Defining Issues®
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Lease Accounting Discussions Near Completion

The FASB and IASB are ready to stop talking about lease accounting – at least for now.[1] With the completion of the IASB's March meeting, other than any minor clean-up issues, both say they are finished building their new lease accounting mousetraps. They have told their staff to begin writing the final standards. The standards will contain numerous points of divergence, the most significant of which relate to lessee accounting. Neither has decided when the new standards will become effective. However, they plan to issue their final standards by the end of this year.

This edition of *Defining Issues* discusses the Boards' significant decisions on lease accounting subsequent to October 2014 and provides KPMG's observations on their potential impacts. The complete highlights of the new lease accounting models are included in the Summary of Decisions Reached in Redeliberations.

Key Facts

- The Boards decided to require new lessee disclosures, but reached different conclusions on the specific disclosures and how they would be presented.
- Both Boards agreed to allow a modified retrospective transition approach. However, they had different views on whether to permit full retrospective transition and the details of modified retrospective transition.
- The Boards talked about changing the definition of a lease so that fewer transactions would qualify as leases. Ultimately, they decided not to.
- The FASB talked about aligning the reassessment requirements for variable lease payments based on an index or rate with the IASB's decisions, but decided not to.

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[1] FASB Proposed Accounting Standards Update (Revised), Leases, May 16, 2013, available at www.fasb.org, and IASB ED/2013/6, Leases, May 2013, available at www.ifrs.org. For more information about the Boards' previous discussions see KPMG's Defining Issues Nos. 14-46, FASB and IASB Enter Home Stretch in Redeliberations on Lease Accounting – but on Different Tracks, 14-29, FASB and IASB Continue Discussions on Lease Accounting, and 14-17, FASB and IASB Take Divergent Paths on Key Aspects of Lease Accounting, all available at http://www.kpmg-institutes.com.

- The IASB decided to specify that leased assets that are dependent on, or highly interrelated with other leased assets do not qualify for the small-ticket lease exemption that will apply under IFRS. It also decided to indicate in the basis for conclusions to its standard that the exemption is intended to apply to assets with a value of $5,000 or less when new.

Other than on-balance sheet recognition for lessees and the prospective elimination of leveraged lease accounting for lessors, the FASB's new lease accounting requirements will not represent a significant change from current U.S. GAAP.

Key Impacts

- Lessees will be required to disclose more information about leases than they currently do.
- Transition alternatives may increase the difficulty for financial statement users trying to compare companies applying U.S. GAAP to those applying IFRS. For preparers, the transition alternatives will generally reduce the cost and effort of initially applying the new requirements.

Background

When the FASB and the IASB began their leases project, their primary objectives included:

- Reducing complexity in lease accounting;
- Eliminating arbitrary accounting distinctions for transactions that are economically similar;
- Requiring lessees to recognize all leases on-balance sheet; and
- Developing converged lease accounting requirements.

Although the project will meet the objective for lessees to recognize leases on-balance sheet, it will not achieve the other objectives. Other than lessees recognizing leases on the balance sheet, the project will result in modest changes to lease accounting under U.S. GAAP. While the changes to lessee accounting are more significant under IFRS, the changes to lessor accounting under IFRS are also minimal.

Last year, the Boards reached significantly different decisions about lessee accounting. The FASB opted for a dual model approach. Under that approach, a lessee will recognize a right-of-use (ROU) asset and a lease liability for its obligation to make lease payments for all leases other than short-term leases. Subsequent accounting for the ROU asset and presentation of lease expense, however, will depend on whether the lease is classified as Type A (most capital leases under current U.S. GAAP) or Type B (most operating leases under current U.S. GAAP). For Type A leases, the lessee generally will recognize a front-loaded pattern of total lease expense comprising interest on the lease liability and amortization of the ROU asset, similar to today's accounting for capital leases. For Type B leases, the lessee will recognize a single lease expense amount on a straight-line basis over the lease term, similar to today's accounting for operating leases. The carrying amount of the ROU asset for Type B leases will be determined as a "plug" to achieve straight-line total lease expense. Conversely, the IASB opted for a single model approach in which lessees will account for all leases other than short-term leases as Type A leases.

On lessor accounting, the Boards reached converged decisions to keep the key aspects of lessor accounting substantially unchanged from existing guidance. As a result, lessors will account for most leases as executory contracts (i.e., as operating leases).

The Boards also reached different conclusions on many issues in addition to the basic lessee accounting model. Additional areas in which the Boards' decisions diverged include lessee reassessments of variable lease payments, accounting for subleases and sale-leaseback transactions, accounting for small-ticket leases and leases between related parties, financial statement presentation for lessees, lessee disclosures, and transition.

The Boards' disparate approaches may cause significant differences in financial reporting by companies applying U.S. GAAP versus companies applying IFRS, complicating comparisons by financial statement users.

