Leases – Technical Update
Tom Keefe, Partner
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Most leases on balance sheet for lessees

Classification will drive expense profile

Lessor model implications

Most changes result from alignment with ASC 606

FASB tried to make things easy

Classification, reassessment, transition

Effective 2019, but don’t wait to assess impact

Process and systems changes may be required

Potential impact on debt covenants
Review of ASC 842
Effective date and transition

**Effective date**
- **Public business entities** — effective for periods beginning after December 15, 2018 and interim periods therein (calendar 2019)
- **All other entities** — effective for periods beginning after December 15, 2019, and interim periods thereafter (calendar 2020)
- Early adoption is permitted

**Transition**
- Lessees and lessors are required to use a modified retrospective transition method for all existing leases
- Application of method linked to current lease classification and new lease classification
- Guidance in ASU 2016-02 requires that the new model be applied and reflected as of the earliest year presented in the financial statements

**Alternative Transition Approach**
Board tentatively approved an alternative, but optional, transition approach:
- If elected, only contracts that exist as of or that are entered into on or after the effective date would be transitioned, with a cumulative effect adjustment as of that date
- All comparative periods prior to the effective date will retain the financial reporting and disclosure requirements of ASC 840

FASB issued a proposed ASU on January 5, 2018
*Final ASU expected in Q2 2018*
Definition of a lease
What is a lease under ASC 842?

A lease is a contract, or part of a contract, that **conveys the right to control the use** of identified property, plant, or equipment for a period of time in exchange for consideration.

Depend on the use of an identified asset

- Asset may be **explicitly** or **implicitly** specified
- Physically distinct part of larger asset may be an identified asset
- Substitution rights must be considered if substantive [based on practical ability + economic benefit to substitute]
- Warranty or upgrade considerations **do not** impact the determination of whether an identified asset exists

Convey the right to control the use

- Right to obtain substantially all of the economic benefits from asset use (**directly or indirectly**)
- Right to direct the use of the asset throughout the period of use, which is based on:
  - The customer having the ability to direct the “how and for what purpose” the asset is used throughout the period of use
  - The relevant decisions about how and for what purpose the asset is used are predetermined and either (1) the customer operates the asset or (2) the customer designed the asset that predetermines how it will be used over the period of use.
**Mini case study – Identified asset**

<table>
<thead>
<tr>
<th>Background</th>
<th>Considerations</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Does this agreement contain an identified asset?</strong></td>
<td>1. Does the agreement contain an identified asset?</td>
</tr>
<tr>
<td>Company A owns a storage facility with total storage capacity of 10 Bcf. Company B enters into a 5-year agreement to store up to 5 Bcf of natural gas.</td>
<td>2. What if Company A were allowed to move Company B gas to other tanks?</td>
</tr>
<tr>
<td>For purposes of this example assume the following:</td>
<td>Assume Company B gas would not be commingled and he would get it upon extraction.</td>
</tr>
<tr>
<td>• Company A’s storage capacity is based on 10 – 18cf tanks</td>
<td></td>
</tr>
<tr>
<td>• The agreement specifies that Company B will have exclusive use of tanks 1 – 5.</td>
<td></td>
</tr>
</tbody>
</table>

Yes. Company B has use of specified tanks.
## Definition of a lease

### Mini case study – Right to control the use

### Background

Company A owns one wind generating facility. Company A enters into a 10-year PPA to provide energy from the facility to Company B.

For purposes of this example assume the following:

- Company A retains ITCs which represent 20% of the value associated with facility.
- Company B has exclusive rights to all of the output of the facility (power and RECs)
- Assume that at the commencement of the PPA, the price of power in the PPA is 10% lower than the market price

### Considerations

<table>
<thead>
<tr>
<th>Does Company B have the right to substantially all the economic benefits?</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Does the retention of ITCs impact the analysis?</td>
</tr>
<tr>
<td>2. Does the price of market power matter in determining the economic benefits?</td>
</tr>
</tbody>
</table>

Yes. Company B receives all the outputs. Contract pricing does not have any bearing on economic benefits of the asset.
## Background

### Who has the right to direct the use of the asset?

Company A owns one natural gas generating facility. Company A enters into a 10-year PPA to provide energy from the facility to Company B.

