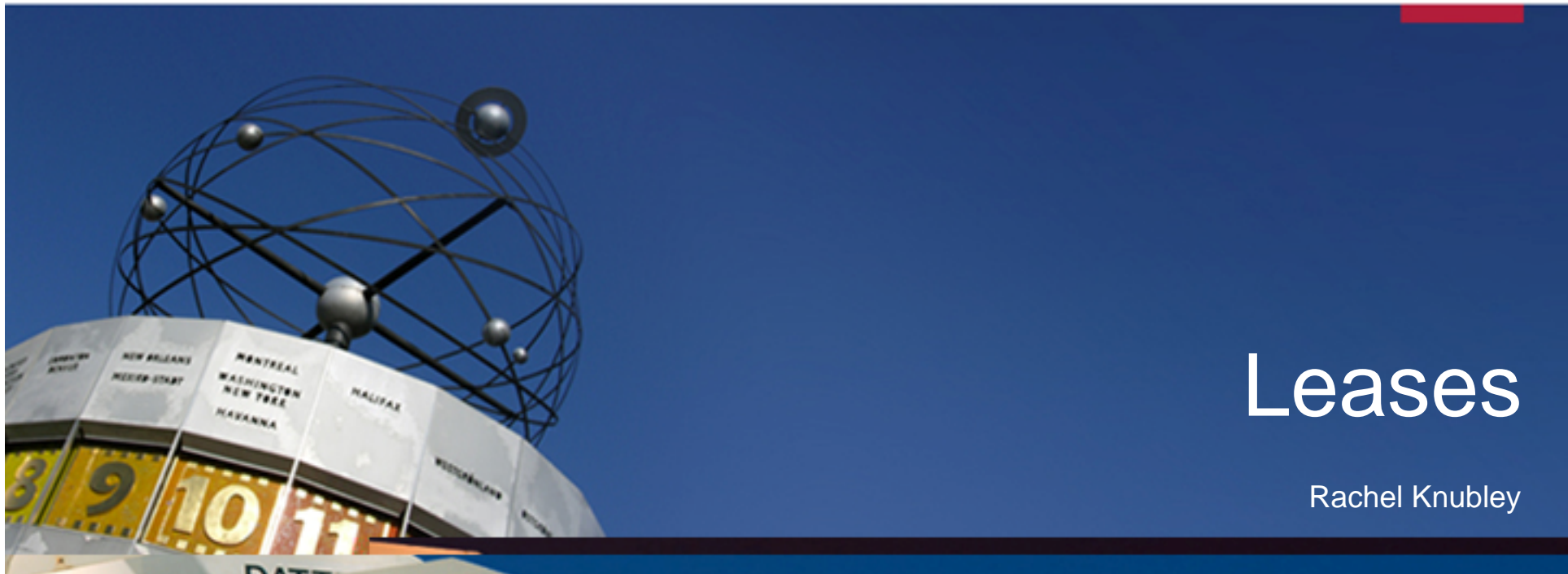


July 2009

International Financial Reporting Standards

GLOBAL PREPARERS FORUM
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AGENDA PAPER 2



Leases

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The views expressed in this presentation are those of the presenter, not necessarily those of the IASC Foundation or the IASB



Overview

- Scope
- Approach – simple lease
- Initial measurement
- Subsequent measurement
- Approach – more complex leases
- Leases with options
- Contingent rentals
- Lessor accounting
- Next steps
- Discussion questions



- Based on scope of existing standards
 - Need to reconcile scopes of IAS 17 and SFAS 13
- Some constituents have suggested scope exclusions for:
 - Non-core asset leases
 - Short term leases



Approach – simple lease

- Identified the rights and obligations
- Decided whether they meet the definition of an asset or liability
- The lessee recognises:
 - A right-of-use asset
 - An obligation to pay rentals
- Other approaches considered (but rejected)
 - Whole asset
 - Executory contract



- Obligation to pay rentals
 - Present value of lease payments discounted using the lessee's incremental borrowing rate
- Right-of-use asset
 - Cost = Present value of lease payments discounted using the lessee's incremental borrowing rate



Subsequent measurement

- Obligation to pay rentals
 - Amortised cost
 - Incremental borrowing rate
 - FASB would not require reassessment
 - IASB would require reassessment
- Right-of-use asset
 - Amortised cost
 - Impairment approach to be determined



Approach – more complex leases

- Leases often include:
 - Options to extend, terminate or purchase
 - Obligations to pay contingent rentals
 - Residual value guarantees
- Could recognise and measure components of a lease separately
- Boards decided not to adopt a components approach
- Lessee recognises
 - A single right-of-use asset that includes rights acquired under options
 - A single obligation to pay rentals that includes obligations arising from contingent rentals and residual value guarantees



Leases with options

- Address uncertainty about lease term through recognition
- Recognise an obligation to pay rentals for a specified lease term

Example

- A machine is leased for 10 years
- Lease includes an option to extend for an additional 5 years
- Lessee must decide whether to recognise:
 - an obligation to pay 10 years of rentals
 - an obligation to pay 15 years of rentals



Leases with options

- Determine **most likely** lease term
- Consider
 - Contractual
 - Non-contractual
 - Business factors
- Reassessment at each reporting date
- Recognise change in obligation as an adjustment to the right-of-use asset
- Purchase options
 - Account for in the same way as renewal options



