IASB/FASB Meeting
Week commencing 18 July 2011

IASB Agenda reference 5D

Staff Paper

IASB/FASB Education Sessions
Week commencing 11 July 2011

FASB Agenda reference 190

Project	**Leases**
Topic	**Lessee Disclosures**

Objective

1. The objective of this paper is to discuss the disclosure requirements for lessees.

2. However, the following disclosure issues that are relevant for lessees will be addressed in separate agenda papers. Those issues include:

   (a) Variable lease payments (discussed in separate paper on lessee statement of cash flows)

   (b) Short-term leases (discussed in separate paper on lessee short term lease disclosure)

   (c) Sub-leases and sale and leasebacks (to be discussed in a separate paper on lessor disclosures at a future meeting).

Background

3. The *Leases* Exposure Draft (ED) would require a number of new disclosures for lessees compared with existing disclosure requirements for lessees. Appendix A provides a table of the requirements in the ED and the corresponding guidance under existing IFRSs and U.S. GAAP. The staff has highlighted requirements that would either be new or significantly modified when compared to current IFRSs and U.S. GAAP. The staff also has isolated the requirements that pertain to lessees separately from the requirements for lessors.

4. Many comment letters included concerns about the disclosure requirements proposed in the ED. In many of the comment letters, concerns were expressed about the volume of required disclosures, and the costs associated with providing such information. Respondents also encouraged the Boards to emphasize in the final standard that entities exercise materiality and judgment in determining what disclosures to make and the amount of information they should provide.

5. In addition to issues raised in the comment letters, the staff also has considered changes to the disclosures based on the tentative decisions made by the Boards in redeliberations that have changed the recognition and measurement of leases by lessees.

6. This paper will address the following issues regarding the disclosure requirements of the ED:

   (a) Reconciliation of beginning and ending balances (ED paragraph 77)

   (b) Maturity analysis (ED paragraph 85)

   (c) Details of leases (ED paragraph 73)

   (d) Additional disclosures (and presentation) issues based on the Boards' decisions about recognition and measurement

   (e) Combining amortization and interest expense related to leases

   (f) Other issues

   (g) Nonpublic entities (FASB)

Summary of staff recommendations

7. The staff recommends the following:

   (a) Retain the proposals in the ED for lessees:

      (i) to present a maturity analysis of the liability to make lease payments

      (ii) to disclose in that maturity analysis the undiscounted cash flows for each of the following five years and a total of the amounts for remaining years

      (iii) to not disclose information about discount rates used to calculate the liability to make lease payments.

   (b) Retain the disclosure required in paragraphs 73(a)(ii) – 73(a)(iii) of the ED relating to information about the nature of leases but remove the requirements to disclose (i) the existence and principal terms of any options for the lessee to purchase the underlying asset and (ii) initial direct costs incurred on a lease.

   (c) Require presentation or disclosure of amounts for lease interest expense and lease interest paid but retain the proposal in the ED to separately present amortization and interest expense.

   (d) Not to provide guidance in the leases standard on disclosures of arrangements that no longer contain a lease.

8. The staff was split on recommendations relating to the following:

   (a) The reconciliation of beginning and ending balances by rolling forward the liability to make lease payments and right of use asset between reporting periods.

   (b) Including commitments related to leases not yet commenced in the maturity analysis.

Reconciliation of beginning and ending balances (roll forward)

9. Paragraph 77 of the ED requires a lessee to disclose:

> a reconciliation of opening and closing balances of right-of-use assets and liabilities to make lease payments, disaggregated by class of underlying asset. The reconciliation shall show separately the total cash lease payments paid during the period.

Feedback

10. The reconciliation of beginning and ending balances (roll forward) of right-of-use (ROU) assets and liabilities to make lease payments, each by underlying type of asset, were the focus of many comment letter responses.

