

**Emerging Issues Task Force
Agenda Committee Report
August 2, 2005**

	<u>Pages</u>
• Decisions on Proposed Issues	
1. Reevaluation of the Amortization Period for Preexisting Leasehold Improvements to Consider Additional Renewal Periods When New Leasehold Improvements Are Placed into Service Significantly after and Are Not Contemplated at or near the Beginning of the Lease Term	1-4
• Other Matters	
○ Agenda for the September 15, 2005 EITF Meeting	5
○ Status of Open Issues and Agenda Committee Items	6-11

**Emerging Issues Task Force Agenda Committee
Decisions on Proposed Issues**

1. Reevaluation of the Amortization Period for Preexisting Leasehold Improvements to Consider Additional Renewal Periods When New Leasehold Improvements Are Placed into Service Significantly after and Are Not Contemplated at or near the Beginning of the Lease Term

FASB Statement No. 13, *Accounting for Leases*, requires that a lessee determine the *lease term* at the inception of a lease. Paragraph 5(f) of Statement 13 defines lease term as the fixed noncancelable term of the lease plus all periods covered by bargain renewal options or for which failure to renew the lease imposes a penalty on the lessee in such an amount that a renewal appears to be reasonably assured. Once the lease term (including renewals that are deemed reasonably assured) is determined, an entity can then determine (a) the classification of the lease (capital versus operating) and (b) the period to recognize straight-line rents. In accordance with paragraph 9 of Statement 13, the lease term for purposes of lease classification can only change if the provisions of the lease are modified in such a manner that results in the lease being considered a new agreement.

Paragraph 11(b) of Statement 13 requires that assets recognized under capital leases (and in which the lease does not (a) transfer ownership of the property to the lessee at the end of the lease term or (b) contain a bargain purchase option) be amortized in a manner consistent with the lessee's normal depreciation policy except that the amortization period is limited to the lease term (which includes renewal periods that are reasonably assured). In other words, a lessee should expect that it will not control assets recognized under capital leases in periods that are not reasonably assured of renewal. Therefore, the lessee cannot expect to receive any economic benefits from those assets in periods that are not reasonably assured of renewal. While the amortization period of leasehold improvements for operating leases is not addressed in Statement 13, practitioners generally analogize to the guidance provided in paragraph 11(b) of that Statement. This analogy is generally accepted because, similar to assets recognized under capital leases, an entity should expect that it will not control and therefore will not receive any economic benefits from leasehold improvements recognized under operating leases in periods that are not reasonably assured of renewal.

Prior to the Task Force's discussion on EITF Issue No. 05-6, "Determining the Amortization Period for Leasehold Improvements Purchased after Lease Inception or Acquired in a Business Combination," practice had evolved such that leasehold improvements placed in service (or contemplated) at or near the beginning of the initial lease term were amortized over the lesser of the leasehold improvement's useful life or the lease term.

At the June 15–16, 2005 EITF meeting, the Task Force reached a consensus on Issue 05-6 that leasehold improvements placed in service significantly after and not contemplated at or near the beginning of the lease term should be amortized over the shorter of the useful life of the assets or a term that includes required lease periods and renewals that are deemed to be reasonably assured (as defined in paragraph 5 of Statement 13) at the date the leasehold improvements are purchased.

Additionally, the Task Force discussed whether the amortization period for an existing leasehold improvement should be reevaluated after the initial determination of the amortization period, but was not asked to reach a consensus. The Task Force directed the FASB staff to further develop that issue and present it to the EITF Agenda Committee for consideration as a separate Issue for the EITF's agenda.

Accounting Issue and Alternatives

Whether the amortization period for preexisting leasehold improvements should be reevaluated¹ to consider additional renewal periods when new leasehold improvements are placed into service significantly after and are not contemplated at or near the beginning of the lease term.

View A: The amortization period for preexisting leasehold improvements should not be reevaluated to consider additional renewal periods when new leasehold improvements are

¹ Consistent with the consensus reached in Issue 05-6, the reevaluation of the amortization period would be the shorter of the useful life of the assets or a term that includes required lease periods and renewals that are deemed to be reasonably assured at the date of the reevaluation.

placed into service significantly after and are not contemplated at or near the beginning of the lease term.

Proponents of View A note that paragraph 11(b) of Statement 13 requires that assets recognized under capital leases be amortized in a manner consistent with the lessee's normal depreciation policy except that the amortization period is limited to the lease term (which includes renewal periods that are reasonably assured). While Statement 13 does not address the amortization period of leasehold improvements for operating leases, practitioners generally analogize to the guidance in paragraph 11(b). Therefore, proponents of View A do not believe it would be appropriate to reevaluate the amortization period for these preexisting leasehold improvements since it would be in direct conflict with paragraph 11(b).

