Objective

1. The purpose of this paper is to discuss the accounting for variable lease payments in a lease arrangement that meet a high threshold.

2. This paper also discusses the subsequent measurement of those variable lease payments.

3. This paper is organized as follows:

   (a) Summary of staff recommendations

   (b) Background

   (c) Summary of feedback received (including feedback on practical application of current guidance)

   (d) Staff analysis of variable lease payments that meet a high threshold

   (e) Staff analysis of the reassessment and subsequent measurement of variable lease payments that meet a high threshold

   (f) Appendix A: Summary of current guidance in U.S. GAAP and IFRS.

Summary of staff recommendations

4. The staff recommends that the high threshold to be applied to variable lease payments should be "reasonably assured" (which is the equivalent of

"probable" in the United States). That is, variable lease payments should be included in the lessee's liability to make lease payments (lessee's liability) and the lessor's right to receive lease payments (lessor's receivable) only if they are "reasonably assured".

5. Additionally, the staff recommends that variable lease payments should be included in the measurement of the lessee's liability and the lessor's receivable only if those payments can be reasonably estimated.

6. The majority of the staff recommends that the Boards do not require variable lease payments that meet a high threshold to be included in the measurement of the lessee's liability and the lessor's receivable. However, the minority of the staff recommends that the Boards do require variable lease payments that meet a high threshold to be included in the measurement of the lessee's liability and the lessor's receivable

7. The majority of the staff recommends that the measurement of variable lease payments in the lessee's liability and the lessor's receivable should not be reassessed after lease commencement.

8. However, the minority of the staff recommends that variable lease payments that meet a high threshold should be reassessed. That is, lessees and lessors would be required to reassess the carrying amount of the liability to make lease payments and the right to receive lease payments arising from each lease and include variable lease payments in the measurement of the lessee's liability and the lessor's receivable if they are reasonably assured of occurring.

9. If the Boards decide to require reassessment of the measurement of variable lease payments, the staff recommends that changes to the lessee's liability and the lessor's receivable because of changes in estimates of variable lease payments that are reasonably assured should be recognized consistently with the proposals in the *Leases* Exposure Draft (ED). That is, changes in the expected amount of such payments should be reflected in (a) net income to the extent that those changes relate to current or prior periods and (b) as an adjustment to the right-of-use (ROU) asset and the lessor's receivable to the extent that those changes relate to future periods.

Background

10. At the February 2011 joint Board meeting the Boards decided to include an estimate of variable lease payments that meet a high threshold in the measurement of the lessee's liability and the lessor's receivable. However, decisions were not made for what threshold would be required (for example, virtually certain, reasonably certain, probable, etc.).

11. The Boards also requested that the staff perform additional targeted outreach activities to obtain further feedback of the costs and benefits of including lease payments that meet a high threshold in the measurement of the lessee's liability and the lessor's receivable.

Summary of feedback received

12. The staff has performed outreach activities since the Boards discussed variable lease payments at the February 2011 joint Board meeting. Part of that outreach was to determine whether the Boards should apply a threshold to determine whether variable lease payments should be included in the measurement of the lessee's liability and the lessor's receivable. The feedback received from those outreach activities is summarized below.

Practical application of current guidance

13. Based on outreach performed by the staff since the February 2011 joint Board meeting, the staff notes that in practice, at least for public companies in the United States, lessors do not recognize contingent rentals in advance of the contingency being resolved. That is because SAB 104, *Revenue Recognition*, states, in part, that "...contingent rental 'accrues' (i.e. it should be recognized as revenue) when the changes in the factor(s) on which the contingent lease payments is (are) based actually occur."

14. Additionally, although U.S. GAAP states that lessees should recognize contingent rental expense before the achievement of the specified target,

provided the achievement of the specified target is probable,[1] recognition of contingent rental expense before the achievement of the specified target is rare. If contingent rental expense is recognized in interim period financial statements before the achievement of a specified target, it is typically for contingent rental expense that is probable for the current reporting period.