For purposes of this example assume the following:

- Company B has exclusive rights to all of the output of the facility
- Company A will provide operations management services (i.e. they will operate the plant)
- Company B may choose to run the plant as necessary to serve its needs
- The PPA stipulates that one month of each year, Company A may take the plant offline to perform O&M work

## Considerations

1. Does Company A’s provision of operations management services give Company A the right to control?

2. Does Company A’s right to perform O&M work one month of the year have any bearing on control?

**Bonus Question:** Assuming the PPA is determined to be a lease, how should the parties account for the operations management services component of the arrangement?

Company B. Although Company B has operating responsibilities, Company B makes relevant decisions about HAFWP (when the plant will operate).
Lessee accounting model
What does the lessee model look like?

Most* leases are recorded on the balance sheet using a right-of-use asset approach.

### Initial measurement
- **Lease obligation** — PV of lease payments not yet paid
- **ROU asset** — lease obligation + initial direct costs – lease incentives + prepaid lease payments

### Subsequent measurement
- **Lease obligation** — amortized using the effective interest method
- **ROU asset** — depends upon lease classification
- Expense recognition pattern:
  - Finance lease — front-loaded
  - Operating lease — generally straight-line

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* Short-term leases: A lessee can elect, by asset class, not to record on its balance sheet a lease with a lease term of 12 months or less and that does not include a purchase option that the lessee is reasonably certain to exercise.
What does the lessor model look like?

**Lessor accounting model**

- Most changes result from alignment with ASC 606
- Classification depends on an assessment of control of the underlying asset

*Title transfer no longer required for real estate*

### Sales-type
- Lessee gains control of the underlying asset
- Underlying asset is derecognized
- Net investment in a lease is recognized
- Selling profit or loss recognized at lease commencement
- Initial direct costs recognized at lease commencement unless no selling profit or loss

### Direct financing
- Lessee does not obtain control of the asset, but the lessor relinquishes control
- Underlying asset is derecognized
- Net investment in a lease is recognized
- Profit deferred and amortized into income over the lease term
- Initial direct costs deferred and amortized into income over the lease term

### Operating
- Lessor retains control of the underlying asset
- Underlying asset remains on the lessor’s balance sheet
- Income recognized on a straight-line basis unless another systematic basis is more appropriate
- Initial direct costs deferred and expensed over the lease term in a manner consistent with income
### Presentation requirements

<table>
<thead>
<tr>
<th>Financing lease</th>
<th>Operating lease</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Lessor model</strong></td>
<td></td>
</tr>
<tr>
<td>Presentation consistent with current lessor model:</td>
<td></td>
</tr>
<tr>
<td>• <strong>Balance sheet</strong> — presentation depends on lease classification</td>
<td></td>
</tr>
<tr>
<td>• <strong>Income statement</strong> — profit or loss recognized in a manner consistent with business model</td>
<td></td>
</tr>
<tr>
<td>• <strong>Cash flow statement</strong> — recognized as cash inflows from operating activities</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lessee model</th>
<th>Income statement</th>
<th>Cash flow statement</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Balance sheet</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROU asset</td>
<td>Amortization expense</td>
<td>Principal (Financing)</td>
</tr>
<tr>
<td>Lease liability</td>
<td>Interest expense</td>
<td>Interest (Operating)</td>
</tr>
<tr>
<td><strong>Income statement</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROU asset</td>
<td>Lease expense (single line on straight-line basis)</td>
<td>Lease payments (Operating)</td>
</tr>
<tr>
<td>Lease liability</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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Disclosure requirements

**Disclosure objective** — Enable financial statement users to assess the amount, timing, and uncertainty of cash flows arising from leases

<table>
<thead>
<tr>
<th>Lessee disclosures</th>
<th>Lessor disclosures</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Nature of its leases</td>
<td>• Nature of its leases</td>
</tr>
<tr>
<td>• Information about leases that have not yet commenced</td>
<td>• Significant assumptions and judgments used</td>
</tr>
<tr>
<td>• Related-party lease transactions</td>
<td>• Related-party leases transactions</td>
</tr>
<tr>
<td>• Accounting policy election regarding short-term leases</td>
<td>• Tabular disclosure of lease-related income</td>
</tr>
<tr>
<td>• Finance and operating lease costs</td>
<td>• Components of the net investment in a lease</td>
</tr>
<tr>
<td>• Short-term and variable lease costs</td>
<td>• Information on the management of risk associated with residual asset</td>
</tr>
<tr>
<td>• Sublease income</td>
<td>• Maturity analysis of operating lease payments and lease receivable</td>
</tr>
<tr>
<td>• Gain or loss from sale-and-leaseback</td>
<td>• Information required by ASC 360 (PP&amp;E)</td>
</tr>
</tbody>
</table>
Accounting policy considerations
Companies can use a reasonable capitalization threshold when applying the recognition guidance under ASC 842