The Boards have now told their staff to begin writing the final standards. Nuances in the language of the different standards may produce divergence in application for areas where the Boards' decisions are converged. During the drafting process there likely will be questions that the Boards will be asked to resolve in one or more public meetings. However, those discussions are not likely to significantly change either Board's decisions. The Boards will decide later this year when the new standards will become effective. It could be that the standards have different effective dates. However, it's likely that the effective date of both standards will be aligned with the effective date of each Board's new revenue recognition standard.[2] Both Boards are expected to decide whether to defer the effective date of those standards later this year.

Lessee Disclosures

At their January meeting, the Boards agreed that the objective of lessee disclosures is to help users understand the amount, timing, and uncertainty of cash flows from leases. Lessees will use judgment to determine the appropriate level of disclosure aggregation. However, the Boards reached different decisions about both the qualitative and quantitative information lessees will have to disclose. Some of these differences are due to their divergence on lessee accounting.

Qualitative Disclosures. The FASB decided to require lessees to disclose:

- Information about the nature of leases (and subleases), including:
  - A general description of those leases;
  - The basis, and terms and conditions, on which variable lease payments are determined;
  - The existence, and terms and conditions, of options to extend or terminate the lease;
  - The existence, and terms and conditions, of lessee residual value guarantees; and

[2] FASB Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers, available at www.fasb.org, and IFRS 15, Revenue from Contracts with Customers.

– Restrictions or covenants imposed by leases.

- Information about leases that have not yet commenced, but that create significant rights and obligations for lessees;
- Information about significant judgments and assumptions made in accounting for leases, including:
  – The determination of whether a contract contains a lease;
  – The allocation of the consideration in a contract between lease and non-lease components; and
  – The determination of the discount rate.
- Main terms and conditions of any sale-leaseback transactions; and
- Whether an accounting policy election was made to apply the short-term lease exemption.

The FASB decided not to include guidance about how to aggregate qualitative disclosures.

The IASB decided *not* to include a list of required qualitative disclosures in its final standard. Lessees will be required to provide qualitative disclosures in addition to the quantitative disclosures only if necessary to satisfy the lessee disclosure objective.

Quantitative Disclosures. Lessees will be required to disclose:

Disclosure	U.S. GAAP	IFRS
For Type A leases, amortization of right-of-use (ROU) assets and interest on lease liabilities (including capitalized interest)	✓	Amortization split by class of underlying asset
Additions to ROU assets		✓
The carrying amount of ROU assets, by class of underlying asset		✓
Type B lease expense (including capitalized costs)	✓	
Short-term lease expense, when the lease term exceeds 30 days	✓	✓
Small-ticket lease expense		✓
Variable lease expense	✓	✓
Sublease income	✓	✓
Gains and losses on sale-leaseback transactions	✓	✓

Disclosure	U.S. GAAP	IFRS
A maturity analysis of lease liabilities for each of the first five years after the balance sheet date and in total thereafter, including a reconciliation of the undiscounted cash flows to lease liabilities on the balance sheet	✓	
A maturity analysis of lease liabilities in accordance with IFRS 7, separate from the maturity analysis for other financial liabilities[3]		✓
Cash paid for amounts included in the measurement of lease liabilities, segregated between Type A and Type B leases and between operating and financing cash flows	✓	
Total cash outflows for leases		✓
Supplemental noncash information on lease liabilities exchanged for ROU assets separately for Type A and Type B leases	✓	
The weighted-average remaining lease term, presented separately by Type A and Type B leases	✓	
The weighted-average discount rate for Type B leases as of the balance sheet date	✓	

Presentation. The IASB decided to require lessees to present quantitative disclosures in a tabular format (unless another format is more appropriate). Lessees applying IFRS will present all lessee disclosures in a single note or separate section in the financial statements. The FASB did not agree to the same presentation requirements, but agreed to include an example illustrating quantitative disclosure requirements in a tabular format in its final standard. Example 1 provides an illustration of the FASB's quantitative lessee disclosures, other than the maturity analysis of lease liabilities, in a tabular format.

Other Decisions Reached. The FASB decided to require the same lessee disclosures for public and nonpublic business entities. It decided not to require lessees to disclose:

- A reconciliation of the opening and closing balances of lease liabilities; or
- A maturity analysis of commitments for non-lease components (e.g., services provided by the lessor) related to a lease.

The IASB decided not to require lessees to disclose a reconciliation of the opening and closing balances of ROU assets.

[3] IFRS 7, Financial Instruments – Disclosures.

KPMG Observations

Based on the Boards' decisions, lessee disclosures will increase as compared to current GAAP. This increase is likely due in part to the Boards' divergent lessee accounting models.

