

VA Financial Policies and Procedures
Capital Lease Liability

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1801 OVERVIEW

This chapter establishes the Department of Veterans Affairs (VA) financial policies and procedures relating to the liabilities associated with capital leases for financial reporting purposes. The lease liability that is recorded in the Standard General Ledger (SGL) liability account reflects the amount of liability for the net present value of minimum lease payments for a capital lease agreement.

VA has the authority to enter into capital lease transactions for facilities to provide medical care under 38 U.S.C 8103. VA may make arrangements with the General Services Administration (GSA) to obtain leased space for a variety of purposes. In addition, VA may request approval from GSA to use a delegation of authority to obtain leased space. See GSA Bulletin 2008-B1, *Delegation of Lease Acquisition Authority Notification, Usage and Reporting Requirements for General Purpose, Categorical and Special Purpose Space Delegations*.

This policy establishes a uniform, Departmentwide framework for accounting treatment of VA's capital lease liabilities. The policy outlines the parameters by which each of VA's Administrations and staff offices should capture, record and report their capital lease liabilities to ensure VA meets audit and financial reporting requirements.

VA uses four criteria for identifying capital leases. Refer to section 180501 for discussion of the criteria. The criteria for identifying capital leases for financial reporting purposes differ from the Office of Management and Budget (OMB) criteria for budget scoring of leases described in OMB Circular No. A-11, *Preparation and Submission of Budget Estimates*. OMB provides four additional criteria which relate to the level of private sector risk involved in a lease-purchase agreement. This is necessary because, for budget purposes, there is a distinction between lease-purchases with more or less risk. This distinction is not made, however, in financial reports. Therefore, the Financial Accounting Standards Advisory Board (FASAB) does not include the four criteria related to risk levels as part of the criteria for determining when a lease is a capital lease type. OMB Circular A-11 also discusses the distinctions between capital leases, operating leases and lease purchase agreements.

180101 RECOGNITION OF CAPITAL LEASE LIABILITIES. VA will recognize a lease as a capital lease if, at its inception, it meets one or more of the criteria described in section 180501.

180102 ACCOUNTING AND RECORDING CAPITAL LEASE LIABILITIES. SFFAS No. 5, *Accounting for Liabilities of the Federal Government* and SFFAS No. 6, *Accounting for Property, Plant and Equipment*, provide guidance for determining and reporting liabilities and accounting for property plant and equipment.

180103 FINANCIAL REPORTING AND DISCLOSURE FOR CAPITAL LEASE LIABILITY. OMB Circular A-136 mandates required financial reporting and disclosure of capital leases.

1802 POLICIES

180201 RECOGNITION OF CAPITAL LEASE LIABILITIES.

VA will recognize a lease transaction as a capital lease if, at its inception, it meets one or more of the criteria described in section 180501.

180202 ACCOUNTING AND RECORDING CAPITAL LEASE LIABILITIES.

A. VA may enter into a lease agreement to acquire real or personal property as an alternative to outright purchase.

B. VA will ensure that the purchase price of the General Property, Plant and Equipment (G-PP&E) acquired through a capital lease arrangement satisfies VA's capitalization criteria¹.

C. VA, as the lessee under a capital lease, will record an amount equal to the net present value of rental and other minimum lease payments during the lease term, excluding certain costs paid by the lessor.

180203 FINANCIAL REPORTING AND DISCLOSURE FOR CAPITAL LEASE LIABILITY.

VA will adhere to the reporting and disclosure requirements in OMB Circular A-136, which include reporting capital lease liabilities as "Other Public Funded Liabilities."

1803 AUTHORITY AND REFERENCE

[180301 Statement of Federal Financial Accounting Standards \(SFFAS\) No. 5, Accounting for Liabilities of the Federal Government](#)

[180302 SFFAS No. 6, Accounting for Property, Plant and Equipment](#)

[180303 Office of Management and Budget \(OMB\) Circular A-11, Preparation, Submission and Execution of the Budget](#)

[180304 OMB Circular A-94, Guidelines and Discount Rates for Benefit Cost Analysis of Federal Programs](#)

[180305 OMB Circular A-136, Financial Reporting Requirements](#)

[180306 Department of the Treasury, United States Standard General Ledger \(USSGL\), Approved Scenarios - Leases](#)

¹ Refer to Volume V, Chapter 9, *General Property, Plant and Equipment*, for VA's capitalization criteria.