Do not default to existing PP&E capitalization thresholds

- Existing threshold does not incorporate:
  - Effect of additional asset base
  - Liability recognition
- Reasonable approaches include:
  - Capitalization threshold set as the lesser of:
    - Capitalization threshold for PP&E, inclusive of ROU assets
    - Recognition threshold for liabilities, inclusive of lease liabilities
  - Recognize all lease liabilities, but, subject to threshold, expense amounts associated with the ROU asset
- Choose one approach, apply consistently, and consider disclosures

Basis for Conclusions
Paragraph BC122: “Entities will likely be able to adopt reasonable capitalization thresholds below which lease assets and lease liabilities are not recognized...”
### Illustrative example

<table>
<thead>
<tr>
<th>Key facts</th>
<th>Lessee considers the following to identify a threshold for its leases</th>
</tr>
</thead>
</table>
| - Lease of a machine  
- Lease term: 5 years  
- ROU asset = $3,260  
- Lease liability = $3,260 | - Gross balances of its ROU assets ($3,260) and lease liabilities ($3,260)  
- Disclosures that would be omitted if certain leases were not recognized  
- Internal controls needed to apply and monitor the threshold  
- Materiality considerations in SAB Topic 1.M |

#### “Lesser of” approach
- Threshold for PP&E, including ROU assets = $3,500  
- Threshold for liabilities, including lease liabilities = $3,000  
- ROU asset and lease liability ($3,260) > recognition threshold for liabilities ($3,000, the lower of the two)  
- **Lessee should recognize the ROU asset and lease liability**

#### “Recognize all liabilities” approach
- Threshold for PP&E, including ROU assets = $3,500  
- ROU asset ($3,260) < capitalization threshold for PP&E ($3,500)  
- **Lessee should expense amounts associated with the ROU asset**  
- **Lessee should recognize the lease liability**
**Accounting policy considerations**

**What options are available?**

Below is a summary and description of various accounting policy alternatives that are available for preparers:

<table>
<thead>
<tr>
<th>Topic</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Comparatives under ASC 840 option</strong></td>
<td>An entity may elect not to present 2 years of comparative financial statements and adopt the standard using a cumulative catch-up approach similar to the cumulative catch-up approach provided under the new revenue guidance.</td>
</tr>
<tr>
<td><strong>Package of three (Transition practical expedient)</strong></td>
<td>An entity may elect not to reassess: ▪ whether expired or existing contracts contain leases under the new definition of a lease; ▪ lease classification for expired or existing leases; and ▪ whether previously capitalized initial direct costs would qualify for capitalization under Topic 842.</td>
</tr>
<tr>
<td><strong>Use of hindsight (Transition practical expedient)</strong></td>
<td>Hindsight is allowed when considering the likelihood that lessee options to extend or terminate a lease or purchase the underlying asset will be exercised, and in assessing the impairment of ROU assets. ▪ Elect on its own or with the package of practical expedients.</td>
</tr>
<tr>
<td><strong>Short-term lease exemption</strong></td>
<td>As an accounting policy, a lessee may elect not to apply the recognition requirements in ASC 842-20 to short-term leases. Instead, a lessee may recognize the lease payments in profit or loss on a straight-line basis over the lease term and variable lease payments in the period in which the obligation for those payments is incurred.</td>
</tr>
<tr>
<td><strong>Lessor nonlease component separation practical expedient (proposed)</strong></td>
<td>As a practical expedient, a lessor may elect not to separate nonlease components from the lease components in the arrangement provided certain criteria are met. ▪ Subsequent accounting of the combined components depends on significance of the lease and nonlease components.</td>
</tr>
<tr>
<td><strong>Portfolio approach</strong></td>
<td>ASC 842 may be applied on a portfolio basis to similar leases if the entity reasonably expects that the outcome will not differ from applying the standard to the individual leases.</td>
</tr>
</tbody>
</table>
Proposed “alternative” transition approach
Comparatives under ASC 840 option

Transition guidance requires that entities recognize the effects of applying ASC 842 as a cumulative effect adjustment to retained earnings as of the date of initial application.