The FASB's decision not to provide further guidance on the disaggregation of qualitative disclosures (e.g., by class of underlying asset, lease term, lease payment terms, geographical region, etc.) is different than the new revenue recognition standard, which includes disaggregation guidance in its qualitative disclosure requirements.

The FASB decided not to require a reconciliation of lease liabilities due to preparers' concerns about the costs and complexity of implementation. Some preparers cited the need for more robust IT systems and/or process capabilities to track and accumulate reconciling items that are not identified for disclosure today. Instead, the FASB agreed to require lessees to disclose key components of the reconciliation, including total lease expense and cash paid for amounts included in the measurement of lease liabilities. This decision is consistent with current U.S. GAAP on financial liabilities, which does not require a similar reconciliation.

The FASB expects lessees to be able to prepare the new quantitative disclosures using their existing systems and processes as many of requirements are similar to current U.S. GAAP.

Example 1: Selected Lessee Quantitative Disclosures in a Tabular Format (FASB)

For the years ended December 31, 20X8 and 20X7 (in thousands)	20X8	20X7
Lease expense		
Type A lease expense		
Amortization of ROU assets	600	525
Interest on lease liabilites	150	110
Type B lease expense	1,000	900
Short-term lease expense	50	40
Variable lease expense	75	60
Sublease income	(10)	(8)
Total lease expense	**1,865**	**1,627**
Other information		
(Gains) losses on sale-leaseback transactions, net	(8)	5
Cash paid for amounts included in the measurement of lease liabilities		
for Type A leases		
Operating cash flows	1,400	1,300
Financing cash flows	200	170
Cash paid for amounts included in the measurement of lease liabilities		
for Type B leases		
Operating cash flows	800	635
ROU assets obtained in exchange for lease liabilites	475	515
Weighted-average remaining lease term (in years)		
Type A leases	9.7	8.9
Type B leases	5.2	5.4
Weighted-average discount rate for Type B leases	6.1%	6.3%

Transition

The Boards separately discussed transition approaches, including transition disclosures, at their respective February meetings. The Boards reached notably different decisions about transition requirements for lessees, lessors, and subleases. The FASB also reached decisions about transition requirements for build-to-suit leasing transactions that are not applicable under IFRS.

Transition Requirement	U.S. GAAP	IFRS
Definition of a Lease		
Entities permitted to not reconsider whether a contract is or contains of a lease for all contracts that are ongoing at the date of initial application.[4] An entity that chooses not to apply the new definition of a lease will do so for all contracts that are ongoing at the date of initial application, and disclose that fact.	Only if elected with certain other specified reliefs (see below)	✓
Lessee Transition		
Modified retrospective transition required for all leases existing at, or entered into after, the date of initial application.[5] No transition accounting required for leases that expired prior to the date of initial application.	✓	
Lessees permitted to elect not to reconsider: • Whether any expired or existing contracts are or contain leases. • The lease classification for any expired or existing leases. • Whether existing capitalized initial direct costs would have qualified for capitalization under the new leases standard. These must be elected as a package and applied to all leases. They cannot be elected on a lease-by-lease or relief-by-relief basis.	✓	
Lessees permitted to use hindsight in evaluating whether payments for lease renewals and purchase options should be included in lease payments when accounting for existing leases. This specified relief may be elected separately	✓	

[4] Under the IASB proposal, the first day of the annual reporting period in which a lessee first applies the requirements of the new standard.

[5] Under the FASB proposal, the beginning of the earliest comparative period presented in the financial statements.

Transition Requirement	U.S. GAAP	IFRS
from the other specified reliefs, but cannot be elected on a lease-by-lease basis.		
Lessees to choose either a fully retrospective approach or a modified retrospective approach on transition, to be applied consistently across their entire portfolio of operating leases. • Under the modified retrospective approach, a lessee will not restate comparative information. • At the date of initial application, recognize the cumulative effect of initial application as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate).		✓
Lessees required to apply a modified retrospective transition approach for build-to-suit lease arrangements existing at, or entered into after, the date of initial application. This approach will not require any transition accounting for build-to-suit leases that expired prior to the date of initial application. • Lessees that have recognized assets and liabilities solely as a result of a transaction's build-to-suit designation must derecognize those assets and liabilities at the later of (a) the date of initial application or (b) the date that the lessee is determined to be the accounting owner of the asset under existing build-to-suit guidance. Any difference between the amounts of the assets and the liabilities derecognized must be recorded as an adjustment to equity at that date. A lessee will then follow the general lessee transition guidance for the lease itself. • For build-to-suit leases in which the construction period ends prior to the date of initial application, but the lease term has not expired as of that date, and the transaction qualified for sale-leaseback accounting under existing guidance prior to that date, the	✓	

