



**Audit of Governmental Accounting
Standards Board (GASB)
Statement 87 Implementation**

Project #22-21

Prepared by
Office of the Inspector General

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SOUTH FLORIDA WATER MANAGEMENT DISTRICT

April 13, 2023

Governing Board Members

Re: Audit of Governmental Accounting
Standards Board (GASB) Statement 87
Implementation – *Project No. 22-21*

This audit was performed pursuant to the Inspector General's authority set forth in Chapter 20.055, F.S. Our audit objective primarily focused on assessing whether the requirements of GASB 87 have been adequately addressed to ensure that District leases, as defined by GASB 87, are fairly stated in the District's financial statements for the Fiscal Year Ended September 30, 2022. Jankie Bhagudas and I prepared this report.

Sincerely,

A handwritten signature in blue ink, reading "J. Timothy Beirnes".

J. Timothy Beirnes, CPA
Inspector General

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BACKGROUND

In June 2017 the Governmental Accounting Standards Board (GASB) issued Statement No. 87 (GASB 87), titled Leases. The requirements of GASB were originally effective for reporting periods beginning after December 15, 2019, however; due to the Covid Pandemic the effective implementing date was extended to fiscal years beginning after June 15, 2021. Thus, the South Florida Water Management District's required implementation date is for its fiscal year beginning October 1, 2021 and ending September 30, 2022.

GASB 87 established significant changes in the methods of accounting and financial reporting for leases by lessees and lessors. The requirements of the standard apply to financial statements of all state and local governments. GASB 87 defines a lease as; "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". The standard does not apply to leases of intangible assets, biological assets, and inventory of service concession arrangements. GASB 87 also provides exclusions for some leases such as, short-term leases with terms of 12 months or less, leases for which both the lessee and the lessor have an option to terminate the lease without permission from the other party. The standard also address how option periods are handled in determining whether a lease is excluded.

GASB 87 requires the lessee to treat a lease as a liability and the lessor treat it as an asset. A lessee initially should measure the lease liability at the present value of payments expected to be made during the lease term. The value of the lessee's right to use the property is recognized as an offsetting asset. A number of factors are considered in measuring the present value of the lease payments.

OBJECTIVE, SCOPE, AND METHODOLOGY

The audit assessed whether the requirements of GASB 87 have been adequately addressed to ensure that District leases, as defined by GASB 87, are fairly stated in the District's financial statements for the Fiscal Year Ended September 30, 2022.

Audit procedure included:

- Reviewing and assessing the process for identifying the population of all the District's leases.
- Reviewing the process for assessing lease contract term options, and other criteria, to determine whether the lease meets one of the exclusions specified in GASB 87.
- Reviewing a sample of leases to determine that the agreement terms were accurately captured on the leases inventory.
- Analyzing lease classifications (i.e., long-term or short-term) and whether lease modifications and option probabilities have been adequately addressed as well as any other exclusionary provisions of GASB 87.
- Assessing the reasonableness of the assumptions used in establishing the discount rate used to calculate the net present values (NPVs).
- Recalculated the net present values (NPVs) to determine that NPVs are fairly stated.
- Reviewing a sample of leases to determine that NPVs were calculated in accordance with GASB 87.
- Reviewing a sample of journal entries to determine that leases were properly recorded in the SAP financial system.

The Audit scope did not include reviewing notes to financial statements to determine if they include all the provisions required by GASB 87.

The judgmental sample method was used throughout the audit. Judgmental sampling is considered the preferred methodology based on consideration of the audit population's size and characteristics, as well as audit efficiency and professional judgment. Although the sample cannot be statistically projected to the total population, we believe the sample, along with the results of the audit tests, provide reasonable assurance for us to determine whether adequate internal controls are in place.

The audit was performed in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

AUDIT RESULTS

Executive Summary

Overall, we found that the process developed for reviewing District contract agreements was sufficiently designed to capture the relevant data from District agreements to ensure reasonable assurance of complying with the provisions of GASB 87. Two Guidance Checklists were prepared; one for reviewing agreements where the District is the lessor, and one for where the District is lessee. These Guidance Checklists provided a process for reviewing District agreements to determine whether the agreements were subject to the requirements for GASB 87.

