lease or a lease that transfers ownership of the underlying asset). A lessor continues to recognize the asset underlying the lease. The lease receivable is the present value of lease payments expected to be received for the lease term. The deferred inflow of resources is the value of the lease receivable plus any payments received at or prior to the beginning of the lease that relate to future periods.

A lessor recognizes interest revenue on the lease receivable and revenue from the amortization of the deferred inflow of resources over the term of the lease. The notes to the financial statements are to include a description of the leasing arrangements and the total amount of revenue recognized from the leases.

Lease Terminations and Modifications – A lease termination is accounted for by reducing the carrying values of the lease liability and lease asset by the lessee, or the lease receivable and deferred inflow of resources by the lessor, with any difference being recognized as a gain or loss. A lease modification is accounted for by remeasuring the lease liability and adjusting the related lease asset by the lessee, or remeasuring the lease receivable and adjusting the related deferred inflow of resources by the lessor.

Subleases and Leaseback Transactions – Subleases are treated as transactions separate from the original lease. A sale-leaseback transaction is accounted for as a separate sale and lease transactions, except that any difference between the carrying value of the capital asset that was sold and the net proceeds from the sale is reported as a deferred inflow/outflow of resources and recognized over the term of the leaseback. A lease-leaseback transaction is accounted for as a net transaction. The gross amounts of each portion of the transaction are disclosed.

This Statement is effective for reporting periods beginning after December 15, 2019. It applies to earlier periods presented (the beginning of the earliest period restated).

Recommendation for Utah School Districts:

- Compile lease contracts and information. Identify lease terms, payments, initial direct costs (ancillary charges necessary to place an asset into service; does not include debt issuance costs), and lease incentives.
- Implement the new standard no later than July 1, 2020. (Because the standard applies to each period presented, begin to measure leases under the new standard on July 1, 2019.)
- For leases financed with general governmental resources, governmental funds will reflect the amount of the lease asset as an expenditure and other financing source. *Accordingly, the budget should also reflect these amounts.*
- In governmental fund financial statements, lease receivables and deferred inflows of resources are recorded by the lessor.
- Disclose lease assets and related accumulated amortization (by major classes of underlying assets) separately from other capital assets.
- Disclose the principal and interest components of lease liabilities separately from other long-term liabilities for each of the next five years and in five-year increments thereafter.

APPLICATION

Does the agreement meet the definition of a lease?

A lease is a contract that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Exceptions include short-term leases (maximum possible term of 12 months or less) and transfers of ownership.

What are the terms of the agreement?

The lease term is the period during which a lessee has a noncancelable right to use an underlying asset, plus the following periods, if applicable, covered by a lessee's option to:

- *Extend the lease if it is reasonably certain that the lessee will exercise that option*
- *Terminate the lease if it is reasonably certain that the lessee will not exercise that option.*

What are the expected cash flows?

Payments expected to be made for the lease term, payments made at or before the beginning of the lease, indirect costs, lease incentives, purchase options, termination penalties, and residual guarantees.

What discount rate should be used to calculate the present value of payments expected to be made during the term of the lease?

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) would normally be used.

How would a government lessee or lessor account for the lease, initially and during the lease term?

Initial measurement of lease transaction:

	Assets	Liability	Deferred Inflow
Lessee	Intangible lease asset (right to use underlying asset)—value of lease liability plus initail indirect costs that are ancillary to place asset in use	Present value of future lease payments, variable payments based on index or rate, reasonably certain residual guarantees, etc.)	Not applicable
Lessor	• Lease receivable (generally includes same items as lessee's liability) • Continue to report leased asset	Not applicable	Equal to lease receivable plus any cash received up front that relates to a future period

Subsequent lease activity:

	Assets	Liability	Deferred Inflow
Lessee	Amortize the intangible lease asset over shorter of useful life or lease term	Reduce by lease payments (less amount for interest expense)	Not applicable
Lessor	• Reduce receivable by lease payments (less amounts needed to cover accrued interest) • Depreciate leased asset (unless indefinite life or required to be returned in its original or enhanced condition)	Not applicable	Recognize revenue over the lease term in a systematic and rational manner

Assume the following facts regarding a district's lease, beginning July 1, 2019:

1. 10-year lease of a building, with an option to extend for an additional 5 years.
2. Lease payments are $50,000 per year during the initial term and $55,000 per year during the optional period, all payable in arrears.
3. The district incurs initial direct costs (for improvements) of $65,000.
4. The district receives a $50,000 lease incentive at the beginning of the lease.
5. At the beginning of the lease, the district concludes that is it not reasonably certain to exercise the option.
6. The district's incremental borrowing rate at the beginning of the lease is 5%.

The present value of the 10 remaining payments is $386,087. The lease asset is measured at $401,087 (the initial lease liability + initial direct costs – lease incentive).

Payment Schedule

	Date	Payment	Interest	Principal	Balance
	7/1/2019				386,087
1	6/30/2020	50,000	19,304	30,696	355,391
2	6/30/2021	50,000	17,770	32,230	323,161
3	6/30/2022	50,000	16,158	33,842	289,319
4	6/30/2023	50,000	14,466	35,534	253,785
5	6/30/2024	50,000	12,689	37,311	216,474
6	6/30/2025	50,000	10,824	39,176	177,298
7	6/30/2026	50,000	8,865	41,135	136,162
8	6/30/2027	50,000	6,808	43,192	92,971
9	6/30/2028	50,000	4,649	45,351	47,619
10	6/30/2029	50,000	2,381	47,619	-
		500,000	113,913	386,087	

At the end of Year 1, the lease liability is $355,391 and the lease asset is $360,978.

Amortization Schedule

	Date	Amortization	Balance
	7/1/2019		401,087
1	6/30/2020	40,109	360,978
2	6/30/2021	40,109	320,869
3	6/30/2022	40,109	280,761
4	6/30/2023	40,109	240,652
5	6/30/2024	40,109	200,543
6	6/30/2025	40,109	160,435
7	6/30/2026	40,109	120,326
8	6/30/2027	40,109	80,217
9	6/30/2028	40,109	40,109
10	6/30/2029	40,109	0
		401,087	

Note that total interest expense and total amortization expense over the term of the lease is $515,000 ($113,913 interest + $401,087 amortization).

For the year ending June 30, 2020, the district would account for the lease as follows:

	dr.	cr.
Initial measurement		
Governmental Fund:		
Cash		(15,000)
Expenditure - lease	401,087	
Other financing use - lease		(386,087)
At end of Year 1		
Governmental Fund:		
Cash		(50,000)
Expenditure - lease	50,000	
Government-wide financial statements:		
Lease asset	401,087	
Accumulated amortization - lease asset		(40,109)
Lease liability		(355,391)
Expenditure - lease		(451,087)
Other financing use - lease	386,087	
Interest expense	19,304	
Lease amortization	40,109	

GASB 89, *Accounting for Interest Costs Incurred before the End of a Construction Period*, issued June 2018, effective for reporting periods beginning after December 15, 2019; earlier application is encouraged.

This Statement –

- Enhances the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period
- Simplifies accounting for certain interest costs

Accounting

"In financial statements prepared using the economic resources measurement focus [government-wide and proprietary fund financial statements], interest costs incurred before the end of a construction period should be recognized as an expense in the period in which the cost is incurred. Such interest cost should not be capitalized as part of the historical cost of a capital asset."

"In financial statements prepared using the current financial resources measurement focus [governmental fund financial statements], interest cost incurred before the end of a construction period should be recognized as an expenditure on a basis consistent with governmental fund accounting principles."

Application

Changes adopted to conform to the provisions of this Statement should be applied prospectively. For construction-in-progress, interest costs incurred after the Statement is applied should not be capitalized.