11. Roll forwards are part of existing IFRSs and U.S. GAAP and part of the proposed revenue recognition and insurance contracts projects' disclosure requirements. Roll forwards were reviewed as part of the cross cutting disclosure work (March 1-2, 2011, joint meeting;- FASB Memo 1/ IASB Agenda Paper 8), and it was determined that because of the differences in each of the projects, the utility of each roll forward needs to be evaluated in the context of each project separately. If roll forwards are part of the final leases standard, the cross cutting work indicated that the guidance for the roll forwards should be written consistently with the guidance in the revenue recognition and insurance contracts projects.

12. Users were strongly in favor of the disclosure of roll forwards. Preparers were critical of the requirements.

13. Respondents who were not in favor of the requirements in paragraph 77 of the ED had two main criticisms.

    (a) Some respondents questioned the incremental utility of a roll forward if the user is provided with the components of that roll forward in other proposed presentation and disclosure requirements.

    (b) Some preparers questioned the disaggregation of the roll forwards, in particular, the liability to make lease payments by class of underlying asset.

Incremental utility

14. Respondents noted that any additional disclosure requirements, and roll forwards in particular, involve additional costs to compile and additional time to review and audit.

15. Respondents argued that there is little additional benefit to be derived from the roll forward of the liability because users receive information about the cash flows associated with leases in the statement of cash flows (SCF) and about future cash flows in the schedule of maturities required in paragraph 85 of the ED.

16. Respondents stated that the other information presented and disclosed explains the future commitments of the entity and gives insight into the entity's risk profile and liquidity.

Disaggregation

17. Some preparer respondents stated that they would understand the usefulness of roll forwards of right-of-use assets disaggregated by underlying assets but not the liability to make lease payments.

18. Those respondents argued that if the liability to make lease payments is rolled forward, it should be done to the liability to make lease payments as a whole. The respondents stated that whether the entity is leasing equipment or real estate, the important information is about the entity's commitment to future payments. Disaggregating the roll forward of the liability to make lease payments does not add to the usefulness of that information.

Staff Analysis

19. The staff thinks the usefulness of the disclosure has less to do with the structure of the disclosure but, rather, that the disclosure provides information that is:

    (a) Important to the users of the financial statements

    (b) Not available elsewhere in the financial statements or the notes.

20. Although roll forwards often contain useful information about the changes in asset and liability balances and provide insight to the cash flows of an entity, in the case of the lessee, that information is mainly provided elsewhere (either in the financial statements or in the notes to the financial statements).

21. Cash flows for payments of the liability to make lease payments would be presented separately within the SCF. Furthermore, the maturity disclosure provides information about contractual future cash flows of the entity (see paragraphs 29-49 of this memo).

22. Additionally, there are no other requirements in IFRSs or U.S. GAAP to roll forward financing liabilities such as long term debt.

23. The staff notes that IAS 16 requires the roll forward of property plant and equipment (PP&E) by underlying asset type. The staff thinks the roll forward of the ROU asset disaggregated by underlying asset type would be consistent with this existing guidance. There is no similar disclosure requirement in U.S. GAAP.

24. However, during the joint Capital Markets Advisory Council/Global Preparers Forum meeting on June 22 in London, some participants were more supportive of carrying forward from the ED the proposal to roll forward the liability to make lease payments than the roll forward of the ROU asset. Those participants noted the importance of the cash flows associated with the lease, and that those cash flows are made evident in the analysis of the liability, not the asset. Those participants also stated that it is useful to have all of the information in one roll forward table because of difficulties they have with compiling a roll forward themselves from numbers that are presented and disclosed in different places throughout the financial statements.

25. Other user participants supported the proposals in the ED for disclosure of both a ROU asset and a liability to make lease payments roll forward. Those users thought that information such as impairments, revaluations and ROU assets added through business combinations can be important pieces of information in understanding expense patterns versus cash flows.

Staff recommendation

26. The staff is split on which reconciliations to retain.

27. However, the staff agreed, that if the Boards decide to retain the requirement to roll forward the liability to make lease payments the Boards should not require disaggregation of that roll forward by underlying asset type. That is because a commitment to pay a lease liability does not differ because of the underlying asset type.