The Projects & Assets Section, within the Finance Bureau, also created two Excel spreadsheets, one for leases where the District is lessor, one where the District is lessee. The spreadsheets provided a tool to capture 26 different data elements from each agreement to determine whether they should be classified as a lease in accordance with the provisions of GASB 87. Thirty-two (32) agreements were analyzed where the District is the lessee, of which seven (7) were determined to be subject to the requirements of GASB 87. Also, 129 agreements were analyzed where the District is the lessor, of which 14 were determined to be subject to the requirement of GASB 87. In total, 161 agreements were analyzed, and 21 were determined to be subject to the provisions of GASB 87.

Audit procedures entailed testing a sample of the agreements contained in each spreadsheet to determine that the data elements were sufficiently captured from the agreements and that each agreement appeared to be properly classified. Audit results indicate that the Lessee Analysis Data Spreadsheet and the Lessor Analysis Data Spreadsheet sufficiently captured the data from lease agreements and that the classification of each agreement appeared appropriate. Also, our recalculation of the lease net present values (NPVs) revealed that they were fairly stated.

Audit procedures also entailed assessing the methodology used to establish the discount rates used for calculating the NPVs. Since District lease agreements rarely, if ever, contain a stated interest rate, the incremental borrowing rate criteria permitted by GASB 87 was used to establish the District's discount rate to calculate NPVs. The

District's financial advisory firm, PFM, prepared a synthetic yield curve showing the District's incremental borrowing rate for each of 20 years terms. The methodology used to establish the discount rates appears reasonable and appropriately reflects the criteria contained in GASB-87. Also, an appropriate expert in the public debt market, PFM, was used to assist in establishing the appropriate incremental borrowing rates.

Implementation Process Sufficiently Captures Agreement Data

Our review of the Guidance Checklists revealed the process developed for reviewing District contract agreements was sufficiently designed to capture the relevant data from District agreements to ensure reasonable assurance of complying with the provisions of GASB 87. The Projects & Assets Section, within the Finance Bureau, prepared a checklist titled Accounting Contract Review Guidance Checklist for GASB 87 Lease Accounting Standard Compliance (the “Guidance Checklists”).

Two Guidance Checklists were prepared; one for reviewing agreements where the District is the lessor, and one for where the District is lessee. These Guidance Checklists provided a process for reviewing District agreements to determine whether the agreements were subject to the requirements for GASB 87. The Guidance Checklists also provided definitions, tables, examples, and other visual aids to assist the agreement reviewers. The relevant data items listed in the guidance checklist were recorded in an Excel spreadsheet in the column number that corresponded with each of the different checklist items. The spreadsheet also included a schedule for the minimum lease payments for each fiscal year for the duration of the lease. A dashboard was used to track the progress of the agreement review process.

Lessee Analysis Data Spreadsheet Sufficiently Captured Agreement Data

The Projects & Assets Section, within the Finance Bureau, prepared a spreadsheet to capture the necessary data elements from each of 32 agreements, where the District is the lessee, to determine whether they should be classified as a lease in accordance with the provisions of GASB 87. The spreadsheet contained a column for 26 different contract elements needed to assess whether the agreements should be classified as a lease under GASB 87. Spreadsheet column 27 contained the conclusion of such assessment. The analysis identified seven (7) of the 32 agreements analyzed that were subject to the requirements of GASB 87. We selected a sample of leases from the Lessee Analysis Data Spreadsheet to determine that the agreement terms were sufficiently captured on the leases inventory and performed the following procedure:

- Analyzed the spreadsheet to determine whether lease modifications and option probabilities were adequately addressed, as well as any other exclusionary provisions of GASB 87.
- Determined whether leases NPV's were calculated in accordance with GASB 87.
- Recalculated the Net Present Values (NPV) to determine that NPV's were reasonably fairly stated.
- Determined whether journal entries were fairly stated and properly entered into the SAP financial system.

The following table contains the results of our audit testing for the 6 agreements selected using the judgmental sampling method.

