MINUTES

FINANCIAL ACCOUNTING STANDARDS BOARD

MEMORANDUM

To:	Board Members
From:	Leases Team (Gwizdala x263)
Subject:	Minutes of February 25, 2015 Board Meeting
Date:	March 4, 2015
cc:	Sutay

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 or a Statement of Financial Accounting Concepts.

Topic:	Leases
Basis for Discussion:	FASB Memo 305-310: Cover Memo, Reassessment of Variable Lease Payments, Lessee Transition, Lessor Transition, Sale and Leaseback Transition, Build-to-Suit Lease Arrangements
Length of Discussion:	February 25, 2015—12:40PM to 02:00PM EST

Attendance:

Board members present:	Golden, Kroeker, Buck, Schroeder, Linsmeier, Siegel, Smith
Board members absent:	None
Staff in charge of topic:	Zeyher
Other staff at Board table:	Cosper, Esposito, Muir, Muehlbauer, Winkler, Gwizdala
Outside participants:	None

Type of Document and Timing Based on the Technical Plan:

The FASB continued redeliberating the proposals in the May 2013 Exposure Draft, *Leases*, specifically discussing the following topics: (1) reassessment of variable lease payments, (2) lessee transition, (3) lessor transition, (4) sale and leaseback transition, (5) build-to-suit lease arrangements, and (6) sweep issue—lessee disclosure of the weighted-average discount rate for Type A leases.

Tentative Board Decisions:

Reassessment of Variable Lease Payments

The Board affirmed that a lessee should reassess variable lease payments that depend on an index or a rate only when the lessee remeasures the lease liability for other reasons (for example, because of a change in the lease term resulting from a reassessment).

(FASB: 4-3)

Lessee Transition

The Board decided to require a lessee to apply a modified retrospective transition approach for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements (the date of initial application). The modified retrospective approach would not require any transition accounting for leases that expired before the date of initial application. The Board decided to not permit a full retrospective transition approach.

The modified retrospective transition approach should be applied to existing leases as follows:

Capital Leases

1. A lessee should initially recognize a Type A right-of-use (ROU) asset and lease liability at the later of (a) the date of initial application and (b) the date of initial recognition under Topic 840, Leases, measured at the carrying amount of the capital lease asset and capital lease obligation under Topic 840 immediately before that date.
2. Any unamortized initial direct costs not included in the capital lease asset under Topic 840 that would have qualified for capitalization under the new leases standard should be subsumed into the Type A ROU asset; otherwise, those costs that would not have qualified for capitalization should be written off as an adjustment to equity.

3. Before the effective date, a lessee should subsequently measure the Type A ROU asset and lease liability in accordance with the subsequent measurement guidance in Topic 840.
4. Beginning on the effective date, a lessee should subsequently measure the Type A ROU asset and lease liability in accordance with the subsequent measurement guidance in the new leases standard, except that a lessee should not remeasure the Type A ROU asset or lease liability for changes in the amount the lessee expects to pay under residual value guarantees unless it remeasures the asset or liability for other reasons (for example, because of a change in the lease term resulting from a reassessment).
5. Beginning on the effective date, if a lessee modifies the lease (and that modification is not a separate lease) or is required to remeasure the lease liability for any reason, it should follow the new leases standard.

Operating Leases

1. A lessee should initially recognize a Type B ROU asset and lease liability at the later of (a) the date of initial application and (b) lease commencement.
2. Unless the lease is modified (and that modification is not a separate lease), or the lease liability is required to be remeasured, on or after the effective date, a lessee should initially and subsequently measure the lease liability at the present value of the sum of:
    a. The remaining *minimum rental payments* (as defined under Topic 840) plus
    b. Any amounts the lessee expects to pay to satisfy a residual value guarantee, using a discount rate established in accordance with the new leases standard as of the “later of” date.
3. A lessee should measure the Type B ROU asset throughout the lease at an amount equal to the lease liability, adjusted for any prepaid or accrued rent, lease incentives, or unamortized initial direct costs that would have qualified for capitalization under the new leases standard.
4. Any unamortized initial direct costs at the “later of” date that would not have qualified for capitalization under the new leases standard should be written off as an adjustment to equity.
5. Beginning on the effective date, if a lessee modifies the lease (and that modification is not a separate lease) or is required to remeasure the lease liability for any reason, it should follow the new leases standard.

The Board further decided to permit a lessee to elect the following specified reliefs, which must be elected as a package and must be applied to all of a lessee’s leases (that is, they cannot be elected on a lease-by-lease or relief-by-relief basis):

1. A lessee need not reassess whether any expired or existing contracts are or contain leases.
2. A lessee need not reassess the lease classification for any expired or existing leases.
3. A lessee need not reassess initial direct costs for any existing leases (that is, whether those costs would have qualified for capitalization under the new leases standard).

Lastly, the Board also decided to permit a lessee to elect to use hindsight with respect to lease renewals and purchase options when accounting for existing leases. This specified relief may be elected separately or in conjunction with the above specified reliefs as an accounting policy election (that is, it cannot be elected on a lease-by-lease basis).

(FASB: 5-2)

Lessor Transition

The Board decided to require a lessor to apply a modified retrospective transition approach for sales-type, direct financing, and operating leases existing at, or entered into after, the date of initial application. The modified retrospective approach would not require any transition accounting for leases that expired before the date of initial application. The Board decided to not permit a full retrospective transition approach.

