

MINUTES



Financial Accounting
Standards Board

To: FASB Board Members

From: Leases Team
(Phillips, x443)

Subject: Minutes of the September 16, 2009, FASB Board Meeting: Leases—Comment letter analysis and plan for redeliberations

Date: October 26, 2009

cc: FASB: Golden, Bielstein, Lott, Proestakes, Stoklosa, Mechanick, Zeyher, Helmus, Homant, Gonzales, Martin, Phillips, C. Smith, Brickman, Hood, Gabriele, Sutay, FASB Intranet, McGarity, Klimek, Willis; FASAC: Chookaszian, Posta, Guasp; IASB: Leisenring, Francis, Knubley, Lian, Vatrenejak, Kim

The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue an Accounting Standards Update.

Topic: Leases

Basis for Discussion: FASB Memo No. 37—Cover Note
FASB Memo No. 38—Comment Letter Summary
FASB Memo No. 39—Plan for Deliberations

Length of Discussion: 8:50 a.m.–9:50 a.m. (EDT)

Attendance:

Board members present: Herz, Linsmeier, Siegel, Seidman, and Smith

Board members participating by phone: None

Board members absent: None

Staff in charge of topic:	Zeyher
Other staff at Board table:	Golden, Stoklosa, Homant, Helmus, Gonzales, Martin, and Phillips
Outside participants (IASB staff participating by phone):	Knubley, Lian, Vatrenejak, and Kim

Summary of Decisions Reached

At the September 16, 2009, meeting the Boards discussed the following:

1. A summary of the responses to the Discussion Paper, *Leases: Preliminary Views*
2. Plans for the leases project over the next few months.

The comment letter summary is available at the FASB website. The Boards will continue their discussion of both lessor and lessee accounting issues at future meetings.

Objective of the Meeting

The objective of the meeting was to discuss the comments received on the Discussion Paper on leases and the plan for redeliberations. The Discussion Paper was issued in March 2009. The comment period ended July 17, 2009. A total of 290 comment letters were received as of August 11, 2009.

Matters Discussed and Decisions Reached

Issue 1: Comment Letter Analysis

General Overview

1. Ms. Helmus presented a general overview of the comments received on the Discussion Paper on leases and an overview of the comments related to the scope of proposed new lease guidance.
2. **Board Comments:** Ms. Seidman questioned if there was an overlap in the respondents who supported exclusion of short-term leases and non-core assets with those who did not support the right-of-use model.

3. Mr. Linsmeier said that many leases currently classified as short term also include renewal options that would likely increase the lease term of such leases in accordance with the proposed new lease guidance. He also stated that the Boards must address the issue of servicing arrangements within leases. Mr. Siegel noted that the Boards intend to discuss the issue of service arrangements in December.
4. In current practice, Ms. Zeyher said that the tension for distinguishing between leases and service arrangements is not as high under current lease accounting guidance, because if the leases are operating leases, operating leases and service arrangements receive the same accounting (expense as incurred).
5. Mr. Smith noted that during the working group meeting held on September 3, 2009 and the aviation meeting held on September 2, 2009, these groups expressed similar concerns. Mr. Smith also noted that the Boards will need to address the issue of service arrangements on a broader basis concerning all service arrangements embedded in a lease arrangement. Additionally, Mr. Smith stated that the analysis of service arrangements is imperative to discussions in confirming the proposed right-of-use model.
6. Mr. Linsmeier agreed that the accounting will get more complicated if leasing arrangements are viewed as intangible leases because they will begin to resemble a service arrangement at times.
7. Mr. Smith asked if the staff is planning to readdress whether intangibles should be included in the scope of the proposed new lease model.
8. Ms. Zeyher confirmed that the staff is planning to readdress the issue of scope with the intention of possible convergence between the FASB and the IASB.
9. Mr. Linsmeier clarified that he was not necessarily concerned on whether intangibles were included or excluded from the scope; rather, he was concerned with the resulting accounting when including a service arrangement with the leased asset.

Overall Approach to Lessee Accounting

10. Ms. Helmus presented an overview of the comments in relation to the overall approach to lessee accounting and the analysis of the rights and obligations and assets and liabilities arising in a simple lease contract.

11. **Board Comments:** Mr. Smith asked if the cross-cutting analysis was completed on responses in relation to those (a) who supported the Boards' approach to not take a components approach and (b) respondents who disagreed with the Boards' proposed approach to recognizing options and contingent rentals.
12. Ms. Zeyher commented that many respondents did not want to recognize options and contingent rentals through a components approach or recognize them on a single asset basis.

Initial and Subsequent Measurement

13. Ms. Helmus presented an overview of the comments in relation to the initial and subsequent measurement of the lessee's right-of-use asset and obligation to pay rentals.
14. **Board Comments:** Mr. Siegel raised concerns that depreciation /amortization may be a label that denotes a non-cash expense in comparison to *rental expense*. Mr. Smith stated that the accounting for the decrease in the value of the right-of-use asset did not just represent a labeling issue. He added that the issue also is related to whether one agrees with the fundamental decision that a right-of-use, rather than an executory contract, is being obtained.
15. Mr. Golden noted that financing expense may be appropriate for certain leases; whereas operating expense may be appropriate for other leases.