15. For example, in a capital lease arrangement, if a lessee leases a photocopier for three years and pays a base rental plus one cent per copy, in practice under current leases guidance, the lessee would not recognize in year one an estimate of lease expenses for copies expected in years two and three because they often do not consider those probable. The same would be true for retail leases with a contingent lease payment as a percentage of sales (for example, retailers do not currently recognize in year 1 an estimate of lease expenses for sales expected in years 2-10 because they are often not considered probable).

16. Therefore, in practice, companies only assess within the current fiscal year (when the specified target occurs) and do not forecast over the life of the lease arrangement or assess what level of sales/usage are probable over the entire term. However, the concept of including an estimate of disguised minimum lease payments in the measurement of lease assets and liabilities is applied in practice and is discussed in IASB Agenda Reference 1A/FASB Agenda Reference 156.

Feedback received on tentative decisions reached

17. The majority of entities that participated in the targeted outreach performed (which included preparers, users, accounting firms, etc.) did not support including variable lease payments that meet a high threshold in the measurement of the lessee's liability and the lessor's receivable. They suggested either (a) eliminating the requirement or (b) requiring the threshold to be set at a level higher than reasonably assured, such as virtually certain.

18. Accounting firms that participated in the outreach did not see the need to include variable lease payments in the measurement of the lessee's liability and the lessor's receivable if the Boards require entities to include disguised

[1] The staff notes that the term *probable* is applied differently in U.S. GAAP and IFRS.

minimum lease payments. They argue that capturing those payments in the measurement of the lessee's liability and the lessor's receivable may help prevent structuring opportunities.

19. Preparers that participated in the outreach activities stressed the fact that including variable lease payments that meet a high threshold would be as difficult, if not more difficult, to apply than the proposals in the ED. That is because, for example, entities expect to meet some level of sales and the high threshold would be a new concept. In general, including variable lease payments in the measurement of lessee's liabilities and lessor's receivables at any threshold would be costly to apply because preparers would have to determine an estimate of what the variable lease payment would be and then determine whether it is probable.

20. Most users stated that they would be concerned about the reliability of the estimates, especially for long-term lease arrangements and would prefer that information about variable lease payments be provided in disclosures. However, a few users noted that management's estimate would be the most useful information to begin their analysis with.

21. Working group feedback and feedback from private entities was consistent with that of the overall preparer feedback received.

Variable lease payments that meet a high threshold

22. The staff notes that during discussions of variable lease payments that meet a high threshold at the February 2011 joint Board meeting, decisions were not made for what threshold would be required (for example, virtually certain, reasonably certain, probable, etc.), but the Boards expressed support for a "reasonably assured"/"probable" threshold.

23. The staff is presenting the following approaches (from lowest to highest threshold) for defining the threshold to be applied to variable lease payments:

    (a) Lessees and lessors would be required to use a "more likely than not" threshold, consistent with the proposals for revenue recognition

(b) Lessees and lessors would be required to use a "reasonably assured" threshold (equivalent of "probable" in the United States)

(c) Lessees and lessors would be required to use a "virtually certain" threshold

(d) Lessees would be required to use a lower threshold than lessors. For example, lessees would be required to use a "probable" threshold while lessors would be required to use a "reasonably assured" threshold.

24. The "more likely than not" threshold was used in the ED. Concerns were expressed by all constituents in comments letters and outreach about the high cost and difficulties in reliably estimating variable lease payments based on a "more likely than not" threshold. Therefore, the staff does not recommend such a threshold.

25. The staff also does not think the Boards should require a "virtually certain" threshold for lessees or lessors. That is because the staff thinks that variable lease payments that are virtually certain most likely represent disguised minimum lease payments (see IASB Agenda Reference 1A/FASB Agenda Reference 156. If the Boards tentatively decide to define the threshold as "virtually certain" the staff thinks it may be less complex to only include guidance on disguised minimum lease payments, and require the measurement of the lessee's liability and the lessor's receivable to include an estimate of disguised minimum lease payments, to achieve that result.