28. Furthermore, for any roll forward requirement retained, the staff would align the format to be consistent with the guidance included in the revenue recognition and insurance contracts projects. That is, the disclosure requirements would include the types of line items an entity would use when disclosing the reconciliation of beginning and ending balances as well as the requirement to include any other information that would be useful in understanding the change in the balances.

Question 1

Do the Boards want to retain the requirement in the ED to reconcile the beginning and ending balances of:

i) ROU assets by underlying asset type?

ii) the liability to make lease payments (without the requirement to disaggregate the reconciliation by underlying asset type)?

Maturity analysis

29. Paragraph 85 of the ED requires a lessee to disclose:

> a maturity analysis of the liabilities to make lease payments showing the undiscounted cash flows on an annual basis for the first five years and a total of the amounts for the remaining years. The maturity analysis shall distinguish the minimum obligations specified in the lease (ie excluding contingent rentals and expected payments under term option penalties and residual value guarantees) and the amounts recognised in the statement of financial position.

30. Respondents commented on three issues relating to these proposals:

(a) Which amounts should be included in the maturity analysis?

(b) Which time bands should be used in the maturity analysis?

(c) Should the discounts rates used to measure the liability to make lease payments be disclosed?

Amounts included in the maturity analysis

Feedback

31. Respondents generally did not dispute the usefulness of the maturity disclosure for contractual amounts related to liabilities to make lease payments. Users strongly favored the disclosure of maturity analyses.

32. Some respondents were not in favor of disclosing maturities of non-fixed amounts and amounts related to renewal options. Others were confused by what amounts were supposed to be disclosed in addition to the fixed undiscounted cash flows related to the contractual obligation from the lease. This is because the ED required that these amounts be included in the liability to make lease payments and therefore be part of the maturity analysis.

33. Some think that distinguishing amounts between fixed and variable future cash flows would be costly.

34. Additional feedback from users indicates that historical information about variable lease payments would provide information for their analysis of future cash flows.

Staff Analysis

35. The Boards have decided to limit the inputs that are included in the initial measurement of the ROU asset and the liability to make lease payments compared to what was included in the ED. The staff observed that many of the amounts that respondents expressed concerns over as part of the maturity analysis are no longer part of the determination of the liability to make lease payments as a result of the Boards' redeliberations on the accounting for variable lease payment and term options.

36. The staff thinks the disclosure of undiscounted future cash flows that relate to the amounts included in the determination of the liability to make lease payments would be available to the preparer because those amounts would be necessary to determine the amounts recorded.

37. To be consistent with the Boards' decisions about variable lease payments and term options, the future cash flows related to those amounts that were not included in the determination of the ROU asset and the liability to make lease payments should be excluded from the maturity analysis.

38. Additionally, some staff members think that including leases that have not yet commenced in the maturity disclosure would be useful because those liabilities, although not included in the financial statements until lease commencement, are a contractual obligation of the entity. Those amounts should be disclosed separately from the amounts related to leases that have commenced.

39. However, some constituents think that leases not yet commenced are executory contracts until the lease commences and therefore should not be disclosed as a future lease commitment.

40. Other staff prefer to not expand the maturities analysis and to retain the disclosure requirement from paragraph 73(b) in the ED, which requires disclosure of the following:

> …information about the principal terms of any lease that has not yet commenced if the lease creates significant rights and obligations for the entity.

41. With the inclusion of quantitative information about leases not yet commenced in the maturities analysis, the staff does not think there is a need for the requirement in paragraph 73(b) of the ED.

Staff Recommendation

42. Therefore, the staff recommends that the final standard require the disclosure of a maturity analysis of undiscounted amounts to be paid that are included in the liability to make lease payments.

43. Some staff members also would require separate disclosure of a maturity analysis of undiscounted contractually obligated fixed amounts related to leases that have not yet commenced. Other staff members would retain the disclosures from the ED regarding leases not yet commenced rather than including those amounts in the maturity analysis.

Time bands

Feedback

44. The ED requires a maturity analysis of liabilities to make lease payments showing undiscounted cash flows on an annual basis for the first five years and a total of the amounts for remaining years.

