MINUTES

Financial Accounting Standards Board

To:	FASB Board Members
From:	Leases Team (Paul x263)
Subject:	January 6, 2011, Roundtable Minutes: Leases, Norwalk Afternoon Session
Date:	June 28, 2011

Topic: Proposed Accounting Standards Update: *Leases*

Length of Discussion: 1:00 p.m. to 4:00 p.m.

Attendance:

Outside Participants

Kimber Bascom	KPMG
Marc Betesh	KBA Lease Services
Bill Bosco	Leasing Industry/Working Group Member
John Briscoe	Transocean
Richard Jones	Ernst & Young
Charles Knight	Toys R Us
Jenifer Minke-Girard	SEC
Kurt Schwarz	AIG
Kelvin Smith	Financial Computer Systems, Inc.
Bill Solomon	Aviation Working Group
Robert Sorrentino	Xerox
Gerry White	CFA Institute

FASB & IASB Participants

Leslie Seidman	FASB Chairman
Russ Golden	FASB Board Member
Tom Linsmeier	FASB Board Member
Marc Siegel	FASB Board Member
Larry Smith	FASB Board Member
Patrick Finnegan	IASB Board Member
Paul Pacter	IASB Board Member
Kevin Stoklosa	FASB Assistant Director
Danielle Zeyher	FASB Project Manager

Henry Rees IASB Technical Principal
David Humphreys IASB Practice Fellow

SCOPE

1. Participants from the auditing and leasing industries noted that the significance of the services included in a lease contract should be considered in scoping and defining a lease.

2. Other participants from the auditing and leasing industries noted that an economic benefit can be derived from the intangible right to use an asset without identifying the specific asset.

3. Many respondents, including those from the auditing, airline, and leasing industries, expressed concerns over the accounting for executory contracts and their distinction from leases. A respondent from the auditing industry noted that treatment of executory contracts should be consistent regardless of whether those contracts are embedded in lease contracts. Another respondent from the leasing industry noted that once the distinction between the lease and service components of a contract is made, the accounting for the lease becomes less problematic under the proposed guidance.

4. A respondent from the airline industry stated that under the proposed guidance, basic (*dry*) and full service (*wet*) leases would produce different accounting outcomes while the economics of the two contracts are the same.

5. A respondent from the airline industry noted that lessors do not necessarily agree that a lease is a financing agreement.

6. A participant from the leasing industry expressed concern that the proposed guidance does not provide enough clarification for lease contracts that are structured on different bases.

7. A participant from the oil industry expressed concern that contracts specifically structured as service contracts will be inappropriately included in the scope of the proposed guidance.

LESSOR MODEL

8. Many respondents agreed with the need for two models of accounting for lease transactions entered into by the lessor. However, respondents noted the issues related to the proposed guidance for the lessor, including consistency with the revenue recognition project and clarity of the proposed guidance.

9. Many participants expressed concern with the difficulty of determining the model that is applicable to a particular transaction under the proposed guidance. A participant from the leasing industry suggested that the type of additional services included in the contract would be more appropriate than a distinction based on significant risks and benefits. Other participants suggested the significance of ongoing performance by the lessor as an appropriate distinction. However, a participant from the financial services industry noted the subjectivity of *significance* in applying the suggested distinction.

10. Participants in the auditing, leasing, airline, and financial services industries expressed concern over the pattern of revenue recognition that would occur under the two models in the proposed guidance. A participant from the auditing industry noted that the amount of pretax net income for a contract can differ between the two models. A participant from the leasing industry noted that the pattern of revenue recognition should differ based on whether the ownership right or the right of use of an asset is transferred.

11. A participant from the financial services industry noted the difficulty in testing the multiple assets capitalized under the proposed guidance for impairment.

12. Participants in the airline and financial services industries stated that a major change to the accounting for the lessor may not be needed. A participant from the airline industry noted that equity analysts and users have not raised significant issues with the current approach to accounting for the lessor, including operating lease treatment.

13. A participant from the leasing industry expressed support for the proposed derecognition model with operating lease or fair value treatment for lease contracts that do not fit the scope of the derecognition model.

LEASE TERM

14. Participants from the leasing and financial services industries expressed concern over the phrase "more likely than not" in the definition of lease term in the proposed guidance. A participant from the leasing industry stated that while a tenant will usually stay in a space after a lease term is complete, the tenant rarely exercises a renewal option as is and renegotiates a new lease. A participant from the financial services industry noted that a threshold higher than *more likely than not* is needed.

15. Many respondents, including those in the oil drilling and software industries, spoke about the difficulties inherent in predicting whether lessees will exercise renewal or termination options. A respondent in the software industry stated that significant leasehold improvements to a property should mean economic compulsion to renew the lease term. However, a respondent from the oil drilling industry noted several intangible factors considered in a lessee's decision to exercise a lease term option.

16. A user suggested using expected value over a portfolio of leases to measure the lease term. However, a participant from the financial services industry disagreed with expected value because it may produce partial years in the term calculations.

17. A participant from the software industry expressed concern that the proposed guidance does not properly reflect the economics of different lease term structures. For example, a 1-year initial lease term with 14 renewal options has value in its flexibility that a 15-year term does not.

18. A respondent from the auditing industry suggested the current definition of a lease term included in *FASB Accounting Standards Codification Topic®* 840, Leases, as an appropriate alternative definition.

VARIABLE PAYMENTS

19. A participant from the financial services industry stated that contingent rental payments should not be included in the proposed guidance because they do not meet the definition of

an asset or a liability. Participants from the software and airline industries agreed by stating that contingent rental payments do not meet the definition of a liability.

20. Users and participants from the auditing industry noted that the proposed probability-weighted approach is inappropriate because it is too complex and does not reflect the different economics in the different kinds of variable payments. One participant from the auditing industry suggested a best estimate approach for some variable payments and current guidance for indexed rental payments. Another participant from the auditing industry suggested expensing contingent rental payments. A user suggested using expected value over a portfolio of leases for the measurement of variable lease payments.

21. Respondents from the leasing and software industries noted that periodic reassessment of variable lease payments would be complex and impractical.

22. A participant from the leasing industry noted that the revenue recognized at the beginning of a lease term under the proposed guidance for variable lease payments does not properly reflect the economics of a lease transaction.