26. Some staff members argue that the threshold for including variable lease payments in the measurement of lease liabilities and lease assets should be consistent with the proposals for revenue recognition. However, the staff observes that one of the objectives of the leases standard is to best depict the assets and liabilities that arise from a lease contract at each reporting date. The objective of the revenue recognition standard is to depict the amount of consideration the entity expects to receive for the transferred goods and services – that is, predict the amount of consideration that will ultimately be realized from the contract, rather than depict the value of the contract at each reporting date.

27. Uncertain consideration in the revenue recognition standard is discussed in IASB Agenda Reference 2A/FASB Agenda Reference 141A. In that memo, the staff recommends that the threshold for an entity to determine the transaction price is the amount more likely than not to be received unless the entity has a large number of contracts with similar characteristics, in which case the entity would use an expected value technique to determine the transaction price. However, the staff also recommends a “reasonably assured” constraint on the amount of revenue recognized. In effect, this constraint assesses the quality of the estimate of the transaction price.

28. The staff thinks that an appropriate threshold for defining the threshold is “reasonably assured”. The staff has analyzed the advantages and disadvantages of defining the threshold as “reasonably assured” below:

Advantages	Disadvantages
• Would create more comparability between international entities than the use of a threshold such as “probable”, which is applied differently between U.S. GAAP and IFRS preparers. • May be less costly and may result in a more reliable estimate than a “more likely than not” threshold. • If reassessment is required, may result in less frequent reassessment because a “more likely than not” threshold may be more easily attained.	• Creates a fairly high threshold that some would argue may create the understatement of lease assets and lease liabilities.

Staff recommendation

29. The staff recommends that the threshold for defining the threshold to be applied to variable lease payments should be “reasonably assured”. The staff thinks that a “reasonably assured” threshold appropriately addresses the concerns expressed in comment letters and outreach about the cost and reliability of the estimate while ensuring the measurement of the lessee’s

liability and the lessor's receivable reflect payments expected under the lease arrangement.

30. Additionally, the staff recommends that variable lease payments should be included in the measurement of the lessee's liability and the lessor's receivable only if those payments can be reasonably estimated.

31. However, consistent with the staff recommendations in the memo on the accounting for variable lease payments (IASB Agenda Reference 5A/FASB Agenda Reference 129) that was presented to the Boards at the February 2011 joint Board meeting, the majority of the staff recommends that the Boards do not require variable lease payments that meet a high threshold to be included in the measurement of the lessee's liability and the lessor's receivable. That is because those staff members think that the costs of including those payments in the measurement of the lessee's liability and the lessor's receivable (both at initial measurement and, to a greater extent, if reassessment is required) would outweigh the benefits of including those payments in the measurement.

32. However, other staff members recommend that the Boards do require variable lease payments that meet a high threshold to be included in the measurement of the lessee's liability and the lessor's receivable. Those staff members think that the approach appropriately addresses the operationality and reliability concerns expressed by preparers while still providing users of financial statements with useful information to assess amounts, timing, and the uncertainty of cash flows.

Question 1 – High threshold
Question 1 – Do the Boards agree with the staff recommendation that the threshold for including variable lease payments in the measurement of the lessee's liability and the lessor's receivable should be "reasonably assured". If not, which approach do the Boards prefer?

Question 2 – Recognition
Question 2 – The majority of the staff recommends that the Boards do not require variable lease payments that meet a high threshold to be included in the measurement of the lessee's liability and the lessor's receivable. The minority of the staff recommends that the Boards do require variable lease payments that meet a high threshold to be included in the measurement of the lessee's liability and the lessor's receivable. Which approach do the Boards prefer?