[180307 General Services Bulletin 2008-B1, Delegation of Lease Acquisition Authority Notification, Usage and Reporting Requirements for General Purpose, Categorical and Special Purpose Space Delegations](#)

1804 ROLES AND RESPONSIBILITIES

180401 The Assistant Secretary for Management/Chief Financial Officer (CFO) oversees all financial management activities relating to the Department's programs and operations, as required by the Chief Financial Officers Act of 1990 and 38 U.S.C. 309. Specific responsibilities include the direction, management and provision of policy guidance and oversight of VA's financial management personnel, activities and operations. The CFO establishes financial policy, systems and operating procedures for all VA financial entities and provides guidance on all aspects of financial management.

180402 Under Secretaries, Assistant Secretaries, Chief Financial Officers, Finance Officers, Chief Accountants and other key officials are responsible for ensuring compliance with the policies and procedures set forth in this chapter.

180403 The Office of Asset Enterprise Management (OAEM) provides oversight in the capital asset arena and ensures a consistent and cohesive Department approach to capital asset management. OAEM serves as the principal policy office and business advisor regarding the acquisition, management and disposal of all VA capital assets. OAEM works collaboratively with all areas of the Department to ensure capital investments are based on sound business practices and principles and, most importantly, meet our Veterans' health care, benefits and burial needs.

180404 The Office of Construction & Facilities Management (CFM) provides design, major construction and lease project management, design and construction standards and historic preservation services. CFM acquires fee-simple or lesser (including easements, licenses, permits and leases) interest in real property, provides guidance for real property lease projects, executes procurement for some of the real property lease projects, executes all VA major construction, is responsible for financial execution of major construction projects, transfer of disbursement authority for minors and reports to the Executive Director, Office of Acquisition, Logistics and Construction. CFM maintains a major construction working reserve account for each Administration, from which funds may be used to finance, in part, the construction, alteration, extension and improvement of any of the facilities under the jurisdiction of VA or for any of the purposes set forth in various sections of Title 38 of the United States Code.

1805 PROCEDURES

180501 RECOGNITION OF CAPITAL LEASE LIABILITIES.

Capital leases are leases that transfer substantially all the benefits and risks of ownership to the lessee. If, at its inception, a lease meets one or more of the following four criteria, it should be recognized as a capital lease by VA:

- A. The lease transfers ownership of the property to VA by the end of the lease term.
- B. The lease contains an option for VA to purchase the leased property at a bargain price.
- C. The lease term is equal to or greater than 75 percent of the estimated economic life of the leased property.
- D. The net present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equals or exceeds 90 percent of the fair value of the leased property.

NOTE: The last two criteria are not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property. If a lease does not meet at least one of the above criteria it should be classified as an operating lease.

180502 ACCOUNTING AND RECORDING CAPITAL LEASE LIABILITIES.

- A. VA may enter into a capital lease agreement for either real or personal property. The responsible Finance Activity will enter data on capital leases into the VA financial accounting system.
- B. VA may acquire General Property, Plant and Equipment (G-PP&E) under a capital lease on an installment plan and the purchase price must satisfy VA's capitalization criteria. VA will record an asset (leased real property or equipment) and a liability (lease obligation) equal to the net present value of the minimum lease payments over the life of the lease term and will record depreciation for the asset over the economic life of the asset. See Appendix A for discussion of budget object codes to use for capital lease transactions. For budgetary purposes, the total costs of a capital lease will be obligated in the year the lease is awarded.
 - Generally, the cost of G-PP&E acquired under a capital lease will equal the amount recognized as a liability for the capital lease at its inception.
 - If the amount so determined above, however, exceeds the fair value of the leased property at the inception of the lease, the amount recorded as the liability should be the fair value.

- If the portion of the minimum lease payments representing executory costs is not determinable from the lease provisions, the amount should be estimated.