The modified retrospective transition approach should be applied to existing leases as follows:

Sales-Type/Direct Financing Leases

1. A lessor should not reassess whether a sales-type lease would have qualified for upfront selling profit recognition in accordance with the new leases standard.
2. A lessor should initially recognize a net investment in the lease at the later of (a) the date of initial application and (b) lease commencement, measured at the carrying amount of the net investment in the lease under Topic 840 immediately before that date. For a direct financing lease, the net investment in the lease should include any unamortized initial direct costs that were capitalized in accordance with Topic 840.
3. Before the effective date, a lessor should subsequently measure its net investment in the lease in accordance with the subsequent measurement guidance in Topic 840.
4. Beginning on the effective date, a lessor should subsequently measure the net investment in the lease in accordance with the subsequent measurement guidance in the new leases standard.

5. Beginning on the effective date, if a lessor modifies the lease (and that modification is not a separate lease), it should follow the new leases standard.

Operating Leases

1. The carrying amount of the underlying asset and any lease assets or liabilities (for example, prepaid or deferred rent) should be the same as that recognized under Topic 840 at the later of (a) the date of initial application and (b) lease commencement.
2. If a lessor had previously securitized receivables arising from leases that were classified as operating leases in accordance with Topic 840, the lessor should account for those transactions as secured borrowings in accordance with other Topics.
3. A lessor should recognize any initial direct costs that would have qualified for capitalization under the new leases standard as an expense over the lease term on the same basis as lease income; otherwise, those costs that would not have qualified for capitalization should be written off as an adjustment to equity as of the applicable "later of" date.

The Board decided that a lessor may apply the same specified reliefs as permitted for a lessee subject to the same restrictions. The Board decided that the specified relief elections must be consistently applied by an entity for all lessee and lessor leases (that is, an entity that is a lessee and a lessor must make the same specified relief elections).

(FASB: 6-1)

Lessee and Lessor Transition Disclosures

The Board decided that lessees and lessors should provide transition disclosures consistent with Topic 250, Accounting Changes and Error Corrections, without the disclosure of 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 (that is, without the requirements in paragraph 250-10-50-1(b)(2)).

(FASB: 7-0)

Sale and Leaseback Transition

Accounting for Previous Sale and Leaseback Transactions

The Board decided that an entity should not reassess whether a transaction previously accounted for as a sale and leaseback transaction under Topic 840 would have qualified as a sale (or purchase) in accordance with Topic 606, Revenue from Contracts with Customers.

(FASB: 7-0)

The Board decided that an entity should account for the leaseback in any transaction that qualified as a sale and leaseback under Topic 840 in accordance with the lessee and lessor transition requirements.

(FASB: 7-0)

Deferred Gain or Loss Treatment for Sale and Capital Leaseback

The Board decided that for any transaction previously accounted for as a sale and *capital* leaseback transaction under Topic 840, the seller-lessee should continue to amortize any deferred gain or loss.

(FASB: 4-3)

Deferred Gain or Loss Treatment for Sale and Operating Leaseback

The Board decided that for any transaction previously accounted for as a sale and *operating* leaseback transaction under Topic 840:

1. The seller-lessee should recognize 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 and the date of sale.
2. Any seller-lessee deferred gains or losses that resulted from off-market sales and leaseback terms should be recognized as an adjustment to the leaseback ROU asset (if a deferred loss) or accounted for as a remaining financial liability (if a deferred gain) at the date of initial application.

(FASB: 7-0)

Build-to-Suit Lease Arrangements

The Board decided to affirm its current tentative decision to not include specific guidance about lessee involvement in asset construction in the new leases standard other than the guidance that was proposed in the 2013 Exposure Draft (paragraph 842-40-55-2).

(FASB: 7-0)

The Board decided to require a lessee to apply a modified retrospective transition approach for build-to-suit lease arrangements existing at, or entered into after, the date of initial application. The modified retrospective approach would not require any transition accounting for build-to-suit leases that expired before the date of initial application.

The modified retrospective transition approach should be applied to existing build-to-suit leases as follows:

1. An entity that has recognized assets and liabilities solely as a result of a transaction's build-to-suit designation in accordance with Topic 840 should derecognize those assets and liabilities at the later of (a) the date of initial application and (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 should be recorded as an adjustment to equity at that date. The lessee should then follow the general lessee transition guidance for the lease itself as it would have had the lease not been accounted for in accordance with the build-to-suit guidance.
2. For build-to-suit lease arrangements in which the construction period ended before the date of initial application, but the lease term is not expired as of that date, and the transaction qualified as a sale and leaseback transaction under the existing guidance in Subtopic 840-40 before that date, the entity should apply the lessee transition requirements.

(FASB: 7-0)

Sweep Issue—Lessee Disclosure of the Weighted-Average Discount Rate for Type A Leases

The Board decided to require a lessee to disclose the weighted-average discount rate for Type A leases as of the reporting date together with the other quantitative disclosure requirements that were decided by the Board at the January 2015 joint FASB/IASB Board meeting.

(FASB: 4-3)

Next Steps

The Board will discuss private company considerations at a future Board meeting. The staff will also begin drafting a final leases standard based on the tentative decisions reached by the Board. Later in the drafting process, the Board will discuss the benefits and costs of the new leases standard, effective date, and any sweep issues that arise during drafting of the final leases standard.