Reassessment and subsequent measurement of variable lease payments that meet a high threshold

Summary of proposals in the ED

33. The ED states:

> After the date of commencement of the lease, the lessee/lessor shall reassess the carrying amount of the liability to make lease payments/right to receive lease payments arising from each lease if facts or circumstances indicate that there would be a significant change in the liability/right to receive lease payments since the previous reporting period. (paragraph 17, 39 and 56)

34. When facts or circumstances indicate that there would be a significant change in the lessee's liability due to a reassessment of variable lease payments, the ED states that a lessee should distinguish changes in variable lease payments that relate to current or prior periods from those that relate to future periods as follows:

> A lessee shall recognize changes in the expected amount of such payments:
>
> a. In net income, to the extent that those changes relate to current or prior periods.

> b. As an adjustment to the right-of-use asset to the extent that those changes relate to future periods.
>
> For example, when lease payments depend on the amount of the lessee's sales, changes relating to sales in current or prior periods are recognized in net income, whereas changes relating to expectations of future sales are recognized as an adjustment to the right-of-use asset. (paragraph 18)

35. Similar guidance is proposed for lessors that apply the performance obligation approach except that changes in the lessor's receivable are reflected as an adjustment to the lease liability (performance obligation). Lessors that apply the derecognition approach would be required to reflect changes in the lessor's receivable in the expected amount of the right to receive lease payments in net income.

Feedback received

36. A minority of respondents to the ED (which included preparers, users, industry organizations, etc.) expressed support for the requirement for lessees and lessors to remeasure assets and liabilities arising under a lease when significant changes to those amounts occur based on a reassessment of variable lease payments. Those respondents stated that this would provide users of financial statements with up-to-date management estimates. However, many respondents noted that they would support the reassessment requirements more if the threshold for recognizing variable lease payments were to be increased.

> Given the significant use of estimates and judgement under the proposed leases model, we agree periodic reassessment is necessary to ensure that the statement of financial position accurately reflects the rights and obligations under the lease contract. Revised amounts would provide users of the financial statements with a more accurate assessment of those rights and obligations. However, we believe the model, as proposed, will create significant practical and operational issues for entities and we have concerns that the cost of performing the proposed reassessment may outweigh the benefits. In fact, we believe that using the proposed definition of lease term and lease payments, the reassessment provisions are unworkable. (CL #74)

37. Users, in particular, had mixed views on the proposals for reassessment. Some users agreed that it was necessary to reassess assets and liabilities arising under a lease because of the significant estimates that would be made in the

measurement of those assets and liabilities. However, some users noted that the proposals on reassessment would result in significant operational and practical difficulties. Many users suggested clarifying the term *significant* and requested specific guidance on the facts or circumstances that indicate that there is a significant change.

> As currently written the ED imposes a significant and ongoing burden on both lessees and lessors to capture and reliably document information that could lead to changes in estimating term and lease payments. The remeasurement of the estimate of lease term will lead to volatility in earnings. Additionally, the requirement for remeasurement when there is evidence of significant change leaves too much room for interpretation as it does not include any guidance on how significant is to be interpreted. These requirements seem to be contrary to the stated goal of reducing the complexity of lease accounting. (CL #224)

> We agree with the measurement principle which requires remeasurement of lease payments or the right to receive lease payments based upon significant changes in the aforementioned lease features as we believe this best represents the economics of the transaction. We agree that subsequent re-measurement for items related to current or prior periods should be adjusted through profit and loss and remeasurements related to future periods should adjust the right-of-use asset or performance obligation. We do, however, believe clearer guidance needs to be provided on the facts or circumstances which indicate that there is a significant change in the liability to make lease payments or in the right to receive lease payments and when such indicators exist. If there is not regular periodic updating required we believe that guidance on circumstances which may necessitate a remeasurement are necessary. (CL #780)

38. Many preparers and workshop participants expressed concerns relating to the cost of performing reassessments and questioned whether those costs would be exceeded by the benefits for users of financial statements. Additionally, respondents cited the increased difficulty in complying with the reassessment requirements when faced with interim or quarterly reporting requirements.