C. When VA is the lessee under a capital lease, VA will record an amount equal to the present value of the rental and other minimum lease payments during the lease term, excluding that portion of the payments representing executory cost to be paid by the lessor.

- The discount rate to be used in determining the present value of the minimum lease payments ordinarily would be VA's incremental borrowing rate unless (1) it is practicable for VA to learn the implicit rate computed by the lessor and (2) the implicit rate computed by the lessor is less than VA's incremental borrowing rate. If both of these conditions are met, VA shall use the implicit rate. VA's incremental borrowing rate will be the Treasury borrowing rate for securities of similar maturity to the lease term.

- During the lease term, each minimum lease payment should be allocated between a reduction of the capital lease liability and interest expense so as to produce a constant periodic rate of interest on the remaining balance of the liability. The effective interest method will be used to allocate the rental payments between principal and interest.

180503 FINANCIAL REPORTING AND DISCLOSURE FOR CAPITAL LEASE LIABILITY.

Per OMB Circular No. A-136, VA will report capital lease liabilities as "Other Public Funded Liabilities" in Note 14 of the quarterly and annual financial statements. When VA is the lessee, OMB Circular No. A-136 requires that VA discloses:

A. Any future known commitment for capital leases for real property and equipment will be based on leases in effect as of September 30.

B. A Summary of Assets under Capital Lease. This will show the gross assets under capital lease, by major asset category and the related total accumulated amortization.

C. A Description of Lease Arrangements. This will include the Department's funding commitments including, but not limited to, the major asset categories and associated lease terms, including renewal options, escalation clauses, contingent rentals restrictions imposed by lease agreements and the amortization period.

D. Future Payments Due. VA will project anticipated future costs for the ensuing five years.

1806 DEFINITIONS

180601 Bargain-Purchase Price Option. A lease in which the lessee has the option to buy the underlying asset at less than its fair market value at the end of the lease.

180602 Budget Object Code (BOC). Categories in a classification system that present obligations by the items or services purchased by the Federal Government.

180603 BOC 3160. Equipment Acquired Under Lease Purchase Contracts -- Capitalized. Includes principal payment under capital leases, leases for purchases of ADP equipment and leases for telecommunications equipment that costs \$100,000 or more.

180604 BOC 3161. Equipment under Capital Lease Purchase Contracts – Non-Capitalized. Includes principal payments under capital leases, leases for purchases of ADP equipment and leases for telecommunications equipment that costs under \$100,000.

180605 BOC 3222. Land, Building and Other Structures Acquired Under Lease Purchase Contracts – Capitalized. Includes principal payments under capital lease.

180606 BOC 3224. Buildings Under Capital Lease – Non-Capitalized. Buildings and other structures acquired under lease purchase contracts-non-capitalized.

180607 Capital Leases. Leases are installment purchases and will be recorded and capitalized when the purchase price satisfies the Department's capitalization criteria. Capital leases transfer substantially all the benefits and risks of ownership to the lessee. A capital lease may be for real or personal property. The amount to be capitalized is the amount recognized as a liability for the capital lease. A lease satisfying any one of the following criteria will be recorded as a capital lease: (1) the lease transfers ownership of the property to the Department by the end of the lease term; (2) the lease contains an option for VA to purchase the leased property at a bargain price; (3) the lease term is equal to or greater than 75 percent of the estimated economic life of the leased property; (4) the present value of rental and other minimum lease payments equals or exceeds 90 percent of the fair market value of the leased property. Leases not satisfying one of the four descriptions will be classified as operating leases and will not be capitalized. The last two criteria are not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property.

Per SFFAS No. 6, the cost of general property, plant and equipment acquired under a capital lease is equal to the amount recognized as a liability for the capital lease at its inception (i.e., the net present value of the minimum lease payments over the term of the asset unless the net present value exceeds the fair value of the asset. If the net present value exceeds the fair value of the asset at the inception of the lease, the amount recorded as the liability should be the fair value).

180608 Capital Lease Liability. The present value of liabilities for assets acquired under a lease agreement that meets the test for capitalizing the assets.