Modified retrospective transition:
- Date of initial application = beginning of the earliest period presented
  - Recast comparative periods
  - Apply ASC 842 to lease activity during the comparative periods

Transition requirements as originally included in ASU 2016-02

1/1/2017
Earliest period presented

1/1/2019
Effective date and date of initial application

^Assuming a calendar-year end PBE
Transition guidance requires that entities recognize the effects of applying ASC 842 as a cumulative effect adjustment to retained earnings as of the **date of initial application**.

**Modified retrospective transition**
- Date of initial application = **beginning of the earliest period presented**
  - Recast comparative periods
  - Apply ASC 842 to lease activity during the comparative periods

**Comparatives under ASC 840 option**
- Date of initial application = **effective date**
  - Do not recast comparative periods
  - Provide ASC 840 disclosures during comparative periods (including MLP footnote)

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1. Assuming a calendar-year end PBE

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1/1/2017
Earliest period presented

1/1/2019
Effective date\(^1\) and date of initial application

Comparative periods under ASC 840
Transition practical expedients
Package of three

ASC 842-10-65-1(f)

An entity may elect the following practical expedients, which must be elected as a package and applied consistently by an entity to all of its leases (including those for which the entity is a lessee or a lessor), when applying the pending content that links to this paragraph to leases that commenced before the effective date:

1. An entity need not reassess whether any expired or existing contracts are or contain leases.
2. An entity need not reassess the lease classification for any expired or existing leases (for example, all existing leases that were classified as operating leases in accordance with Topic 840 will be classified as operating leases, and all existing leases that were classified as capital leases in accordance with Topic 840 will be classified as finance leases).
3. An entity need not reassess initial direct costs for any existing leases. . .

Identified errors may not be carried forward

In applying the practical expedient in ASC 842-10-65-1(f)(1), entities may not carry forward any previous “errors” (i.e., incomplete identification of leases). In certain circumstances, for example, an entity may not have previously identified contracts that met the definition of a lease under ASC 840.
Transition practical expedients (cont.)
Use of hindsight

ASC 842-10-65-1(g)
An entity also may elect a practical expedient, which must be applied consistently by an entity to all of its leases (including those for which the entity is a lessee or a lessor) to use hindsight in determining the lease term (that is, when considering lessee options to extend or terminate the lease and to purchase the underlying asset) and in assessing impairment of the entity’s right-of-use assets.

Use of hindsight may increase complexity
While the election of hindsight may result in a more accurate reflection of the measurement of ROU assets and liabilities in transition, it may introduce a certain level of complexity...

• Since hindsight directly affects the lease term, the inclusion of additional periods in the lease term may affect straight-line rent calculations as well as the measurement of lease liabilities.
• Because an entity will need to apply the practical expedient to all of its leases and consider events and circumstances impacting lease term up to the effective date of the new standard, it may add an additional level of complexity.
Accounting policy considerations

Short-term lease exemption

ASC 842-20-25-2

As an accounting policy, a lessee may elect not to apply the recognition requirements in this Subtopic to short-term leases. Instead, a lessee may recognize the lease payments in profit or loss on a straight-line basis over the lease term and variable lease payments in the period in which the obligation for those payments is incurred (consistent with paragraphs 842-20-55-1 through 55-2). The accounting policy election for short-term leases shall be made by class of underlying asset to which the right of use relates.

The short-term lease exemption is...

• Only available for lessees (i.e., lessors cannot apply short-term lease exemption)
• Election made by class of underlying asset
• Can **not** be elected if the lease includes a purchase option that is reasonably certain of being exercised
• Should **not** be applied for leases in transition that have an original term of greater than 12 months, but have a remaining term of 12 months or less

*Not an industry-specific issue, but of high-interest based on discussions at the EEI/AGA lease training*
At its March 28 meeting, the FASB discussed the proposed ASU on an optional practical expedient for lessors:
Reaffirmed that a lessor *would not* be required to separate lease and nonlease components when certain conditions are met:

- The timing and pattern of transfer of the lease and nonlease components are the same
- The lease component, if accounted for separately, would be classified as an operating lease

Agreed to remove the proposed ASU requirement that a lessor always account for the combined component as a lease under ASC 842:

- Lessor should consider the magnitude of the nonlease component(s) to determine whether the combined component should be accounted for under ASC 842 or ASC 606
- Lessor should account for the combined component under ASC 606 if the nonlease component(s) is the predominant component in the combined component

“Big Service” versus “Little Lease” considerations
As a practical expedient, a lessee may, as an accounting policy election by class of underlying asset, choose not to separate nonlease components from lease components and instead to account for each separate lease component and the nonlease components associated with that lease component as a single lease component.