Additionally, proponents of View A believe that there should be a distinction between preexisting leasehold improvements and leasehold improvements placed in service significantly after the beginning of the lease term. These proponents believe that a distinction between preexisting leasehold improvements and new leasehold improvements is necessary because the determination of the amortization period for the preexisting leasehold improvements is linked to the assumptions used to establish the original lease term whereas the introduction of new leasehold improvements is not linked to those assumptions.

View B: The amortization period for preexisting leasehold improvements should be reevaluated to consider additional renewal periods when new leasehold improvements are placed into service significantly after and are not contemplated at or near the beginning of the lease term.

Based on the consensus reached in Issue 05-6, an entity may consider renewal periods that are reasonably assured at the date a leasehold improvement is placed into service for purposes of determining the amortization period of that asset if it is placed into service significantly after and is not contemplated at or near the beginning of the lease term. Proponents of View B believe that it may be inappropriate to use an assumption regarding the exercise of renewal options in evaluating the amortization period of a preexisting leasehold improvement that is different from the assumption for new leasehold improvements. These proponents believe that in many

instances, new leasehold improvements that are placed into service could extend the useful life of a preexisting leasehold improvement and consequently the amortization period of the preexisting leasehold improvement should reflect that event.

Agenda Committee Decisions: *The Agenda Committee decided not to add this Issue to the EITF Agenda. Rather, the Agenda Committee agreed to propose that the Task Force clarify that the consensus reached in Issue 05-6 does not apply to preexisting leasehold improvements. Therefore, the amortization period for preexisting leasehold improvements should not be reevaluated as a result of the consensus reached in Issue 05-6 to consider additional renewal periods when new leasehold improvements are placed into service significantly after and are not contemplated at or near the beginning of the lease term.*

The Task Force will be asked to modify the consensus reached in Issue 05-6 to include the following:

At the September 15, 2005 EITF meeting, the Task Force agreed to clarify that the consensus reached in Issue 05-6 does not apply to preexisting leasehold improvements. Therefore, the consensus reached in Issue 05-6 should not be used to justify the reevaluation of preexisting leasehold improvements for additional renewal periods when new leasehold improvements are placed into service significantly after and are not contemplated at or near the beginning of the lease term.

FASB EMERGING ISSUES TASK FORCE
Proposed September 15, 2005 Meeting Agenda

<u>Issue Number</u>	<u>Issue</u>	<u>Proposed Time</u>	<u>Staff Assigned</u>
04-13	Accounting for Purchases and Sales of Inventory with the Same Counterparty	8:00-9:00	Geary/ Oakley/ Belcher
05-1	Accounting for the Conversion of an Instrument That Becomes Convertible upon the Issuer's Exercise of a Call Option	9:00-10:00	Oakley/ Sarno
	* * * BREAK * * *	10:00-10:15	
05-4	The Effect of a Liquidated Damages Clause on a Financial Instrument Subject to EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"	10:15-11:45	Thuener/ Jacobs/ Richards
	Administrative Matters	11:45-12:15	Geary
	- New Issues		
	- Addendum to Issue 05-6 ¹		
	- Other Matters		
	* * * LUNCH * * *	12:15-1:15	
05-F	Accounting for Modifications to Conversion Options Embedded in Debt Securities and Related Issues	1:15-2:45	Cosper/ Jacobs
	* * * BREAK * * *	2:45-3:00	
05-G	Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature	3:00-4:15	Beswick/ Sarno

¹ Please see the decision reached by the EITF Agenda Committee on page four for the proposed new issue: "Reevaluation of the Amortization Period for Preexisting Leasehold Improvements to Consider Additional Renewal Periods When New Leasehold Improvements Are Placed into Service Significantly after and Are Not Contemplated at or near the Beginning of the Lease Term"

Status of Open Issues and Agenda Committee Items

The following represents the FASB staff's assessment of the status and immediate plans with respect to the open Issues on the Task Force's agenda. The Issues on the proposed agenda for the September 15, 2005 meeting are considered either high priority issues or issues on which meaningful progress can be made within the staff's given complement of resources. The staff's prioritization of issues is based primarily on the FASB staff's understanding of the level of diversity in practice created by each respective Issue, the financial reporting implications of that diversity, the current interaction, if any, of the Issues with active Board projects, and current resource availability among the staff (with respect to both time and relevant technical expertise).

