	IASB/FASB Meeting **Week commencing April 11, 2011**	IASB Agenda reference	**1E**
Staff Paper	***IASB Education Session April 6, 2011*** ***FASB Education Session April 7, 2011***	FASB Agenda reference	**159**

Project	**Leases**
Topic	**Types of Leases – Cover Memo**

Objective

1. The purpose of this paper is to provide an overview of the discussion regarding whether there is more than one type of lease for accounting purposes and whether or not all leases should have a similar profit or loss recognition pattern. Additionally, this paper outlines and provides an executive summary of the series of papers on this topic.

2. In this series of papers the staff plan to discuss the following questions:

   (a) Are there different types of leases for accounting purposes for lessors and lessees?

   (b) If there are different types of leases, how can you distinguish one type (finance lease) from another (other-than-finance lease)?

   (c) Assuming there are different types of leases,

      (i) How should a lessee account for an other-than-finance lease?

      (ii) How should a lessor account for an other-than-finance lease?

      (iii) How should a lessee account for a finance lease?

      (iv) How should a lessor account for a finance lease?

3. In the February 2011 joint meeting, the staff presented Agenda paper 5F / FASB Memo 134 which introduced the discussion on types of leases and presented the Boards with the comment letter feedback on the topic. The objective of 5F / Memo 134 was to seek the Boards approval to perform targeted outreach on the topic and bring the topic back to the Boards in a decision making meeting.

4. The staff performed targeted outreach during March and April 2011 involving over 20 separate meetings and interacting with over 70 entities including users, preparers, accounting firms, standard-setters and the joint working group. The result of the targeted outreach feedback is provided in detail throughout the memos on this topic.

5. This topic is explored further in this series of papers which includes the following memos:

   (a) Agenda paper 1F /FASB Memo 160 – *Types of leases – are there different types?*

   (b) Agenda paper 1G / FASB Memo 161 – *Determining the lease to be a finance lease or an other-than-finance lease*.

   (c) Agenda paper 1H / FASB Memo 162 – *Lessees – Other-than-finance leases*.

   (d) Agenda paper 1I / FASB Memo 163 – *Lessors – Other-than-finance leases*.

   (e) Agenda paper 1J / FASB Memo 164 – *Lessees – finance leases*.

   (f) Agenda paper 1K / FASB Memo 165 – *Lessors – finance leases*.

Executive summary of other papers

Agenda paper 1F / FASB Memo 160 – Types of leases – are there different types?

6. This paper discusses whether or not the profit or loss recognition pattern should be different for different types of leases. Specifically, for lessors and lessees, is there an accounting distinction to be made for profit or loss recognition patterns where:

(i) a finance lease would recognize income/expense using an effective interest method whereby income/expense is recognized at a higher amount in earlier periods of the lease term than later periods and

(ii) an other-than-finance lease would recognize a straight-line profit or loss pattern, unless another systematic and rational basis is more representative of the time pattern in which benefit is derived from the asset.

7. This paper builds on the discussion in the February 2011 Joint Board Meeting and provides feedback from the targeted outreach on the topic. The paper first discusses the advantages and disadvantages of a single lessor approach to profit or loss recognition and then discusses the advantages and disadvantages of a single approach to profit or loss recognition for lessees.

Agenda paper 1G / FASB Memo 161 – Determining the lease to be a finance lease or an other-than-finance lease.

8. This paper discusses the principles and indicators that may be used to differentiate the types of leases (finance and other-than-finance) for both lessors and lessees. This paper builds on the discussion in the February 2011 Joint Board Meeting and provides feedback from the targeted outreach on the topic.

9. The paper outlines the following three approaches to differentiate between a finance and an other-than-finance lease for lessees and lessors:

(a) Retain current IAS 17 principles and supporting indicators.

(b) Utilize new principles and supporting indicators as outlined in the targeted outreach, amended for feedback.

(c) Develop a new principle based on whether the underlying asset is significantly consumed during the lease term.

Agenda paper 1H / FASB Memo 162 – Lessee Accounting – other-than-finance leases

10. This paper assumes that there are two types of leases for lessees and outlines potential initial and subsequent measurement and presentation approaches to apply by lessees for an other-than-finance type lease.

11. All approaches for a lessee other-than-finance lease lead to a systematic or rational method (for example straight-line) profit or loss recognition pattern. The paper outlines the initial and subsequent measurement approaches as follows:

    (a) **Approach A** – ***Linked approach*** – ROU asset is linked to the liability to make lease payments both initially and throughout each subsequent period of the lease.

    (b) **Approach B** – ***Annuity based amortization approach*** – While the ROU asset and liability to make lease payments are linked at inception of the lease, the ROU asset is independent of the liability for lease payments in all subsequent periods. The ROU asset is amortized based on the pattern of benefits used during the lease term.

    (c) **Approach C** – ***OCI approach*** – Straight-line method of profit or loss recognition pattern achieved through use of other comprehensive income (OCI).

12. This paper also discusses presentation of lease expenses as either:

    (a) All recognized within a single line item within operating expense (for example, rent expense)

    (b) A portion of the lease expense recognized as interest expense and the remainder recognized as amortization/depreciation expense.

Agenda paper 1I / FASB Memo 163 – Lessor Accounting – other-than-finance leases

13. This paper again assumes that there are two types of leases for lessors and outlines potential accounting approaches a lessor could apply to an other-than-finance lease transaction.

14. The objective of this paper is to analyze the possible recognition approaches for other-than-finance leases. All of the approaches in this paper reflect a view

that the lessor is performing (by allowing the lessee to use the lessor's underlying asset) under the terms of the lease arrangement continuously over the lease term.

15. First, this paper considers the accounting by the lessor in the statement of financial position for other-than-finance leases:

    (a) Gross presentation of lease assets and liabilities (as proposed in the 'performance obligation' approach in the exposure draft);

    (b) Net presentation of leases assets and liabilities; and

    (c) No recognition of lease assets and liabilities (consistent with current operating lease accounting).

16. Next, this paper considers the impacts on the profit or loss. The alternatives proposed are consistent with those outlined for a lessee other-than-finance lease.

17. Finally, this paper discusses certain impairment considerations.

Agenda paper 1J / FASB Memo 164 – Lessee Accounting – finance leases

18. This paper again assumes that there are two types of leases for lessees and outlines potential accounting approaches that a lessee should apply to a finance type lease.

19. The paper outlines the initial measurement approach, consistent with the proposals in the ED, to recognise a right-of-use asset and a liability to make lease payments, measured at the present value of the future lease payments.

20. Additionally, this paper outlines the subsequent measurement approach for finance leases, including whether:

    (a) the right-of-use asset should be subsequently amortised on a systematic basis, consistent with the proposals in the ED, or using a mortgage-based approach.

    (b) the liability to make lease payments should be subsequently measured using the effective interest method or using a fair value approach.

Agenda paper 1K / FASB Memo 165 – Lessor Accounting – finance leases

21. This paper again assumes that there are two types of leases for lessors, consistent with the proposals in the ED, and outlines potential accounting approaches a lessor could apply for a finance lease.

22. The objective of this paper is to analyze the possible recognition approaches for finance leases. The approaches in this paper reflect the view that the lessor has performed on the commencement date of the lease contract.

23. This paper analyzes the measurement and presentation of lease assets in accordance with the finance lease for lessors, including the lease receivable and the residual asset.

24. This paper also analyzes the lessor's accounting for the underlying asset, that is, how much of the underlying asset should be derecognized at the commencement of the lease.