ASC 842-10-15-37

Additional considerations when applying this practical expedient...

Electing this practical expedient will result in all consideration and variable lease payments being allocated to the lease component:

- Will generally result in a higher lease liability and right-of-use asset
- May impact lease classification as there will be higher lease payments that will be considered when performing the present value classification test
“Hot Topics” impacting the industry
Sales-type or direct financing lease with significant variable payments may result in lessor recognizing a loss at commencement

- Net investment in the lease does not include variable lease payments
- If net investment < carrying amount of leased asset, a loss is recognized

*A book loss, but not an economic loss*

Examples of arrangements that may be affected:

- Renewable energy (e.g., wind or solar) power purchases
- Oil and gas gathering and processing
- Retail real estate
- Medical devices with consumables

FASB considered, but ultimately rejected, possible solutions:

1. Including variable lease payments in measurement of net investment subject to a constraint (by reference to ASC 606)
2. Negative discount rate

FASB clarified to use a zero discount rate
Industry “hot topics”
Design considerations for renewable PPAs

Defining the issue...

• *How and for what purpose* decisions often predetermined
• Asset owner typically responsible for O&M
• Need to evaluate whether the customer designed the asset in a way that predetermines the most relevant decisions about how and for what purpose

Questions to be addressed...

• What types of involvement by the purchasing party will be deemed to constitute design of the asset?
  ➢ Specifying the site?
  ➢ Specifying the technology?
  ➢ Specifying the configuration and layout?
  ➢ Combination of factors?

*All three must be present to satisfy design?*
Industry “hot topics”
Easements and right of ways

**Standard-setting on this topic:**

- FASB issued ASU 2018-01 in January 2018
- ASU provides for the following:
  - As a practical expedient, existing easements are not subject to ASC 842 unless already **accounted for** as leases under ASC 840
  - New or modified easements after adoption of ASC 842 should be **assessed** under ASC 842
  - Amends an example in ASC 350 (clarifies that ASC 842 must be applied first)

- ASU **does not**:
  - Provide guidance on accounting for easements that are not leases
  - Provide guidance on assessing easements under ASC 842
    (e.g., guidance on assessing unit of account, economic benefits, etc.)

*FASB reiterated at a board meeting that the unit of account for easements is an area of judgment. We believe that there are acceptable alternatives and expect to see diversity in practice.*
Industry “hot topics”
Easements and right of ways (cont.)

Under ASC 842, key considerations should include:

- What is the term of the agreement?
  - Perpetual vs. stated term

- What is the proper unit of account?
  - Discrete pieces of land versus larger plot
  - Surface vs sub-surface

- Economic benefits?
  - Is the land being otherwise used for economic purposes?
  - Do you need to think about viable alternative uses for the land?

- What constitutes control?
  - Shared use arrangement?
  - May the easement holder restrict the landowners use (e.g. fence in)?


Industry “hot topics”
Easements and right of ways (cont.)

<table>
<thead>
<tr>
<th>Background</th>
<th>Considerations</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Does this agreement contain a lease?</strong></td>
<td></td>
</tr>
<tr>
<td>Turbines Inc. enters into an easement agreement with Farmer John to place 20 wind turbines within 10 acres of Farmer John’s farmland.</td>
<td>1. What is the unit of account?</td>
</tr>
<tr>
<td>For purposes of this example assume the following:</td>
<td>2. Who determines the how and for what purpose the land is used?</td>
</tr>
<tr>
<td>• The agreement has a term of 50 years</td>
<td>3. Does the exclusive use clause matter if Turbines Inc. does not restrict access (i.e. does not fence in)?</td>
</tr>
<tr>
<td>• The agreement does not specify the discrete land to be used by the turbines; however once the turbines are erected, they will not be moved</td>
<td></td>
</tr>
<tr>
<td>• The total land used by the 20 wind turbines is not significant</td>
<td></td>
</tr>
<tr>
<td>• The agreement specifies that Turbine’s Inc. has exclusive use of the land on which the turbines are placed; Farmer John may continue to farm on the surrounding land</td>
<td></td>
</tr>
</tbody>
</table>
Industry “hot topics”
Pipeline laterals/Drop lines and meters

LAST MILE SCENARIOS

- Pipeline laterals do meet the definition of an identified asset (ASC 842-10-15-16)
- Lease determination should be based on an ASC 842-10-15-4 control assessment
- Two types of laterals specifically discussed by the Board