Lessees – District is Lessee							
No.	Lessor	Lease Classified as GASB-87	Lease Terms Reasonably Captured	Lease Classification Appears Properly Classified	Cash Flows by FY Appear Fairly Stated	PV Calculation Appears Fairly Stated	JE Appear Fairly Stated
4	Optimum Farms Management, LLC	No	Yes	Yes	Yes	NA	NA
6	Lykes Nicodemus Slough	Yes	Yes	Yes	Yes	Yes	Yes
9	XL Ranch Limited Partnership	No	Yes	Yes	Yes	NA	NA
18	Spur Land & Cattle, LLC	No	Yes	Yes	Yes	NA	NA
28	Williamson Cattle Co/300 Plaza, LLC Assigned	Yes	Yes	Yes	Yes	Yes	Yes
31	Federman, LLC	Yes	Yes	Yes	Yes	Yes	Yes
Blue Color = GASB 87 Lease							

We concluded that the Lessee Analysis Data spreadsheet sufficiently captured the data from lease agreements.

Lessor Analysis Data Spreadsheet Sufficiently Captured Agreement Data

The Projects & Assets Section, within the Finance Bureau, prepared a spreadsheet to capture the necessary data elements from each of the 129 lease agreements, where the District is lessor, to determine whether they should be classified as a lease in accordance with the provisions of GASB 87. The spreadsheet contained a column for 26 different contract elements needed to assess whether the agreements should be classified as a lease under GASB 87. Spreadsheet column 27 contained the conclusion of such assessment. The analysis identified 14 of the 129 agreements analyzed that were subject to the requirements of GASB 87. We selected a sample of leases from the Lessee Analysis Data Spreadsheet to determine that the agreement terms were sufficiently captured on the leases inventory and performed the following procedure:

- Analyzed the spreadsheet to determine whether lease modifications and option probabilities have been adequately addressed as well as any other exclusionary provisions of GASB 87.
- Determined whether leases NPVs were calculated in accordance with GASB 87.
- Recalculated the Net Present Values (NPVs) to determine that NPVs were reasonably fairly stated.
- Determined whether journal entries were fairly stated and properly entered into the SAP financial system.

The following table contains the results of our audit testing for the 10 agreements selected using the judgmental sample method.

Lessees – District is Lessor							
No.	Lessee	Lease Classified as GASB-87	Lease Terms Reasonably Captured	Lease Classification Appears Properly Classified	Cash Flows by FY Appear Fairly Stated	PV Calculation Appears Fairly Stated	JE Appear Fairly Stated
10	Vecellio & Grogan Inc.	Yes	Yes	Yes	Yes	NA- Variable lease	NA- Variable lease
12	Gray Media Group F/K/A Raycom National, Inc	Yes	Yes	Yes	Yes	Yes	Yes
14	Old River Cattle Co., LLC	No	Yes	Yes	Yes	NA	NA
30	Marilyn Brady	Yes	Yes	Yes	Yes	Yes	Yes
31	Future Kids of WPB Corp	No	Yes	Yes	Yes	NA	NA
39	Florida DEP	Yes	Yes	Yes	Yes	Yes	Yes
43	New Hope Sugar	Yes	Yes	Yes	Yes	Yes	Yes
49	Clark Cattle, LLC	No	Yes	Yes	Yes	NA	NA
60	PBC / PBSO (Sheriff)	Yes	Yes	Yes	Yes	Yes	Yes
66	PBC-BOCC	No	Yes	Yes	Yes	NA	NA
Blue Color = GASB 87 Lease							

We concluded that the Lessor Analysis Data spreadsheet sufficiently captured the data from lease agreements.