45. The staff noted some questions from constituents about whether the time bands prescribed by the ED should be so prescriptive. Some respondents thought the requirement should provide the flexibility in IFRS 7 for a maturity analysis. However, many of the respondents indicated that disclosing a minimum of each year's cash flows for five years and the amount after five years was appropriate.

46. One user group thought the maturity analysis should extend out based on the significance of the expected term of the lease.

Staff recommendation

47. Because most respondents supported the proposal in the ED and thought that a five year requirement would facilitate comparability, the staff recommends retaining the proposal in the ED for the time bands included within the maturity analysis of liabilities to make lease payments.

Discount rate

Feedback

48. Some respondents suggested that the final standard require the disclosure of the weighted average discount rate used to calculate the liability to make lease payments or the disclosure of a range of discount rates used.

Staff recommendation

49. The staff thinks that the provision of undiscounted amounts in the maturity analysis would allow a user to either derive the weighted-average discount rate or provide an undiscounted basis to which users could apply alternate discount rates. The staff also thinks it could be complex for preparers with multiple lease arrangements to calculate a weighted-average discount rate. Therefore, the staff does not recommend disclosures of discount rates used to calculate the liability to make lease payments.

Question 2
Do the Boards agree with the staff recommendation that the final standard should: i) include a requirement to disclose a maturity analysis of undiscounted amounts to be paid that are included in the liability to make lease payments? ii) retain the time bands for the maturity analysis of liabilities to make lease payments proposed in the ED (that is annually, for the first five years and the total of the amounts for the remaining years)? iii) consistent with the ED, not require disclosures of discount rates used to calculate the liability to make lease payments? Do the Boards think that the final standard should include the requirement to disclose separately in the maturity analysis undiscounted contractually obligated fixed amounts related to leases that have not yet commenced?

Additional information about the nature of leases

50. Many comment letters expressed concern about the requirement to disclose information about the nature of leases. In particular, comment letters focused on paragraph 73 of the ED which states the following:

> An entity shall disclose:
>
> (a) the nature of its lease arrangements, including:
>
> (i) a general description of those lease arrangements.
> (ii) the basis and terms on which contingent rentals are determined.

(iii) the existence and terms of options, including for renewal and termination. A lessee shall provide narrative disclosure about the options that were recognized as part of the right-of-use asset and those that were not.

(iv) the existence and principal terms of any options for the lessee to purchase the underlying asset.

(v) information about assumptions and judgements relating to amortization methods and changes to those assumptions and judgements.

(vi) the existence and terms of residual value guarantees.

(vii) initial direct costs incurred during the reporting period and included in the measurement of the right-of-use asset or right to receive lease payments.

(viii) the restrictions imposed by lease arrangements, such as those relating to dividends, additional debt and further leasing.

(b) information about the principal terms of any lease that has not yet commenced if the lease creates significant rights and obligations for the entity.

51. The staff has analyzed the comments received on paragraph 73 of the ED holistically as well as some of the individual requirements in which there was specific feedback the staff thinks should be considered. Below is a summary of the issues considered by the staff:

(a) Paragraph 73 of the ED taken as a whole (paragraphs 52-59 of this memo)

(b) Renewal, termination and variable lease payments (paragraphs 60-66 of this memo)

(c) Options to purchase the underlying asset and initial direct costs (paragraphs 67-74 of this memo)

Paragraph 73 of the ED taken as a whole

Feedback

52. Although some of the disclosures are currently required as part of current IFRSs and U.S. GAAP (see appendix A), respondents still objected to disclosing information about the terms of the agreements for renewals, terminations, purchases, and variable lease payments.