<table>
<thead>
<tr>
<th>Type 1</th>
<th>Type 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Not a Lease)</td>
<td>(Meet the Definition of a Lease)</td>
</tr>
</tbody>
</table>

- Connected to an integrated pipeline system and share supply sources with the main line and other customers
- Not capable of operating on their own
- Pipeline owner retains certain rights that provide it the ability to control the use of the lateral

- Can be separately shut off from the main line
- Customer is fully capable of utilizing the lateral using their own dedicated assets
- Customer has the right to substantially all the pipeline lateral’s capacity and has ability to obtain substantially all of the economic benefits from use of the lateral

How does this decision impact electric lines? Meters?
Definition of economic benefits

**Background on the Issue:**

Under ASC 842, a party must take substantially all of the economic benefits of the asset over the contract term to have a lease. 842-10-15-17 specifies that benefits include primary outputs (e.g. electricity) and by-products (e.g. RECs).

**Consideration:**
Can/should tax attributes be considered economic benefits?

**Deloitte View:**
Tax attributes (including PTCs) are *not* economic benefits
- PTCs are based on a combination of ownership and asset performance
- PTCs cannot be sold to third parties
- Therefore, economic benefit is due to **ownership** of the asset, not the **use** of the asset
Industry “hot topics”
Common payments in power purchase agreements ("PPA")

**Guaranteed minimum production**

- Do guaranteed minimum production levels in renewable PPAs represent an in-substance fixed lease payment?

- General consensus that they are not
  - Seller makes payment to buyer for shortfalls and therefore reduces the buyer’s net exposure
  - Buyer’s gross payments for electricity generated not impacted by guaranteed production level
  - Seller can’t guarantee physical production
  - Guarantee protects buyer financially from market purchases necessitated by production shortfalls

**Capacity payments**

- Are capacity payments variable if subject to claw back based on availability (excluded from the measurement of lease obligation)?

- Deloitte view is no (i.e., are fixed):
  - Assume asset will be ready for intended use
  - Plant owner largely controls availability
  - Refund potential should be viewed as negative contingent/variable rent
Industry “hot topics”
Considerations for RTOs/ISOs

Dispatch analysis
Dispatch rights generally convey control because they allow the off-taker to determine when a generating unit produces power

• In a RTO/ISO environment, physical dispatch is technically controlled by system operator... How does this affect the HAFWP analysis?

• What is the most important decision to determining how and for what purpose the generating facility is used?
  - Bid behavior directly impacts when/whether a facility will run
  - Establishing bid may be most relevant HAFWP decision
  - Also consider ability to force dispatch (e.g. must-run designation)
Industry “hot topics”
Lighting as a service

**LIGHTING AS A SERVICE**
Agreement with city or municipality to provide them with street lights and electric service

- In some instances the light fixtures are specifically identified in the contract
- In others the assets themselves may not be explicitly identified
- Would the asset be implicitly identified?

Diversity in practice in how these are accounted for under ASC 840

**Key considerations under ASC 842...**

- Is control conveyed to the customer or is it a shared use scenario?
- What impact, if any, does substitution rights have on the conclusion?
- Are all relevant decisions predetermined (if so, who designed)?

**Industry observations**

- Multiple utilities wanted to discuss this issue
- General consensus was that utility still had “control” of the asset
Industry “hot topics”

Pole attachments

**POLE ATTACHMENTS**
Utilities commonly contract to use space on poles belonging to others or rent out space on their own poles to be used by others

Generally **is not** a lease under today’s ASC 840 requirements

**Key considerations under ASC 842…**

- What is the unit of account (entire pole or location on the pole)?
- What is the impact of shared use (pole designed to host other users)?
- Are there substantive substitution rights?
Industry “hot topics”
Rooftop solar

**ROOFTOP SOLAR**
Residential rooftop as well as solar panels that are placed on commercial or industrial entities

- Customer may buy power under PPA; often have ability to sell back to grid
- Utility may buy power from the supplier

Generally **is a lease** under today’s ASC 840 requirements

**Key considerations under ASC 842...**
- Does the customer control the asset?
- Was the customer involved in the design?
- Could there be an embedded lease of the roof space?
Other key provisions and resources
But wait, there’s more...

- Contract combinations
- Leveraged lease accounting
- Accounting for leases at a portfolio level
- Leases in a business combination
- Impairment considerations
- U.S. GAAP to IFRS comparison
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