

Lease Accounting Project Changes Focus

In Response to Feedback, Boards Begin Redeliberation

By Bill Bosco

THE FINANCIAL ACCOUNTING Standards Board (FASB) and the International Accounting Standards Board (IASB) have received an overwhelming response to their proposal to overhaul lease accounting. The Boards received nearly 800 comment letters on their Exposure Draft on Leases, and they held numerous outreach meetings where they heard from a cross section of users, preparers, lessees and lessors. The feedback made a strong impression on the Boards. They are now changing their direction to accommodate the feedback and working to reach acceptable alternatives, which could be good news for the equipment leasing and finance industry.

The comment letters generally all agreed that it is a good idea for lessees to capitalize operating lease obligations. However, the majority of the feedback indicated that the definition of a lease versus a service contract needs clarity; the

estimation of the lease term and contingent payments needs to move closer to current generally accepted accounting principles (GAAP); lessee P&L pattern needs to be reconsidered; and current lessor accounting needs little or no change.

The Boards are now deliberating and seeking input on changes to their proposal. They held deliberations throughout February, March and April and made some tentative decisions. They instructed the staff to field-test the decisions and seek advice through outreach to stakeholders. This outreach and field-testing process will be very important, especially if the Boards decide not to re-expose the proposed rule before issuance. The Boards have indicated that they want to make final decisions on the project in time to make their 2011 target for issuance.

Following are the key issues the Boards are deliberating:

Deadline Delayed

IN MID-APRIL, the FASB and IASB announced a decision to postpone the June target deadline for a new lease accounting standard “a few additional months” to provide more time to respond to feedback.

June “was always intended to be a target, not a deadline” FASB Chairman Leslie Seidman said. “At this point on each of the exposure documents we have received significant and very constructive feedback and we are in the process of working through those issues.”

At press time, the boards had not announced whether they might re-expose a final draft standard for further comment.

Definition of a Lease

- **Significance:** Under current GAAP, operating lease and service contracts had the same off-balance-sheet and straight-line P&L treatment; therefore, definitions did not need to be crisp. Under the Exposure Draft, with leases being capitalized and the P&L front-ended, there is a big difference in accounting treatment, so the definitions are important.
- **Exposure Draft Position:** A lease is a contract in which the right to control the right to use a specified asset (the underlying asset) is conveyed, for a period of time, in exchange for consideration. The definition includes the EITF 01-08 guidance defining when a contract conveys the right to control an asset.
- **Tentative Revised Position to Be Tested:** The Boards agreed to tentatively confirm the “specific asset” notion versus an asset that meets specifications (meaning assets could be substituted). The Boards will ask for feedback by taking both