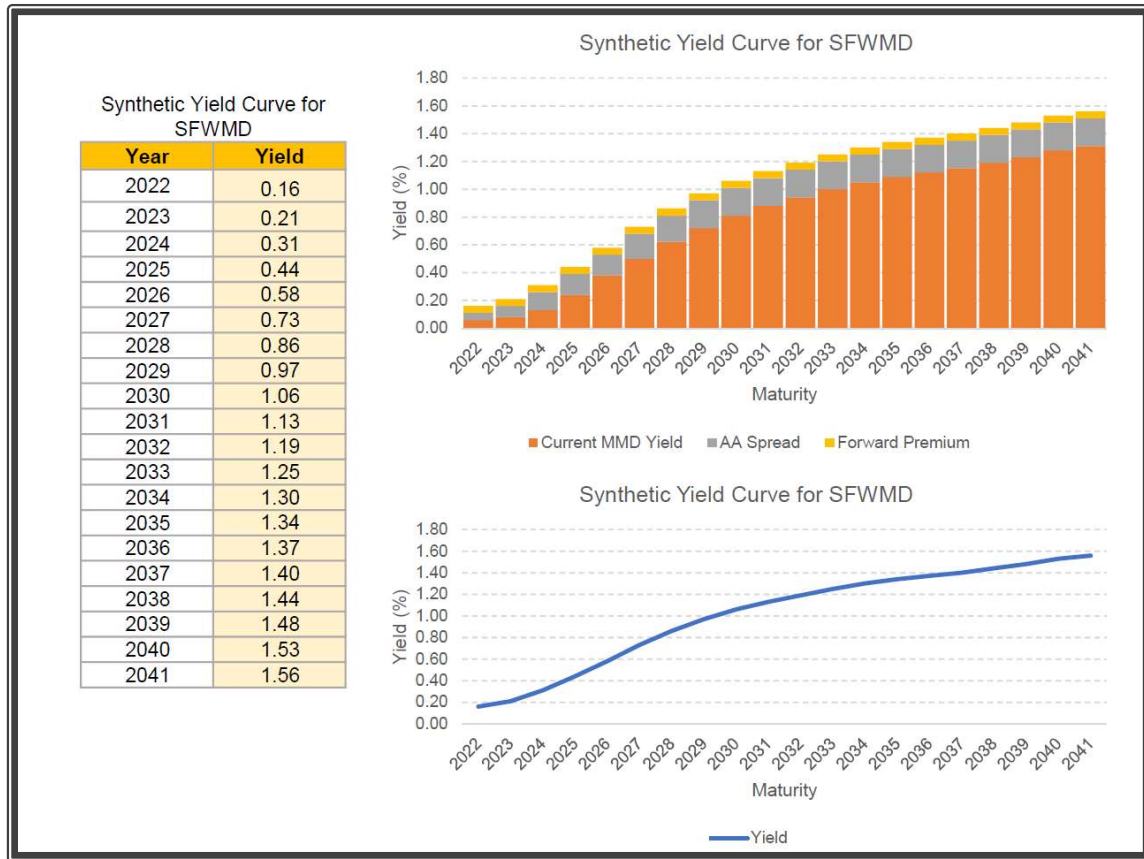
Established Discount Rates Methodology Appears Reasonable

GASB-87, Paragraph 23, specifies the criteria for establishing the appropriate discount rates, which states:

“The future lease payments should be discounted using the interest rate the lessor charges the lessee, which may be the interest rate implicit in the lease. If the interest rate cannot be readily determined by the lessee, the lessee’s estimated incremental borrowing rate (an estimate of the interest rate the would be charged for borrowing the lease payment amounts during the lease term) should be used.”

District lease agreements rarely, if ever, contain a stated interest rate; therefore, the incremental borrowing rate criteria was used to establish the District’s discount rate for leases where the District is lessor. The GASB-87 pronouncement is silent regarding the discount rate to use for leases where the District is lessor; therefore, the reasonable approach was to use the District’s incremental borrowing rate for both lessor and lessee agreements.

The District's financial advisory firm, PFM, prepared a synthetic yield curve showing the District's incremental borrowing rate for each of 20 years terms. The results are shown in the table and graph below, which was prepared as of August 23, 2021.



The methodology used to establish the discount rates appears reasonable and appropriately reflects the criteria contained in GASB-87. Also, an appropriate expert in the public debt market, PFM, was used to assist in establishing the appropriate incremental borrowing rates. The rates also appear to appropriately reflect the market's low interest rates in affect at the beginning of the implementation period (October 1, 2021).