Transition Requirement	U.S. GAAP	IFRS
entity will apply the lessee transition requirements.[6]		
Lessor Transition		
Modified retrospective transition required for all leases other than leveraged leases existing at, or entered into after, the date of initial application. No transition accounting required for leases that expired prior to the date of initial application.	✓	
Lessors permitted not to reconsider: • Whether any expired or existing contracts are or contain leases. • The lease classification for any expired or existing leases. • Whether existing capitalized initial direct costs would have qualified for capitalization under the new leases standard. These must be elected as a package and applied to all leases. They cannot be elected on a lease-by-lease or relief-by-relief basis.	✓	
Lessors permitted to use hindsight in evaluating whether payments for lease renewals and purchase options should be included in lease payments when accounting for existing leases. This specified relief may be elected separately from the other specified reliefs, but cannot be elected on a lease-by-lease basis.	✓	
Specified relief elections must be consistently applied by an entity for all lessee and lessor transactions (i.e., an entity that is a lessee and a lessor must make the same relief elections for all of its leases).	✓	
Lessors required to continue to apply existing accounting for any leases that are ongoing at the date of initial application, except for intermediate lessors in a sublease.		✓

[6] FASB ASC Subtopic 840-40, Leases – Sale-Leaseback Transactions, available at www.fasb.org.

Transition Requirement	U.S. GAAP	IFRS
Subleases Transition		
Intermediate lessors to reassess each ongoing operating sublease at the date of initial application to determine whether under the new standard it is classified as an operating lease or a finance lease. This determination is based on the remaining contractual terms of the head lease and the sublease. For subleases that were classified as operating leases under IAS 17 but finance leases under the new standard, an intermediate lessor will be required to account for the sublease as a new finance lease entered into on the date of initial application.		✓
Sale-Leaseback Transactions		
Entities will not reassess whether a transaction previously accounted for as a sale-leaseback transaction would have qualified as a sale (or purchase) in accordance with the Boards' new revenue recognition standards.[7]	✓	✓
An entity will account for a leaseback in accordance with the lessee and lessor transition requirements.	✓	✓
For any transaction previously accounted for as a sale and capital (finance) leaseback, the seller-lessee will continue to amortize any deferred gain or loss.	✓	✓
For any transaction previously accounted for as a sale and operating leaseback: • The seller-lessee will recognize the portion of any deferred gain or loss not resulting from off-market terms as a cumulative-effect adjustment to equity at the later of the date of initial application or the date of sale. • The portion of any seller-lessee deferred gains or losses that resulted from off-market terms will be recognized as an adjustment to the leaseback ROU asset (if a deferred loss) or as a remaining financial liability (if a deferred gain) at the date of initial application.	✓	

[7] FASB ASC Topic 606, Revenue from Contracts with Customers, available at www.fasb.org, and IFRS 15, Revenue from Contracts with Customers.

Transition Requirement	U.S. GAAP	IFRS
For any transaction previously accounted for as a sale and operating leaseback, account for deferred gains or losses as an adjustment to the leaseback ROU asset.		✓
Disclosures		
Lessees and a lessors will provide transition disclosures consistent with Topic 250, *Accounting Changes and Error Corrections*, except for the following disclosure requirements in paragraph 250-10-50-1(b)(2)): • The effect of the change on income from continuing operations, net income, any other affected financial statement line item, and • Any affected per-share amounts for the current period and any prior periods retrospectively adjusted.	✓	
Lessees will be required to disclose: • The weighted average incremental borrowing rate at the date of initial application, and • Explanation of any difference between: (a) The result of discounting the operating lease commitments reported under IAS 17 at the end of the annual reporting period preceding the date of initial application; and (b) Lease liabilities recognized on the balance sheet immediately after posting the cumulative catch up adjustment on the date of initial application.		✓

KPMG Observations

The FASB decided to not allow a full retrospective transition approach, and to limit how preparers can use transition reliefs. While this limits flexibility for preparers, it will result in transition that is more consistent across companies. The FASB also decided it was important to align transition options for entities that are both lessees and lessors.

In addition to the decisions above, the Boards also went into further detail on how lessees (and lessors for U.S. GAAP) will apply the respective approaches to remeasure existing leases. Those details will be included in a future KPMG publication, along with examples and implementation guidance.

The Boards' separate meetings to discuss transition led to significant differences in transition approaches. For lessee accounting, given the divergence in the Boards' lessee accounting models, this may not be as noteworthy. But it does represent additional divergence, at least for a period of time after initial application, for lessors under each standard. (Lessor accounting is much more converged under the Boards' respective standards.)