53. One respondent stated the following:

> …some of the detailed narrative disclosure requirements set out in the ED, for example paragraph 73, will be quite difficult to satisfy in a meaningful way for an entity with numerous (10,000+) leases. The difficulty will be striking a balance between developing concise disclosures that are meaningful, versus voluminous detailed disclosures. (CL#681)

54. A user stated the following:

> If these terms are required in the footnotes, additional guidance is needed to indicate how the terms can be summarized for an entire portfolio since the descriptions of specific renewal options and contingent rental requirements by lease are certainly not expected. (CL#224)

55. One user group stated that the information provided to comply with these requirements “will result in general, qualitative, highly aggregated and boilerplate disclosures which will not be especially meaningful and decision-useful to investors”. (CL #780)

Staff Analysis

56. The disclosure requirements in paragraph 73 of the ED are largely consistent with the disclosure requirements in current IFRSs and U.S. GAAP. However, many respondents thought the disclosure requirements of the ED would be quarterly disclosures. Furthermore, respondents thought that an improvement in lease accounting should result in less information about leases being needed in the disclosures.

57. The staff sees merit in the comments about the difficulty of making the ED’s disclosures for entities with a large volume of leases. The terms of many significantly different agreements would be costly to accumulate and disclose, and the aggregation of leases that have dissimilar terms could render the disclosure less useful.

58. Although there was user support to include information about the terms of renewal and termination options and terms of variable lease payments, there was a limited understanding by preparers about how that information would be used.

59. Additionally, preparers raised a number of the concerns about the costs of compiling the information even though a number of the disclosures are currently required. Therefore, the staff does not think that costs would be significantly greater than the costs currently incurred for the disclosures that provide information similar to current disclosures.

Renewal, termination and variable lease payments

Feedback

60. Some users were concerned that disclosures about the terms of renewal and termination options and variable lease payments on an aggregated basis would become boiler plate and would not provide the information they would find most useful.

61. One user stated that quantitative information about the terms of renewal and termination options and variable lease payments would allow users to compute the change in liabilities to make lease payments under different plausible scenarios. The current disclosures do not specifically require quantitative information.

62. Another user from targeted outreach wants more disclosures about renewals and variable lease payments.

Staff analysis and recommendation

63. The staff sees merit in the concerns expressed by preparers and users about disclosing the terms of leases especially when the entity has many leases that have very different terms.

64. The staff also thinks additional information about the terms of leases becomes more important because of the Boards' tentative decisions during redeliberations regarding the recognition and measurement of variable lease payments and term options.

65. Furthermore, the staff sees those disclosures as consistent with current disclosure requirements. However, the staff thinks additional guidance that demonstrates the aggregation of various terms of different contracts or illustration of the disclosure requirements would be helpful to preparers.

66. The staff therefore recommends that the disclosures required in paragraphs 73(a)(ii) – 73(a)(iii) of the ED be retained. Furthermore, the staff recommends that implementation guidance should be developed and/or illustrations of the proposed disclosures should be provided.

Options to purchase the underlying asset and initial direct costs

Feedback

67. A respondent noted the following:

> …paragraph 73 (iv) requires disclosure of the existence and principal terms of any options for a lessee to purchase the underlying asset.
>
> We do not see the need to provide extensive disclosure of events that could happen based on the entity exercising an option to buy an asset; an entity always has the option to buy assets. (CL#298)

68. Paragraph 73(a)(vii) of the ED requires the disclosure of initial direct costs incurred during the reporting period and included in the measurement of the right-of-use asset.

69. Some respondents have noted that this disclosure would often not rise to a material level and thus should not be explicitly required. Respondents also stated that the amount of initial direct costs would be small compared to the expense of the total lease and to the entity's total expenses. Although preparers state the initial direct costs would be immaterial, when subject to audit, the burden of proof lies with the preparer and therefore, in many instances, a preparer may be compelled to incur the costs to compile the information to demonstrate that the amount is not material enough to disclose.

70. Furthermore, users did not express strong support for this particular disclosure although they did see benefits to retaining disclosures relating to purchase options and initial direct costs because of the following:

    (a) If the amounts are immaterial they would not have to be disclosed.

    (b) The information could be useful.

    (c) Those disclosures are similar to existing guidance.

71. Some preparers commented that the disclosure would offer little to no benefit to a user of financial statements.

Staff analysis and recommendation

72. The staff sees merit in the argument that an entity always has the option to buy assets. The staff also sees merit in the argument that initial direct costs

would likely be a minor part of a larger lease expense amount which is a component of an even larger total expense amount of the entity.

