




City of Arts & Innovation

City of Riverside Administrative Manual

Effective Date: 07/01/2021
Latest Revision Date: 07/01/2021
Next Review Date: 07/01/2024
Policy Owner(s): Finance Department

Approved:



Michael D. Moore Department
City Manager

SUBJECT:

GASB 87 Lease Policy

PURPOSE:

This policy establishes accounting treatment of lease agreements entered into by the organization, both as a lessee and as a lessor.

The Governmental Accounting Standards Board has issued Statement No. 87, *Leases* (GASB 87), which establishes a single model for lease accounting based on the principle that leases are financings of the right to use an asset. There is no longer an operating versus capital classification. Lessees will recognize an intangible right-to-use asset and a lease liability. Lessors will recognize a lease receivable and a deferred inflow of resources. Contracts for service are not included in this standard. Contracts that contain both a lease component (right to use a building) and a service component (maintenance of the building) should be separated and only the lease component should be included.

POLICY:

As required by GASB 87, the City is required to implement this pronouncement as of July 1, 2021. As a result, the City is required to restate current year beginning balances to reflect the implementation of GASB 87.

The materiality threshold for GASB 87 leases has been established at \$5,000 for both lessee and lessor activities. The lease term threshold for GASB 87 are leases with terms greater than 12 months, including options to extend if it is likely to be extended. The lease must meet both the materiality and term thresholds to be considered a GASB 87 lease.

Capital Financing Activities

Leases that transfer ownership will no longer be classified as capital leases; they will be reported as capital financing activities. This is a terminology change only and does not impact the accounting or financial statement disclosures.

Transactions that are excluded from GASB 87

The Statement excludes the following items from its application:

- Leases for intangibles (including computer software), except for sublease of intangible right-to-use leased asset
- Leases for biological assets
- Leases for inventory
- Leases where underlying asset financed with conduit debt, except for underlying asset and conduit debt reported by lessor
- Service concession agreements
- Supply contracts – electric power purchase agreements
- Short-term leases (maximum term 12 months or less)
- Contracts that transfer ownership of the underlying asset to the lessee (see Capital Financing Activities)

General Rule for Entering Leases into the Lease Software

- *Transition Rate:* As a matter of policy, the City will establish the transition/implicit rate at the individual lease level. The transition/implicit rate below will only apply to the implementation year, fiscal year 2021/22 for all GASB 87 eligible leases in effect as of July 1, 2021.

Fiscal Year 2021/22 Transition/Implicit Rates for GASB 87 Leases	
Lease Term	Interest Rate
1 to 5 years	0.52%
6 to 10 years	1.24%
11 to 20 years	1.68%
21 and thereafter	1.79%

Payment Date: For lease entry into the software solution, the first payment date for all leases will be as of the first day of the month. For example, if a lease agreement indicates that the first payment is due no later than March 22, 2021, the first payment date will be entered as March 1, 2021. All subsequent payments will be assumed to have been due on the first day of the succeeding months.

Incremental Borrowing/Implicit Rate: This is the rate a lessee would pay to borrow the lease payment amounts during the lease term. In most cases, the borrowing rate is not stated in the lease; however, it is implied that there is a cost to borrowing the amounts. Due to the sensitivity of assumptions within the borrowing rate, the City will obtain the 5, 10, 20 and 30 year generic rated municipal yields from City’s Investment Management company as of 6/30 to be used for the current fiscal year (e.g., use 6/30/2021 rates for fiscal year 2021/22) for any new eligible GASB 87 leases and lease amendments.

The following provides guidance in determining the appropriate interest rate variables to use:

- **Explicit Rate** - If an interest rate is specified in the contract, use this rate.
- **Implicit Rate** - If no interest rate is specified in the contract, an interest rate will be determined effective July 1st of each year for any new eligible GASB 87 leases and lease amendments.

For new eligible GASB 87 leases or lease amendments that take effect on or after July 1st, departments will need to enter into LeaseQuery the explicit rate specified in the contract or the implicit rate, which can be obtained from the Finance Department.

Lease Term: The period during which the lease has the noncancelable right to use the underlying asset PLUS periods where:

1. Lessee or lessor has the option to extend (if reasonably certain to exercise) periods
2. Lessee or lessor has the option to terminate (as long as it is not reasonably certain to cancel), including fiscal funding clauses

General Rule for Reporting Leases to the Finance Department

Departments that initiate lease agreements are required to communicate to the Finance Department lease terms, options, and payment provisions. When there is a change in a lease term, estimated lease payment amounts, or other components of lease agreements, such information should be communicated to the Finance Department in a timely manner.

PROCEDURE:

<u>Responsibility</u>	<u>Action</u>
Finance	<ul style="list-style-type: none">• Obtain the 5, 10, 20 and 30 year generic rated municipal yields from City's Investment Management company as of 6/30 to be used for the current fiscal year (e.g., use 6/30/2021 rates for the fiscal year 2021/22).• May assist departments in determining GASB 87 lease applicability.• Administrative functions within LeaseQuery.• Positing yearly GASB 87 entries produced from LeaseQuery into City's financial system.
Departments	<ul style="list-style-type: none">• Input ALL new leases in LeaseQuery regardless of GASB 87 eligibility; leases that are considered short-term or immaterial (non-GASB 87 leases) will be entered and noted in LeaseQuery for lease management purposes only.• Obtain guidance from Finance Department regarding GASB 87 eligibility, when needed.• Monitor, maintain, and track all department leases within LeaseQuery.• Input explicit or implicit rate in LeaseQuery for new eligible GASB 87 leases and/or lease amendments. Implicit rate can be obtained from the Finance Department.

Distribution: Regular