> We agree that lessees and lessors should reassess the lease term and contingent rents when facts and circumstances change and should remeasure the lease liability and right to receive lease payments when the lease term and/or contingent rents change. We believe such reassessments will provide users of financial statements with more relevant information. However, we do not agree that lessees and lessors should reassess the lease term and contingent rentals each reporting period. We believe a requirement to reassess each reporting period poses a significant operational burden-on lessees and lessors. Rather than assessments each

> reporting period, we believe lessees and lessors should reassess the lease term and contingent rentals annually. We do not believe the information provided by reassessments each reporting period justifies the costs to obtain that information. We also do not agree that lessees and lessors should remeasure assets and liabilities for changes in estimated residual value guarantees. As discussed previously, we believe lessees and lessors should measure the liability to make lease payments and the right to receive asset, respectively, using the gross amount of the residual value guarantee. (CL #654)

39. Respondents also identified practical application challenges with the proposals relating to:

    (a) allocating reassessment changes between prior, current, and future accounting periods

    (b) proving that no significant change has occurred, with many commenting that preparers are likely to have to perform all of the reassessment steps that would be required to record a reassessment transaction to determine if a significant change has occurred.

    For example:

> We question the cost and benefit of this requirement. A lessor or lessee would have to review the facts and circumstances relating to all lease contracts once a quarter (for public companies) to assess if there were any significant changes. This effort will result in higher personnel and infrastructure operating costs. (CL #175)

> Allocating changes in contingent rentals, term option penalties and residual value guarantees to current or prior periods and future periods is the most onerous provision of the ED for lessees with a large number of leases. (CL #373)

40. Private company feedback was consistent with the overall feedback received on reassessment.

> Continuous reassessment is particularly burdensome. If a quantitative analysis is required to determine whether a significant change has occurred, there is little benefit in changing the accounting only when the quantitative change is significant since the same level of effort would be needed regardless of whether a change is made. It would be preferable if there were a higher initial recognition threshold and more specific triggers, such as for impairment testing. (CL #122)

Reassessment

41. The staff is presenting the following approaches for whether or not lessees and lessors should reassess variable lease payments that meet a high threshold:

    (a) Require reassessment

    (b) Do not require reassessment.

42. The staff thinks that requiring reassessment of variable lease payments that meet a high threshold will provide both timely and better information to users. However, the some staff agrees with the feedback received from constituents that requests clarification for determining when a significant change has occurred because some think that determining whether a significant change has occurred will be practically difficult to apply. That is, an entity will not know a significant change has occurred without going through the reassessment process, which would be costly to preparers.

43. However, some argue that requiring reassessment for variable lease payments that meet a high threshold will be practically difficult and costly to apply and, therefore, the costs would not outweigh the benefits of such reassessment.

44. The staff has analyzed the advantages and disadvantages of requiring reassessment below:

Advantages	Disadvantages
• Provides relevant and timelier information to users of financial statements because it reflects current economic conditions. If reassessment is not required, information may be outdated, irrelevant, or misleading. • Consistent with the requirement to reassess options to extend or renew a	• May be costly to apply for lessees and lessors that have numerous leasing arrangements. • If the reassessment requirement is to reassess when there has been a significant change, determining when a significant change has occurred may be difficult to practically apply.

lease. • More consistent with current requirements for changes in accounting estimates (Topic 250 and IAS 8). That is, current guidance requires reassessment of accounting estimates.	

Staff recommendation

45. The majority of the staff recommends that variable lease payments that meet a high threshold should not be reassessed because they think that the costs of requiring reassessment would outweigh the benefits of reassessment.

46. The minority of the staff recommends that variable lease payments that meet a high threshold should be reassessed. That is, lessees and lessors would be required to reassess the carrying amount of the liability to make lease payments and the right to receive lease payments arising from each lease and include variable lease payments in the measurement of the lessee's liability and the lessor's receivable if they are reasonably assured of occurring. That is because the staff think that this information is more relevant and timelier to users of financial statements because it reflects current economic conditions.

