ACCOUNTING

3. Liabilities
3.4 Leases and Installment Purchases

3.4.10 Lease Definition

A contract that 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.

3.4.20 Exclusions

The following items are not considered leases. For lessees that means these would not be reported on the Schedule of Liabilities (Schedule 09) as lease liabilities.

- Short-term leases – One that, at the beginning of the lease, has a maximum possible term of 12 months or less, including any options to extend - e.g. rolling month-to-month leases
- Interfund leases – Leases between departments or funds within the same government
- Lease of intangible assets – This includes mineral rights, patents, software, copyrights, except for the sublease of an intangible right-to-use asset created by the original lease of a tangible underlying asset
- Leases of biological assets – such as timber, living plants, and living animals
- Leases of inventory
- Service concession arrangements
- Assets financed with outstanding conduit debt – unless both the asset and conduit debt are reported by the lessor
- Supply contracts – such as power purchase agreements that do not convey control of the right to use the underlying power generating facility
- Certain regulated leases – such as aviation leases between airports and air carriers

3.4.30 Summary of BARS Codes

<table>
<thead>
<tr>
<th>Code</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>34P.PP</td>
<td>Lessors – For lease payments received if leasing is the primary operation of the fund.</td>
</tr>
<tr>
<td>362.00</td>
<td>Lessors – For lease payments received that are not the primary operation of the fund.</td>
</tr>
<tr>
<td>591.PP.70</td>
<td>Lessee – Lease/rental payments (ownership of asset is not transferred at the end of the contract)</td>
</tr>
<tr>
<td>594.PP.70</td>
<td>Installment purchase payments – Ownership of asset is transferred at the end of the contract</td>
</tr>
</tbody>
</table>

3.4.40 Lessor Accounting

Lessor only need to report the cash payments received for lease payments on the Schedule 01. Since lessors are receiving payments, there is no liability to report on the Schedule 09. To receipt payments, use either BARS Code 34P.PP or 362.00. If leasing is the primary operation/function of the fund that the payment is being receipted into, then use BARS Code 34P.PP which is a Charge For Services code. The “P” stands for prescribed numbers that are related to the function of the leasing activity. Review the chart of accounts to identify the applicable function and determine the full BARS Code. An example of when to use the 34P.PP code would be a port whose primary operation is leasing buildings.
If leasing is not the primary operation/function of the fund that the payment is being receipted into, then use BARS Code 362.00. An example of when to use BARS Code 362.00 is when a city or county is receipting lease payments into the general fund.

Lessors will use the revenue codes above for both short term and long term leases.

### 3.4.1.50 Lessee Accounting and Reporting

At the start of the lease, lessees will not report any inflows or outflows on the Schedule 01. Lessees will record actual lease payments made to the lessor on the Schedule 01 using BARS Code 591.PP.70.

If the lease includes additional fees or taxes, only include the portion of the payments related to the right to use the asset in the liability calculation. For example, if a copier lease has a separate maintenance fee or a separate per-copy fee, do not include those in the liability calculation. When paying the maintenance and per copy fees do not use BARS Code 591, instead use the regular BARS functional expense codes. However, if maintenance fees and taxes are included in the regular lease payments and they are not separated out in the contract, then include the full amount of the payment in the liability calculation.

Short term lease payments should be coded to normal, functional BARS expenditure codes. For example, if a government has a short term lease for a copier that is used by the water utility fund, the lease expense would be coded to BARS 534.00.40.

Lessees are also required to include a note disclosure about their lease activity in the Notes to the Financial Statements. See template note at Note X – Leases.

### 3.4.1.55 Lessee Schedule 09 Reporting

Lessees will report a lease liability on the Schedule 09 measured at the total amount of future lease payments. See Schedule 09 reporting instructions.

In the year of implementation, any existing leases should report a beginning balance on the Schedule 09. The beginning balance reported should be the total amount of lease payments that were remaining as of the beginning of the year. In subsequent years, the beginning balance should match the prior year ending balance.

Any leases that are entered into during the year will be reported as an addition on the Schedule 09. The addition will be the total amount of future lease payments.

Reductions are the amount the lease liability is reduced during the year, which is typically the amount of lease payments made.

If the lease liability is remeasured for any of the items listed in Section 3.4.1.70, the change in the lease liability should be reported as either an addition or reduction on the Schedule 09.

### 3.4.1.60 Lease Term

To calculate the total amount of future lease payments for the schedule 09, you need to know how many payments you are expecting to make which depends on the lease term. Here is what should be included in the lease term:

- The period during which a lessee has a non-cancelable right to use an underlying asset

- plus periods covered by a lessee’s or lessor’s option to extend the lease (if reasonably certain the option will be exercised)
- and periods covered by the lessee’s or lessor’s option to terminate the lease (if reasonably certain the option will not be exercised)

- Lease term excludes periods for which both the lessee and lessor each have the option to terminate or both parties must agree to extend

Determining whether a lease option is reasonably certain of being exercised or not requires professional judgement and should take into consideration the specific facts and circumstances at your government. Examples of items to consider in this analysis:
- Is there a history of extending the lease?
- Is the item being leased essential to your government’s operations or services provided to citizens?
- Can the asset be leased from other sources?
- Any other factors relevant to your specific circumstances.

3.4.1.70 Remeasuring the Lease Liability

The lease liability reported on the Schedule 09 must be remeasured (recalculated) if any of the following happen:
- Change in lease term
- Change in likelihood of purchase option
- Change in estimated amounts for payments already included
- Contingency resolved for variable payments.

The lease term might change if you were previously not going to exercise an extension option, but then determine you will extend the lease (or vice versa). In that case you should recalculate the lease liability to include the additional payments related to extending the lease term. If you previously determined you were not going to purchase the asset, but later determine that you will purchase the asset, then you should start treating the contract like an installment sale (use BARS codes 594.PP.70 for payments and the installment purchase codes on the schedule 09). Sometimes purchase options require additional amounts to be paid at the end of the contract in order to purchase the asset, those additional amounts should be added to your installment purchase liability on the schedule 09. If you used estimated amounts to calculate your lease liability and those amounts become known, you should recalculate the liability using the known amounts. If your lease payments were variable and later on all of your remaining lease payments become known (no longer variable), then you should recalculate the lease liability using the known amounts.

3.4.1.80 Installment Purchases (formerly called capital leases)

Leases that transferred ownership of the asset to the lessee were previously called capital leases. These are now called installment purchases. If a lease has a purchase option or bargain purchase option, you will need to determine whether that option will be exercised or not. If you determine the purchase option will not be exercised, treat the contract like a lease. If you determine that the purchase option will be exercised, treat the contract like a financed purchase.

3.4.1.85 Installment Purchase Accounting

You will add a liability to the Schedule 09 (Schedule of Liabilities) for the total amount of future payments, including the cost of any purchase options. At the start of the contract you do not record any
inflows or outflows on your Schedule 01. You will record payments made on your Schedule 01 using BARS Code 594.PP.70.

If your government previously determined they would not exercise the purchase option, but then later do exercise it, you should start treating the contract as an installment purchase at the time the decision is made. That means you should start coding your remaining lease payments to BARS 594.PP.70. However, you should not go back and change the BARS codes of any of your previous payments.