



Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Table of Contents

Overview	2
Introduction	2
Policy	2
General	2
Financed Purchase Lease	2
Procedures	3
Installment Purchases	3
Lease Contract	3
Purchase Option Reasonably Certain to be Exercised	4
Ancillary Charges	4
Payments Made Prior to the Commencement of the Lease Term	5
Guaranteed Residual Value Payments	5
Lease Classification	5
Lease Analysis	6
Leasehold Improvements Must Be Capitalized	6
Recording Leasehold Improvements in FAACS	6
Internal Control	7
General	7
Records Retention	7
General	7
DOA Contact	7
Contact	7
Subject Cross References	8
References	8

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020


Overview

Introduction This topic provides guidance about entering into lease contracts and ensuring proper classification of leases and handling leasehold improvements. All financial information related to nonfinancial asset lease contracts must be properly recorded and accounted for on the books of the Commonwealth with appropriate reporting and disclosure in the Comprehensive Annual Financial Report (CAFR) and agency financial statements in accordance with generally accepted accounting principles (GAAP) and **GASB Statement No. 87, *Leases***, (GASB 87) requirements. The following procedures help to ensure compliance with these requirements.

Policy

General Agencies must ensure that proper documentation and analysis is performed as to whether or not a contract to use a nonfinancial asset is a lease. If it is a lease, proper classification must be determined in order to accurately record, account for and report on the leased asset. If it is not a lease, CAPP Section No. 31200, *Lease Accounting*, is not applicable. Instead, CAPP Sections 30100 through 31100 covering the Fixed Asset Accounting and Control System (FAACS) would be applicable.

Financed Purchase Lease This is a lease where title to the underlying assets passes to the lessee at the end of the lease contract. Financed purchase leases should be recorded in Lease Accounting System 87 (LAS 87).

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Procedures

Installment Purchases

If title passes upon signature, the contract is an installment purchase and **should not** be recorded in LAS 87. If the asset passes the FAACS input requirements (see CAPP Topic No. 30305, *Capitalized or Controlled Assets*), it should be recorded in FAACS.

Lease Contract


All lease contracts should be recorded in LAS 87

Once a contract has been determined to be a lease, enter the following information to properly classify the lease in LAS 87. This information should be available in the lease contract.

Required Lease Information

- **Estimated Value of the Leased Asset:** See Definitions in CAPP Topic No. 31205-LAS 87, *Introduction*. For leased assets that are new, this value is typically the purchase price of the underlying asset and may be obtained from the vendor or may be independently verified by the agency using the following sources:

Continued on next page

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Procedures, Continued

Agency	Item to be Valued
Virginia Information Technologies Agency (VITA)	Electronic data processing equipment
Department of General Services, Division of Engineering and Buildings	Real Estate
Department of General Services, Division of Purchases and Supply, or independent research using state contracts or a “web-search.”	All other items

- **Incremental Borrowing Rate:** See Definition CAPP Topic No. 31205-LAS 87, *Introduction*. LAS 87 uses the current Prime Interest Rate as the default rate to calculate the lease asset and lease liability. **Users should overwrite this rate with the lessor’s rate whenever the lessor’s rate is available.**
- **Executory Costs:** See Definition CAPP Topic No. 31205 – LAS 87 - *Introduction*.
- The number of required payments and the frequency of the lease payments (monthly, quarterly, annually, etc.).
- Any additional terms and conditions regarding extensions or purchase options.


Purchase Option Reasonably Certain to be Exercised

If the lease contract contains a purchase option where the lessee may purchase the leased asset at the end of the lease term **and** the lessee is reasonably certain to exercise this option, then the amount of the purchase option must be entered into LAS 87. Purchase options reasonably certain to be exercised are automatically added by LAS 87 to the last payment in the lease payment stream for purposes of calculating the lease liability.

Ancillary Charges

Ancillary charges are amounts charged by the lessor to place the lease asset into service. If ancillary charges are paid to the lessor, then these amounts must be entered into LAS 87. Ancillary charges are automatically added by LAS 87 to determine the lease asset amount.

Continued on next page

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Procedures, Continued


Payments Made Prior to the Commencement of the Lease Term Payments made prior to the commencement of the lease term are amounts other than ancillary charges paid to the lessor prior to the beginning of the lease term. If payments made prior to the lease contract are paid to the lessor, then these amounts must be entered into LAS 87. Payments made prior to the lease term are automatically added by LAS 87 in the same manner as ancillary charges to determine the lease asset amount.