47. Additionally, although many respondents to the ED did not support the proposed reassessment requirements, the staff thinks that the need to reassess would be less burdensome with a threshold as proposed in paragraph 29.

Question 3 – Reassessment of variable lease payments that meet a high threshold
Question 3 – The majority of the staff recommends that variable lease payments that meet a high threshold should not be reassessed. However, the minority of the staff recommends that variable lease payments that meet a high threshold should be reassessed. Which approach do the Boards prefer?

Accounting for the effects of a reassessment of the measurement of variable lease payments

48. The staff is presenting the following approaches for accounting for the effects of a reassessment of the measurement of variable lease payments that meet a high threshold:

    (a) Retain the proposals in the ED as summarized in paragraphs 34-35.

    (b) Require all changes to the lessee's liability and the lessor's receivable to be recognized in net income (IASB: profit or loss).

49. The guidance on the accounting for changes in accounting estimates in Topic 250 (and similarly in IAS 8) is as follows:

    > A change in accounting estimate shall be accounted for in the period of change if the change affects that period only or in the period of change and future periods if the change affects both. A change in accounting estimate shall not be accounted for by restating or retrospectively adjusting amounts reported in financial statements of prior periods or by reporting pro forma amounts for prior periods. (250-10-45-17)

50. Topic 840 (and similarly in IAS 17) states:

    > Contingent rentals. Increases or decreases in rentals that are dependent on future events such as future sales volume, future inflation, future property taxes, and so forth, are contingent rentals that affect the measure of expense or income as accruable, as specified by paragraph 840-10-25-4. (840-20-25-2)
    >
    > This guidance addresses what constitutes minimum lease payments under the minimum-lease-payments criterion in paragraph 840-10-25-1(d) from the perspective of the lessee and the lessor. Lease payments that depend on a factor directly related to the future use of the leased property, such as machine hours of use or sales volume during the lease term, are contingent rentals and,

> accordingly, are excluded from minimum lease payments in their entirety. (840-10-25-4)

51. The staff thinks that variable lease payments that meet a high threshold are often directly related to the underlying leased asset (for example, usage-based variable lease payments). Therefore, recognizing changes to the lessee's liability as an adjustment to the ROU asset and the lessor's receivable (which would reflect a change in the historical cost of the ROU asset) as proposed in the ED may better reflect the economics of the transaction than recognizing changes only through net income/profit and loss.

52. The staff notes that the feedback received identified practical application challenges with the proposals relating to allocating reassessment changes between prior, current and future accounting periods, which is illustrated by the following comment letter response that the staff thinks should be clarified in the final standard.

> Paragraph 18 states, 'A lessee shall distinguish changes in contingent rentals and expected payments under term option penalties and residual value guarantees that relate to current or prior periods from those that relate to future periods.' Paragraph 18 goes on to state that changes related to current or prior periods are recognized in net income, while changes related to future periods are recorded as an adjustment to the right-of-use asset. We believe that the distinction between changes that 'relate to' current or prior periods on the one hand and future periods on the other hand should be clarified, perhaps through an illustrative example(s).
>
> Consider the following example:
>
> A contract provides for contingent rent based on sales. Under the contract, once rent is increased by contingent payments, it can never go down below that increased level. The lessee originally estimates rents as follows: Year 1 CU100; Year 2 CU110; Year 3 CU120; Year 4 CU130; Year 5 CU140. The Exposure Draft appears to require that, if rents increased to CU150 in Year 1 because of an unexpected increase in sales, the difference between CU150 and the CU100 estimate in Year 1 would be recognized currently in net income. However, the Exposure Draft also could be read to require that the upward increase from the originally estimated rents (from the original estimates to the new minimum of CU150) for all remaining years be recognized currently in net income. (CL #364 and CL #692)

53. Although respondents were concerned with the costs of implementing the ED's proposals, some staff members think that many of the cost concerns noted in the feedback received may be mitigated by the higher threshold that was

recommended by respondents. The proposed requirements in the ED are also similar to the current guidance on changes in accounting estimates (see paragraph 49).