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Summary of Decisions Reached in Redeliberations

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<tr><th>Topic</th><th>FASB Decisions</th><th>IASB Decisions</th></tr>
<tr><td>Definition of a Lease</td><td colspan="2">• A contract will contain a lease if:
– Fulfillment of the contract depends on the use of an identified asset; and
– The contract conveys the right to control the use of the identified asset for a period of time in exchange for consideration, or neither the customer nor the supplier controls the use of the identified asset throughout the period of use and:
• The customer has the right to operate the asset or to direct others to operate it in a manner the customer determines (and the supplier has no right to change those operating instructions); or
• The customer designed the asset, or caused it to be designed, in a way that predetermines during the period of use (a) how and for what purpose it will be used, or (b) how it will be operated</td></tr>
<tr><td rowspan="2">Practical Expedients and Targeted Reliefs</td><td colspan="2">• Optional lessee exemption for short-term leases – i.e., leases with a lease term as determined under the revised proposals ≤ 12 months
• Portfolio-level accounting will be permitted if it does not differ materially from applying the requirements to individual leases</td></tr>
<tr><td>• No exemption for small-ticket leases</td><td>• Optional lessee exemption for small-ticket leases (i.e., leases of assets with a value of $5,000 or less when new), even if material in aggregate</td></tr>
<tr><td>Lessee Accounting Model</td><td>• Dual lease accounting model
• Lease classification test based on IAS 17 classification criteria[8]
• All leases on-balance sheet: lessee will recognize a right-of-use (ROU) asset and lease liability
– Type A leases will be treated as the purchase of an asset on a financed basis
– Type B leases generally will have straight-line recognition of total lease expense</td><td>• Single lease accounting model
• No lease classification test
• All leases on-balance sheet: lessee will recognize a right-of-use (ROU) asset and lease liability
– Treated as the purchase of an asset on a financed basis</td></tr>
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[8] IAS 17, Leases.

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<tr><th>Topic</th><th>FASB Decisions</th><th>IASB Decisions</th></tr>
<tr><td rowspan="3">Lessor Accounting Model</td><td colspan="2">Dual lease accounting model
Lease classification test based on IAS 17 classification criteria
Type B accounting model based on IAS 17 operating lease accounting
Type A accounting model based on IAS 17 finance lease accounting with recognition of net investment in lease comprising lease receivable and residual asset</td></tr>
<tr><td>– Selling profit will not be recognized on commencement of leases that qualify for Type A classification only due to involvement by third parties other than the lessee</td><td>– There will be no restriction on recognizing selling profit on commencement of Type A leases</td></tr>
<tr><td>Existing leveraged leases will be grandfathered from application of the new standard</td><td>N/A – leveraged lease accounting does not exist under IFRS</td></tr>
<tr><td>Related Party Leasing Transactions</td><td>Account for leases between related parties based on their contractual terms, even if they differ from the substance of the arrangement</td><td>N/A – the IASB did not address related party leasing transactions in its proposals</td></tr>
<tr><td>Lease Term and Purchase Options</td><td colspan="2">Payments for optional (e.g., renewal) periods and purchase options will be included in lease accounting if it is reasonably certain that the lessee will exercise those options, consistent with the high threshold in current GAAP
Lessees will reassess renewal and purchase options if there is a significant event or change in circumstances that is within the control of the lessee – e.g., construction of significant leasehold improvements
No reassessment of renewal and purchase options by lessors</td></tr>
<tr><td>Initial Direct Costs</td><td colspan="2">Initial direct costs will include only incremental costs that an entity would not have incurred if it had not obtained the lease
Lessees will include initial direct costs in the initial measurement of the ROU asset and amortize the costs over the lease term
Initial direct costs will be included in determining the lessor’s implicit rate unless the lease is a Type A lease for which selling profit is recognized at lease commencement
Lessors will include initial direct costs for Type A leases
– In the initial measurement of the lease receivable if no selling profit is recognized at lease commencement</td></tr>
</table>

Redeliberations of 2013 Exposure Drafts		
Topic	**FASB Decisions**	**IASB Decisions**
	– In expense at lease commencement if selling profit is recognized at lease commencement • Lessors will capitalize initial direct costs for Type B leases and amortize the costs over the lease term in the same pattern as lease income	
Discount Rate	• The lessee's discount rate will be the lessor's implicit rate if available; otherwise, the lessee's incremental borrowing rate – The value used to determine the lessee's incremental borrowing rate will be the cost of the ROU asset • Lessees will reassess the discount rate when there is – A change in the lease term or the assessment of whether the lessee is, or is not, reasonably certain to exercise a purchase option; and – A lease modification	
	• Nonpublic business entity lessees will be permitted to elect as an accounting policy to use a risk-free discount rate	• N/A – no unique guidance for nonpublic business entities
	• The lessor's discount rate will be the rate implicit in the lease (i.e., the implicit rate) – Initial direct costs will be included in determining the implicit rate unless the lease is a Type A lease for which selling profit will be recognized at lease commencement • Lessors will reassess the discount rate when there is a lease modification	
Variable Lease Payments	• Lease payments used in the initial measurement of lease assets and liabilities will include: – Variable payments based on an index or rate using prevailing (spot) rates or indices at lease commencement; and – Variable payments that represent in-substance fixed payments (consistent with current practice) • No reassessment of variable lease payments by lessors • Variable payments that are not based on an index or rate and are not in-substance fixed payments will be excluded from the measurement of lease assets and liabilities and recognized as expense as incurred or income as earned	
	• Lessees will reassess variable lease payments based on an index or rate only when lease payments are remeasured for	• Lessees will reassess variable lease payments based on an index or rate when:

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<tr><td></td><td>other reasons (e.g., a reassessment due to a change in the lease term)</td><td>– Lease payments are remeasured for other reasons (e.g., a reassessment due to a change in the lease term)
– There is a contractual change in the cash flows (i.e., when an adjustment to the lease payments based on an index or rate takes effect under the terms of the lease)</td></tr>
<tr><td>Arrangements with Lease and Non-lease Components; Contract Combinations</td><td colspan="2">• Activities (or costs of the lessor) that do not transfer a good or service to the lessee (e.g., taxes and insurance on the property) will be considered part of the lease (i.e., not separate components in a contract)
• Lessors will always separate lease and non-lease components and allocate consideration using the new revenue recognition standard’s guidance (i.e., on a relative stand-alone selling price basis)
– Reallocate consideration when there is a contract modification that is not accounted for as a separate, additional lease
• Lessees will choose an accounting policy by class of underlying asset to either:
– Separate lease and non-lease components and allocate consideration based on relative stand-alone prices of components, maximizing the use of observable information
• Reallocate consideration when (a) there is a reassessment of either the lease term or whether exercise of a lessee purchase option is reasonably certain, or (b) there is a contract modification that is not accounted for as a separate, additional lease
– Account for lease and non-lease components together as a single lease component
• Two or more contracts entered into at or near the same time will be combined as a single transaction if:
– The contracts are negotiated as a package with a single commercial objective; or
– The amount of consideration to be paid in one contract depends on the price or performance of the other contract</td></tr>
<tr><td>Lease Modifications</td><td colspan="2">• Lease modifications will be defined as any change to the contractual terms and conditions of a lease that was not part of the original terms and conditions of the lease
• A modification will be considered a separate lease when it grants the lessee an additional ROU that was not included in the original lease and</td></tr>
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<tr><td></td><td colspan="2">that ROU is priced commensurate with its stand-alone price in the context of that particular contract
• For lessees, when a modification is not considered a separate, additional lease:
– If the modification does not reduce the lessee’s ROU, the ROU asset will be adjusted by the amount of the adjustment to the lease liability
– If the modification reduces the lessee’s ROU, the modification will be treated as a full or partial early termination of the lease with a resulting income statement effect
• For lessors, when a modification is not considered a separate, additional lease:
– Type B lease modifications will be treated as a new lease with any prepaid or accrued rent on the original lease considered part of the lease payments for the new lease
– Type A lease modifications will be accounted for under the financial instruments requirements in U.S. GAAP or IFRS as applicable</td></tr>
<tr><td rowspan="2">Subleases</td><td colspan="2">• A lessee-sublessor will account for the head lease and the sublease as two separate contracts unless those contracts meet the contract combinations guidance
– The head lease will be accounted for in accordance with the lessee accounting proposals
– The sublease will be accounted for in accordance with the lessor accounting proposals
• A lessee-sublessor will not offset lease liabilities and assets arising from a head lease and sublease unless they meet the financial instruments requirements for offsetting in U.S. GAAP or IFRS as applicable
• A lessee-sublessor will not offset lease income from a sublease and lease expense from a head lease unless it meets the requirements for offsetting in other U.S. GAAP or IFRS as applicable (e.g., the new revenue recognition standard)[9]</td></tr>
<tr><td>• A sublessor will consider the underlying asset rather than the ROU asset to be the leased asset in determining the classification of the sublease</td><td>• A sublessor will consider the ROU asset to be the leased asset in determining the classification of the sublease</td></tr>
</table>

[9] Members of both Boards believe it is unlikely that sublease income and head lease expense will qualify to be offset if the sublease is classified as a Type B lease.