Guaranteed Residual Value Payments Guaranteed residual value payments paid to the lessor at the end of the lease term when the lessee returns the lease asset back to the lessor must be entered into LAS 87. Guaranteed residual value payments are not automatically included in the calculation of the lease liability. DOA will evaluate any guaranteed residual value payments to determine significance and make manual adjustments to the calculation of the lease liability as deemed necessary.

Lease Classification Lease Classification
 Leases may be classified as short-term, long-term or as a financed purchase. A finance purchase is a contract where the title to the underlying asset passes to the lessee at the end of the contract term. Whether the lease is short-term or long-term depends on the following conditions:

- Short-term leases are leases that have a lease term of 12 months or less including all extension periods regardless of whether or not the extension periods will be exercised and does not include a termination clause. Short-term leases only require footnote disclosure in the financial statements.
- Long-term leases are leases having a lease term of greater than 12 months and where the lease asset equals \$50,000 or more. Long-term leases require recording an intangible asset and liability in the financial statements and footnote disclosure.
- See Lease Classification in CAPP Topic No. 31210-LAS 87, *Economic Analysis* for the requirements associated with lease evaluation and compliance with the Appropriation Act General Provisions.

Continued on next page

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Procedures, Continued

Lease Analysis Tests to determine lease classification are defined in CAPP Topic No. 31210-LAS 87, *Economic Analysis*.

Agencies should perform an analysis of each prospective lease to determine if the lease is (1) a short-term lease (2) a long-term lease or (3) a financed purchase of the underlying asset in accordance with **GASB Statement No. 87, Leases**. Contact DOA for assistance with this analysis as needed.

As previously stated, a lease involving a leased asset with a lease term more than 12 months and a calculated value of less than \$50,000 will be classified as a short-term lease for CAFR reporting purposes.

Contracts where the title passes to the lessee at the end of the contract term are financed purchases of the underlying asset.


**Leasehold
Improvements
Must Be
Capitalized**

Permanent improvements to leased assets are considered an integral part of the leased property and must be capitalized in FAACS when the improvement meets the FAACS recording threshold.

Such improvements represent items that cannot be removed without substantially damaging or requiring substantial repair to the leased asset. Therefore, the capitalized leasehold improvement cost should be depreciated over either the (1) term of the lease or (2) service life of the improvement, whichever is shorter.

**Recording
Leasehold
Improvements
in FAACS**

Leasehold improvements are entered into FAACS using special nomenclature codes for leasehold improvements. Capital assets merely located on leased property and not permanently installed should be recorded in FAACS using the appropriate FAACS nomenclature code to reflect the asset's category (See CAPP Topic No. 30315, *Nomenclature Codes*.)

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Internal Control

General

Each agency and institution should implement cost-beneficial internal control procedures to ensure that:

- All potential contracts to use nonfinancial assets are properly evaluated to determine if the transaction is truly a lease.
 - All leases are properly classified as short-term, long-term or a financed purchase.
 - All leasehold improvements are properly evaluated for inclusion in FAACS.
-

Records Retention

General

Records should be maintained for a period of at least three years or longer, if necessary, to be in compliance with policies established by the Records Management Section, The Library of Virginia. The retention period generally starts at the close of the fiscal period.

For pending, ongoing or unresolved litigation, audits or claims, retain documentation until completion, resolution or negotiation of settlements and retain according to standard schedules. Provide for the periodic destruction of records not subject to permanent deposit in accordance with policies and procedures established by the Records Management Section, Virginia State Library and Archives.

DOA Contact


Contact

Financial Reporting Project Lead

☎ (804) 225-2257

FAX (804) 225-2430

✉ las@doa.virginia.gov

Volume No. 1—Policies and Procedures	TOPIC NO	31215-LAS 87
Section No. 31200—Lease Accounting	TOPIC	Transactions
	DATE	March 2020

Subject Cross References

References

CAPP Topic No. 30305, *Capitalized or Controlled Assets*

CAPP Topic No. 30315, *Nomenclature Codes*

CAPP Topic No. 31205-LAS 87, *Introduction*

CAPP Topic No. 31220-LAS 87, *Reporting*