Contingent rentals

- Rentals that vary with
 - Price changes or an index
 - Lessee's performance (eg sales)
 - Usage
- Obligation to pay contingent rentals = liability
 - Include in measurement of obligation to pay rentals
- Measurement
 - IASB – probability weighted estimate of amount payable
 - FASB – most likely rental payment
 - FASB – if based on an index, use index or rate existing at reporting date



Contingent rentals

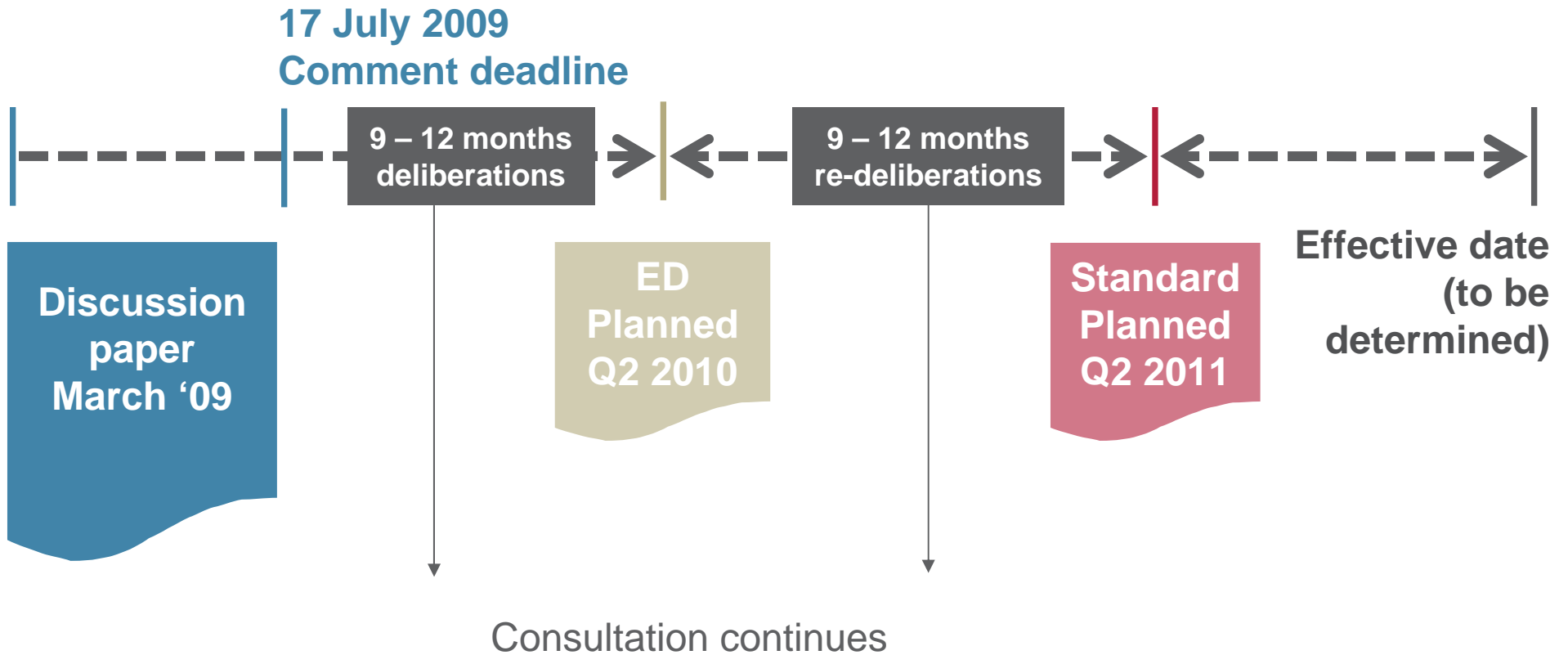
- Remeasurement
 - At each reporting date
- Changes arising from reassessment
 - IASB – as an adjustment to the right-of-use asset
 - FASB – in profit or loss
- Residual value guarantees
 - Account for in the same way as contingent rentals



- July 2008
 - Defer lessor
 - Concentrate on developing lessee accounting
- DP describes lessor issues
 - No preliminary views
- May & July 2009
 - Discussed lessor model in overview
 - Derecognition approach vs. Recognition of a performance obligation
 - Measurement issues
- Next steps
 - Decide whether to include lessor accounting in ED



Next steps



Scope

- What additional guidance (if any) do you think is needed to differentiate service contracts from lease contracts?
- Should a new standard include exemptions for short-term leases or leases of non-core assets? How would you define those leases that would be excluded from the scope?

Approach

- Do you support the right of use approach or would you prefer an alternative approach?



Discussion questions

Measurement

- Do you agree with the proposal to discount the lease payments using the lessee's incremental borrowing rate?
- Should the lessee be required to reassess the incremental borrowing rate after initial recognition?

Options

- Do you agree with the proposed approach to options? What alternative approach would you recommend?



Contingent rentals

- Do you support including contingent rentals in the obligation to pay rentals?
- Which of the two approaches to measurement of contingent rentals do you support (probability weighted or most likely amount)?

Lessor accounting

- Is lessor accounting a significant issue for you?



Discussion questions

General

- What are the practical problems associated with the proposed approach?
- Do you have any suggestions for simplifying the proposed approach to lessee accounting?



Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged. The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.