<table>
<tr><th colspan="3">Redeliberations of 2013 Exposure Drafts</th></tr>
<tr><th>Topic</th><th>FASB Decisions</th><th>IASB Decisions</th></tr>
<tr><td rowspan="5">Sale-Leaseback Transactions</td><td colspan="2">Determining Whether a Sale has Occurred
A sale and leaseback of the underlying asset will be recognized if the requirements for sale recognition in the new revenue recognition standard are met. The existence of the leaseback will not, on its own, result in a conclusion that control of the asset had not been conveyed to the buyer-lessor.</td></tr>
<tr><td>If the leaseback would be classified as a Type A lease by the seller-lessee, then sale recognition will be precluded
A repurchase option held by the seller-lessee in a sale and leaseback transaction will preclude sale recognition unless:
The strike price to repurchase the asset is its fair market value at the date of option exercise; and
The underlying asset is readily available and non-specialized</td><td>N/A – single model approach for lessee accounting
If the seller-lessee has a substantive repurchase option with respect to the underlying asset, sale recognition will be precluded</td></tr>
<tr><td colspan="2">Both the seller-lessee and the buyer-lessor will account for a sale-leaseback transaction that does not qualify for sale accounting as a financing transaction</td></tr>
<tr><td colspan="2">Accounting for a Sale/Purchase
A buyer-lessor will account for the purchase of an asset in a sale-leaseback transaction that qualifies for sale accounting consistent with the guidance that applies to the purchase of a nonfinancial asset
A seller-lessee will account for any loss on a sale-leaseback transaction that qualifies for sale accounting consistent with the guidance that applies to any other sale</td></tr>
<tr><td>Any gain recognized by a seller-lessee on a sale-leaseback transaction that qualifies for sale accounting will be measured consistent with the guidance that applies to any other sale, subject to any adjustment for "off-market" terms</td><td>Any gain recognized by a seller-lessee on a sale-leaseback transaction that qualifies for sale accounting will be restricted to the amount that relates to the buyer-lessor's residual interest in the underlying asset, subject to any adjustment for "off-market" terms</td></tr>
</table>

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<tr><th>Topic</th><th>FASB Decisions</th><th>IASB Decisions</th></tr>
<tr><td rowspan="2"></td><td colspan="2">Accounting for the Leaseback
• If a sale-leaseback transaction qualifies for sale accounting, the leaseback will be accounted for in the same manner as any other lease</td></tr>
<tr><td colspan="2">Accounting for "Off-Market" Terms
• Any potential "off-market" adjustment will be measured as the more readily determinable of:
– The difference between the fair value of the underlying asset and the sales price, or
– The difference between the present value of fair market value lease payments and the present value of the contractual lease payments
• A deficiency in the transaction terms versus market terms will be accounted for as a prepayment of rent
• An excess in the transaction terms versus market terms will be accounted for as additional financing provided by the buyer-lessor to the seller-lessee</td></tr>
<tr><td rowspan="2">Lessee Presentation – Balance Sheet</td><td colspan="2">• Lessees will present Type A ROU assets and lease liabilities either as separate line items on the balance sheet or disclose separately in the notes to the financial statements
– If not separately presented on the balance sheet lessees will:
• Present Type A ROU assets on the balance sheet as if the underlying asset were owned
• Disclose in the notes the line items on the balance sheet in which Type A ROU assets and lease liabilities are included and their amounts</td></tr>
<tr><td>• Lessees will not include Type B ROU assets and lease liabilities in the same line items as Type A ROU assets and lease liabilities on the balance sheet
– If not separately presented on the balance sheet lessees will disclose in the notes the line items on the balance sheet in which Type B ROU assets and lease liabilities are included and their amounts</td><td>• N/A – no Type B lease classification</td></tr>
</table>

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<tr><th>Topic</th><th>FASB Decisions</th><th>IASB Decisions</th></tr>
<tr><td>Lessee Presentation – Statement of Cash Flows</td><td>• Lessees will classify cash paid for:
– Principal on Type A lease liabilities as financing activities
– Interest on Type A lease liabilities as operating activities
– Type B leases, variable lease payments, and leases that are not recognized on-balance sheet (e.g., some short-term leases) as operating activities</td><td>• Lessees will present cash paid for:
– Principal on lease liabilities as financing activities
– Interest on lease liabilities as either operating or financing activities based on the lessee's accounting policy choice under IAS 7[10]
– Variable lease payments and leases that are not recognized on-balance sheet (e.g., some short-term leases) as operating activities
• Lessees will disclose total lease payments in the notes to the financial statements</td></tr>
<tr><td rowspan="2">Lessee Disclosures</td><td colspan="2">• Objective: Enable financial statement users to understand the amount, timing, and uncertainty of cash flows arising from leases</td></tr>
<tr><td>• Lessees will disclose the following qualitative information:
– Nature of leases (and subleases);
– Leases that have not yet commenced, but that create significant rights/obligations;
– Significant lease accounting judgments and assumptions;
– Main terms and conditions of sale-leaseback transactions; and
– Whether an accounting policy election was made for the short-term lease exemption</td><td>• Lessees will disclose other information, in addition to the quantitative disclosures, in sufficient detail to satisfy the lessee disclosure objective</td></tr>
</table>

[10] IAS 7, Statement of Cash Flows.