54. The staff has summarized the advantages and disadvantages of the approaches below:

	Advantages	Disadvantages
Retain ED	• Reflects the economics of many leases because it recognizes costs and income in periods to which those costs and income relate. • Arguably more consistent with the current guidance in U.S. GAAP and IFRS. • Consistent with the tentative decisions made for the remeasurement of options to extend or renew a lease.	• May create complexity and be difficult to apply.
All changes to net income/profit or loss	• May be easier and less complex to apply than the ED proposals.	• May result in significant changes every period. • Inconsistent with the tentative decisions made for the

		remeasurement of options to extend or renew a lease.

Staff recommendation

55. Based on the advantages and disadvantages listed above, the staff recommends that changes to the lessee's liability and the lessor's receivable because of changes in estimates of variable lease payments that meet a high threshold should be consistent with the proposals in the ED. That is, changes in the expected amount of such payments would be reflected in (a) net income to the extent that those changes relate to current or prior periods and (b) as an adjustment to the ROU asset and the lessor's receivable to the extent that those changes relate to future periods.

Question 4 – Subsequent measurement of variable lease payments that meet a high threshold
Question 4 – Do the Boards agree with the staff recommendation that changes in estimates of variable lease payments that meet a high threshold should be consistent with the proposals in the ED? If not, what approach do the Boards prefer?

Appendix A: Summary of current guidance in U.S. GAAP and IFRS

Lessees

A1. Current leases guidance in Topic 840 (originally EITF Issue 98-9), which applies to a lessee's recognition of all leases, states that:

> A lessee shall recognize contingent rental expense (in annual periods as well as in interim periods) before the achievement of the specified target that triggers the contingent rental expense, provided that achievement of that target is considered probable. (840-10-25-35)

A2. IAS 17 states that contingent rents should be charged as expenses in the periods in which they are incurred.

Capital (finance) leases

A3. The guidance in Topic 840 (and similar guidance in IAS 17) states that, for lessees, the total contingent rentals actually incurred for each period for which an income statement is presented should be disclosed in the lessee's financial statements or footnotes.

A4. Lessees are also required to disclose the basis for which contingent rental payments are determined in their financial statements or the footnotes.

Operating leases

A5. The guidance in Topic 840 (and similar guidance in IAS 17) states that, for all operating leases, rental expense is required to be disclosed in the lessee's financial statements or the footnotes for each period for which an income statement is presented, with separate amounts for minimum rentals, contingent rentals, and sublease rentals.

A6. Lessees are also required to disclose the basis for which contingent rental payments are determined in their financial statements or the footnotes.

Lessors

A7. Current leases guidance in Topic 840 (originally EITF Issue 98-9) states that lessors should defer recognition of contingent rental income until the specified target is met, consistent with SAB 101 on revenue recognition. Additionally, Topic 840 states that:

> The lessor shall disclose its accounting policy for contingent rental income. If a lessor accrues contingent rental income before the lessee's achievement of the specified target (provided achievement of that target is considered probable), disclosure of the impact on rental income shall be made as if the lessor's accounting policy was to defer contingent rental income until the specified target is met. (840-10-50-5)

A8. Similar guidance does not exist in IFRS.

Capital (finance) leases

A9. Current leases guidance in Topic 840 (and similar guidance in IAS 17) states that, for lessors with sales-type leases and direct financing leases, contingent rentals shall be included in the determination of income as accruable. Additionally, lessors are required to disclose information on total contingent rentals included in income for each period for which an income statement is presented in the financial statements or footnotes.

Operating leases

A10. For all operating leases, total contingent rentals included in income for each period for which an income statements is presented is disclosed in the financial statements or footnotes.