Leases with Options

16. Ms. Helmus presented an overview of the comments in relation to leases with options.
17. **Board Comments:** Mr. Linsmeier stated concerns that options are not being dealt with consistently across all projects. He stated that options are a cross-cutting issue amongst projects that must be discussed as such.
18. The entire Board noted concerns regarding the differences between projects on various cross-cutting issues and why each project may come to different conclusions. Mr. Golden stated the need to have a meeting on cross-cutting issues amongst projects.

Contingent Rentals and Residual Value Guarantees

19. Ms. Helmus presented an overview of the comments in relation to contingent rentals and residual value guarantees.

20. **Board Comments:** Mr. Smith questioned whether the staff was able to note a difference between those who responded to the IASB and those who responded to the FASB regarding whether they preferred a *most-likely-* or *probability-*based approach in determining the measurement for contingent rentals.
21. Mr. Linsmeier stated that the characterization of the capitalization of contingent rentals to the asset versus expenses that are reflected in profit and loss may not been discussed in the most effective way. The issue primarily is not whether the rentals should be capitalized or expensed, the issue is whether if they are capitalized or expensed whether the resulting effect on net income differs.

Right-of-Use Asset, Performance Obligation, and Lessor Accounting

22. Ms. Helmus presented an overview of the comments in relation to the lessee's presentation of the right-of-use asset and the performance obligation, and an overview of the comments in relation to lessor accounting.
23. **Board Comments:** Ms. Seidman noted that at the working group meeting, there was concern expressed from the lessor point of view to distinguish between in-substance sales and leases. She suggested that it may be beneficial to use guidance from the existing lease literature, such as a risk-rewards based approach to make this distinction and apply right of use to the remaining leases.
24. Mr. Smith stated that in-substance purchases should not be accounted for in accordance with lease accounting. Rather, he said that lease transactions should be accounted for as a sale, where, for example, title may transfer or terms representing a sale are noted.
25. Ms. Seidman noted that recognition occurs on the statement of financial position regardless of where the line is drawn, and that the more important decision is whether upfront revenue recognition is recognized.
26. Mr. Herz said that there is reasonable traction for an element of a leasing agreement to result in profit recognition. However, the difficulty is determining the delineation of those specific leases.

Issue 2: Plans for Redeliberation

27. Ms. Zeyher asked the Boards whether they had any questions on the overview of the plans of the lease project for lessee redeliberations and the time table provided. She also noted that the staff will be presenting the lessor model in more detail during October.
28. **Board Comments:** Ms. Seidman asked the staff when further analysis on the derecognition approach will be brought to the Boards. Mr. Golden stated that derecognition and revenue recognition must be further deliberated on before a decision being made regarding derecognition in relation to leases. Ms. Seidman indicated that she did not want to defer discussion of lessor issues.
29. Mr. Smith noted that respondents expressed concern on why the Boards are not addressing all executory contracts in contrast to only addressing executory contracts in leases. Mr. Herz stated a need for the Boards to determine whether servicing arrangements should be bifurcated. Mr. Linsmeier said that there is a difference in service arrangements that are completed annually and that are not tied to an asset and those service arrangements that are integral to the acquisition of an asset.
30. The Board agreed on the confirmation of the basic right-of-use model; however, it noted that views could change based on any subsequent analysis of the lessor model.

Follow-up Items:

31. As a follow up to the summarization of the comment letters, the staff provided insight on questions raised during the discussion.
32. The Board questioned whether the respondents who supported excluding short-term leases also were not in favor of the model. After reviewing comments of those respondents who supported excluding short-term leases, approximately 40 percent did not support the right-of-use model. About half of those respondents generally did support the model with certain caveats and the remaining were not clear or did not provide responses on their views of the overall model.
33. The Board also questioned whether respondents who were not in favor of the components approach and supported the Boards' preliminary views not to adopt a components approach also did not support the recognition of contingent rentals and residual value guarantees. Many respondents who supported not to adopt a components approach and provided a clear

view on contingent rentals and residual value guarantees supported that contingent rentals and residual value guarantees should be included in amounts payable under contingent rental arrangements, however, only in certain conditions (for example, only those contingencies that would be recorded under Topic 450 of the *FASB Accounting Standards Codification*TM approach (originally issued as FASB Statement No. 5, *Accounting for Contingencies*).

34. Lastly, the Board questioned if respondents who supported measuring the contingent rentals based on the most likely rental payment were respondents from North America. Of those respondents who supported the most likely rental payment approach, approximately 35 percent were from North America, 30 percent were from Europe, 26 percent were from international organizations, and the remaining were from the Asia-Pacific region.

General Announcements:

None.