Redeliberations of 2013 Exposure Drafts		
Topic	**FASB Decisions**	**IASB Decisions**
	• Lessees will disclose the following *quantitative* information:	
	In any format the lessee considers appropriate	In a tabular format, unless another format is more appropriate
	– Amortization of ROU assets and interest on lease liabilities (including capitalized interest)	
	• For Type A leases only – N/A	• Amortization split by class of underlying asset – Additions to ROU assets – Carrying amount of ROU assets, split by class of underlying asset
	– Short-term lease expense (when lease term > 30 days) – Variable lease expense – Sublease income – Gains (losses) on sale-leaseback transactions	
	– Type B lease expense – N/A – Cash paid for lease payments, separately for Type A and Type B leases and segregated between operating and financing cash flows – Supplemental noncash information on lease liabilities exchanged for ROU assets, separately for Type A and Type B leases – Weighted-average remaining lease term, separately for Type A and Type B leases – Weighted-average discount rate for Type B leases as of the balance sheet date	– N/A – Small-ticket lease expense – Total cash outflow for leases – N/A
	– A maturity analysis of lease liabilities for each of the first 5 years after the balance sheet	– A maturity analysis of lease liabilities in accordance with IFRS 7, separate from the

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<tr><th>Topic</th><th>FASB Decisions</th><th>IASB Decisions</th></tr>
<tr><td></td><td>date and in total thereafter, including a reconciliation of undiscounted cash flows to lease liabilities on the balance sheet</td><td>maturity analysis for other financial liabilities</td></tr>
<tr><td>Lessor Presentation</td><td colspan="2">• Lessors will present lease assets and liabilities and income and expense consistent with the current guidance in IAS 17
• Lessors will classify all cash inflows from leases as operating activities in the statement of cash flows</td></tr>
<tr><td rowspan="2">Lessor Disclosures</td><td colspan="2">General
• A lessor will disclose the following information about its leases:
– A general description of its leases;
– The basis, and terms and conditions, on which variable lease payments are determined;
– The existence, and terms and conditions, of options to extend or terminate the lease;
– The existence, and terms and conditions, of options for a lessee to purchase the underlying asset;
– Information about the significant assumptions and judgments made in accounting for its leases, which may include:
• The determination of whether a contract contains a lease;
• The allocation of the consideration in contracts that contain a lease between lease and non-lease components;
• The initial measurement of the residual asset; and
• Information about managing the risk associated with the residual asset
– A table of lease income received during the reporting period
– A maturity analysis of a) the undiscounted cash flows comprising a lessor’s lease receivables (for Type A leases) and b) the undiscounted future lease payments (for Type B leases) for each of the first five years and a total of the amounts thereafter. For Type A leases, the amounts included in the maturity analysis will be reconciled to the balance of lease receivables presented separately in the balance sheet or disclosed separately in the notes.</td></tr>
<tr><td colspan="2">Type B Leases
• General property, plant, and equipment disclosures for assets subject to Type B leases by significant class of underlying asset separately from those disclosures for the lessor’s other owned assets</td></tr>
</table>

Redeliberations of 2013 Exposure Drafts		
Topic	**FASB Decisions**	**IASB Decisions**
	Type A Lease	
	• An explanation of the significant changes in the components of net investment in Type A leases other than the lease receivable during the reporting period	• A qualitative and qualitative explanation of the significant changes in the net investment in Type A leases during the reporting period
Lessee Transition	• Modified retrospective transition: – Required for all leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements – Will not require any transition accounting for leases that expired prior to the date of initial application	• Fully retrospective approach or modified retrospective approach: – Under the modified retrospective approach, a lessee will not restate comparative information – At initial application date, recognize the cumulative effect of application as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate)
	• Lessees may elect certain specified reliefs, which must be elected as a package and applied to all leases.	• N/A
	• Lessees may use hindsight in evaluating whether payments for lease renewals and purchase options should be included in lease payments when accounting for existing leases.	• N/A
Lessor Transition	• Modified retrospective transition: – Required for all leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements – Will not require any transition accounting for leases that expired prior to the date of initial application	• Continue to apply existing accounting for any leases that are ongoing at the date of initial application, except for intermediate lessors in a sublease. • Intermediate lessors in subleases reassess each ongoing operating sublease at the date of initial application to determine whether under the new standard it is classified as an operating lease or

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Topic	**FASB Decisions**	**IASB Decisions**
		a finance lease, based on the remaining contractual terms of the head lease and the sublease. For subleases that were classified as operating leases under IAS 17 but finance leases under the new standard, account for the sublease as a new finance lease entered into on the date of initial application.
	• Lessors may elect certain specified reliefs, which must be elected as a package and applied to all leases.	• N/A
	• Lessors may use hindsight in evaluating whether payments for lease renewals and purchase options should be included in lease payments when accounting for existing leases.	• N/A