180609 Estimated Economic Life of Leased Property. The estimated remaining period during which the property is expected to be economically usable by one or more users, with normal repairs and maintenance, for the purpose for which it was intended at the inception of the lease, without limitation by the lease term.

180610 Executory Costs. Costs excluded from minimum lease payments. The lessee reimburses the lessor for the lessor's expense payments. Examples are insurance, taxes and maintenance.

180611 Fair Value. The price for which an asset could be bought or sold at an arm's-length transaction between unrelated parties (e.g., between a willing buyer and a willing seller).

180612 Lease. The lease is a contractual agreement between the lessor and the lessee, which gives the lessee the right to use specific property. The lease agreement specifies the duration of the lease and rental payments and the obligations for items such as insurance and maintenance which may be assumed by the lessor or the lessee.

180613 Lease Liability. This is an SGL liability account maintained to show the amount of liability for the net present value of minimum lease payments for a capital lease agreement.

180614 Liability. A probable future outflow or other sacrifice of resources as a result of past transactions or events.

180615 Minimum Lease Payments. From the lessee perspective, this includes all lease payments that are required to be made, may be required to be made or, in all probability, will be made to the lessor per the lease agreement. Minimum lease payments for the lessee include, but are not limited to, the lease payments (excluding executory costs) during the non-cancelable lease term, bargain purchase options and any put options, the amount of any lessee residual guarantees and nonrenewal penalties that are insufficiently severe to cause renewal.

180616 Non-Federal Liabilities. These liabilities arise from transactions of an agency of the Federal Government with non-Federal entities. Non-Federal liabilities are claims against the agency by non-Federal entities.

180617 Present Value. The discounted monetized value of the expected asset.

180618 Put Option. In a lease transaction, a put option is the lessor's right to force the lessee to purchase the asset at a predetermined price at the end of the lease term.

1807 RESCISSIONS

None required.

1808 QUESTIONS

Questions concerning these financial policies and procedures should be directed as shown below:

VHA

VBA

All Others

VHA Accounting Policy (Outlook)

VAVBAWAS/CO/FINREP (Outlook)

OFP Accounting Policy (Outlook)

APPENDIX A

BUDGET OBJECT CODES AND ACCOUNTING TRANSACTIONS

A. BUDGET OBJECT CODES (BOC). VA components authorized to enter into capital lease agreements will treat the transaction as an acquisition of a capital asset and the incurrence of a liability.

For equipment, the responsible Finance Activity will enter the capital lease obligation data under BOC 3160, *Equipment Acquired Under Lease Purchase Contracts – Capitalized* or BOC 3161, *Equipment under Capital Lease Purchase Contracts – Non-Capitalized*. For buildings and other structures, the responsible Finance Activity will enter the capital lease obligation under BOC 3222, *Land, Building and Other Structures Acquired Under Lease Purchase Contracts – Capitalized* or BOC 3224, *Buildings Under Capital Lease – Non-Capitalized*. For budgetary purposes, the total costs of a capital lease will be obligated in the year the lease is awarded.

B. ACCOUNTING TRANSACTIONS. The Department of the Treasury Financial Management Service (Treasury), provides Governmentwide accounting and reporting services. This includes gathering and publishing Governmentwide financial information that is used in establishing fiscal and debt management policies. Treasury has published an approved scenario for agencies to use in recording and reporting capital leases.

According to Treasury, the Capital Lease Liability (Account 2940) is used to record the liability incurred for capital leases entered into pursuant to legislative authority. Illustrated below are the entries used to establish the asset and liability accounts to record the capital lease arrangement. Sources for entries to this account include lease agreements and disbursement vouchers.

VA PROFORMA ENTRIES FOR ACCOUNT 2944 – LEASE LIABILITY

A. Recording the value of leased property:

Dr 1811 Equipment Under Capital Lease	XXX	
Dr 1812 Building Under Capital Lease	XXX	
Cr 2944 Lease Liability		XXX

B. Recording payments on capital leases:

Dr 2944 Lease Liability	XXX	
Cr 1021 224 Disbursements		XXX