Issue No.	Description	Date Added	Date(s) Discussed	Next Meeting	FASB Staff	EITF Member Liaison	Immediate Plans	Due Date - Next Deliverable
04-13	Accounting for Purchases and Sales of Inventory with the Same Counterparty	11/04	11/04, 3/05, 6/05	9/05	Geary/ Oakley/ Belcher	Brod	A draft abstract will be posted to the FASB website for public comment by July 7, 2005. The Task Force will consider the comments received at the September 2005 meeting.	September meeting materials
05-1	Accounting for the Conversion of an Instrument That Becomes Convertible upon the Issuer's Exercise of a Call Option	11/04	3/05, 6/05	9/05	Oakley/ Sarno	Graziano	The FASB staff will prepare an Issue Summary for the September 2005 meeting.	September meeting materials

Issue No.	Description	Date Added	Date(s) Discussed	Next Meeting	FASB Staff	EITF Member Liaison	Immediate Plans	Due Date - Next Deliverable
05-4	The Effect of a Liquidated Damages Clause on a Financial Instrument Subject to EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock"	2/05	6/05	9/05	Thuener/ Jacobs/ Richards	Johnson	The FASB staff will prepare an Issue Summary for the September 2005 meeting.	September meeting materials
05-F	Accounting for Modifications to Conversion Options Embedded in Debt Securities and Related Issues	5/05	N/A	9/05	Cosper/ Jacobs	Holman	The FASB staff will prepare an Issue Summary for the September 2005 meeting.	September meeting materials
05-G	Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature	5/05	N/A	9/05	Beswick/ Sarno	Bielstein	The FASB staff will prepare an Issue Summary for the September 2005 meeting.	September meeting materials

Other EITF Issues including Inactive Issues Pending Developments in Board Projects							
Issue No.	Description	Date Added	Date(s) Discussed	Next Meeting	FASB Staff	Immediate Plans	Due Date - Next Deliverable
00-18	Accounting Recognition for Certain Transactions involving Equity Instruments Granted to Other Than Employees	5/00	7/00, 7/01, 11/01, 1/02, 3/02	Not scheduled	Sarno	Pending further progress on Phase II of the Board's share-based payments project.	N/A
<p><i>The remaining issue in Issue 00-18 is Issue 3: For transactions that include a grantee performance commitment, how the grantee should account for the contingent right to receive, upon performing as specified in the arrangement, grantor equity instruments that are the consideration for the grantee's future performance. The Task Force asked the FASB staff to focus on improving the guidance (originally from Issue 96-18) used to determine the date at which a commitment for counterparty performance to earn the equity instruments is reached.</i></p>							
00-27	Application of EITF Issue No. 98-5, "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios," to Certain Convertible Instruments	5/00	11/00, 1/01	Not scheduled	Richards	Pending further progress on Phase II of the Board's liabilities and equity project.	N/A

Other EITF Issues including Inactive Issues Pending Developments in Board Projects							
Issue No.	Description	Date Added	Date(s) Discussed	Next Meeting	FASB Staff	Immediate Plans	Due Date - Next Deliverable
02-D	The Effect of Dual-Indexation both to a Company's Own Stock and to Interest Rates and the Company's Credit Risk in Evaluating the Exception under Paragraph 11(a)(1) of FASB Statement No. 133, <i>Accounting for Derivative Instruments and Hedging Activities</i>	3/02	N/A	Not scheduled	Jacobs	Pending further progress on Phase II of the Board's liabilities and equity project.	N/A
03-15	Interpretation of Constraining Conditions of a Transferee in a Collateralized Bond Obligation Structure	9/00 (AC) 11/02 (TF)	N/A	Not scheduled	Lusniak	Pending developments in the Board's project on QSPE's and reconsideration by the FASB staff as to the extent of the issue.	N/A

Other EITF Issues including Inactive Issues Pending Developments in Board Projects							
Issue No.	Description	Date Added	Date(s) Discussed	Next Meeting	FASB Staff	Immediate Plans	Due Date - Next Deliverable
03-17	Subsequent Accounting for Executory Contracts That Have Been Recognized on an Entity's Balance Sheet	5/03	11/03	Not scheduled	Moss	Issue addresses the amortization of a recognized executory contract that has periods of both positive and negative cash flows. This issue is pending the Board's consideration of how the factors in paragraph 11(d) of Statement 142 should be evaluated in determining the useful life of an intangible asset (formerly EITF Issue 03-9).	N/A
04-7	Determining Whether an Interest Is a Variable Interest in a Potential Variable Interest Entity	5/04	6/04, 9/04, 11/04, 3/05	9/05	Belcher	At its March 30, 2005 meeting, the Board agreed to add a project to provide guidance on the variability that should be considered when determining whether an interest is a variable interest. The FASB staff will ask the Task Force to remove this Issue from its agenda at the September 2005 meeting.	N/A

Issues Pending Further Consideration by the Agenda Committee							
Issue No.	Description	Date Added	Date(s) Discussed	Next Meeting	FASB Staff	Immediate Plans	Due Date - Next Deliverable
N/A	Application of EITF Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets," When a Special-Purpose Entity Holds Equity Securities and Whether an Investment That Is Redeemable at the Option of the Investor Should Be Considered an Equity Security or Debt Security	9/00	N/A	Not scheduled	Jacobs	Pending consideration of an FASB project that may address the measurement of beneficial interests in securitized financial instruments.	Pending developments in a Board project