

**Exhibit No. ECO-15
Dockets UE-151871/UG-151872
Witness: Elizabeth C. O'Connell**

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

**WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,**

Complainant,

v.

PUGET SOUND ENERGY,

Respondent.

**DOCKETS UE-151871/UG-151872
(consolidated)**

**EXHIBIT TO
TESTIMONY OF**

ELIZABETH C. O'CONNELL

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

ASC Update - Definition of Lease

June 7, 2016

FINANCIAL ACCOUNTING SERIES

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Leases (Topic 842)

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Financial Accounting Standards Board

Definition of a Lease

At inception of a contract, an entity should determine whether the contract is or contains a lease. Topic 842 defines a lease as a contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration. Control over the use of the identified asset means that the customer has both (1) the right to obtain substantially all of the economic benefits from the use of the asset and (2) the right to direct the use of the asset.

Under the lessee accounting model in previous GAAP, the critical determination was whether a lease was a capital lease or an operating lease because lease assets and lease liabilities were recognized only for capital leases. Under Topic 842, the critical determination is whether a contract is or contains a lease because lessees are required to recognize lease assets and lease liabilities for all leases—finance and operating—other than short-term leases (that is, if the entity elects the short-term lease recognition and measurement exemption). Topic 842 provides detailed guidance and several examples to illustrate the application of the definition of a lease to assist entities in making this critical determination.

Components

Topic 842 requires an entity to separate the lease components from the nonlease components (for example, maintenance services or other activities that transfer a good or service to the customer) in a contract. Although this was a requirement in previous GAAP, Topic 842 provides more guidance on how to identify and separate components than previous GAAP. Only the lease components must be accounted for in accordance with Topic 842. The consideration in the contract is allocated to the lease and nonlease components on a relative standalone price basis (for lessees) or in accordance with the allocation guidance in Topic 606 (for lessors). Consideration attributable to nonlease components is not a lease payment and, therefore, is not included in the measurement of lease assets or lease liabilities. Entities should account for nonlease components in accordance with other applicable Topics. Activities that do not transfer a good or service to the lessee or amounts paid solely to reimburse costs of the lessor are not components in a contract and are not allocated any of the consideration in the contract.

The above notwithstanding, Topic 842 provides a practical expedient for lessees as it relates to separating lease components from nonlease components. Lessees may make an accounting policy election by class of underlying asset not to separate lease components from nonlease components. If an entity makes that accounting policy election, it is required to account for the nonlease components together with the related lease components as a single lease component.

Sale and Leaseback Transactions

For a sale to occur in the context of a sale and leaseback transaction, the transfer of the asset must meet the requirements for a sale in Topic 606. If there is no sale