73. The staff also did not see strong support for the disclosure of options to purchase leased assets or for the disclosure of initial direct costs.

74. The staff recommends that disclosures relating to purchase options and initial direct costs be removed to be responsive to disclosure overload concerns. The staff thinks this would reduce the disclosure requirements while not impacting the usefulness of the disclosures in a significant way.

Question 3
Do the Boards agree with the staff recommendation to: i) retain the disclosures required in paragraphs 73(a)(ii) – 73(a)(iii) of the ED while providing aggregation guidance and/or illustrations of the proposed disclosures? ii) remove the requirements in the ED to disclose (a) the existence and principal terms of any options for the lessee to purchase the underlying asset and (b) initial direct costs incurred on a lease?

Additional disclosure (and presentation) issues based on the Boards' decisions about recognition and measurement

'Straight-line' lease expense

75. The Boards' tentative decision to require a single lessee model that results in recognition and presentation in the profit and loss of interest expense and amortization expense rather than rent expense has implications for users of financial statements and *cost plus* contractors that may, in part, be addressed through disclosure (and presentation) of amounts in profit and loss.

76. The Boards indicated that additional disclosures should be considered to provide users with information that could be used to determine what amounts an entity would incur if leases were recognized in profit and loss as rent expense on a straight-line or cash basis.

77. Requirements that the staff is recommending in its papers on presentation and disclosure would provide the user of financial statements with the following information:

    (a) Amortization expense of ROU assets by underlying type of asset (if a ROU asset roll forward is to be required)

    (b) Cash paid relating to the:

        (i) liability to make lease payments recognized by a lessee

        (ii) interest component of the liability to make lease payments

        (iii) variable lease payments and short-term lease payments that are excluded from the liability to make lease payments.

78. If the users were to adjust amounts recognized by the lessee in profit or loss to what would be recorded as rent expense under existing operating lease accounting, the user also would need to know lease interest expense and lease interest paid. The adjustment would be done as follows:

Total lease expense recognized in accordance with
the proposed leases standard

-Amortization of ROU assets

-Lease interest expense

+Cash paid for liability to make lease payments

+Cash paid for lease interest

Proxy for rent expense

79. However, users commented that this type of an adjustment has the following limitations:

(a) It adjusts all leases, including those that are classified as a finance/ capital lease under current IFRSs/U.S. GAAP. However, users may only find disclosure of a proxy straight-line rent expense calculation useful for those leases that are currently classified as operating leases.

(b) It does not reflect the straight lining of rent in profit and loss that occurs when lease payment terms are for different amounts in different reporting periods.

No distinction between operating and finance/capital leases

80. With one type of lease, there will be no distinction between what is currently accounted for as an operating lease and what is accounted for as a finance/capital lease.

81. The staff considered drawing a distinction between two types of leases for disclosure purposes. That is, the staff considered recommending separate disclosure of amortization, interest, and cash paid for lease liabilities and ROU assets related to what are currently considered operating leases.

82. The staff thinks that drawing this distinction for disclosure purposes while not requiring the distinction for accounting purposes would be inconsistent and therefore is not recommending it.

83. Though the distinction between operating and capital/financing leases is not provided, the staff thinks the user could make judgments about an industry or entity and decide that a percentage of lease expense should be adjusted or that only amortization of particular ROU asset types should be adjusted.

No straight lining of rent when payment terms are contractually different in different reporting periods

84. Another issue that would complicate the recalculation of rent expense for today's operating leases is that the straight lining of rent occurs when lease payment structures are uneven. Using cash lease payments as a rent expense equivalent would not account for increases and decreases in lease payment structures that are not straight lined.

85. Considering the lack of a distinction between operating and capital/finance leases and the straight-lining of rent expense, a user will not be able to adjust to a precise rent expense as is accounted for in current U.S. GAAP/IFRSs.

User feedback

86. Some users agreed that the adjustments described above could be done and that the limitations noted by the staff such as the inability to split the types of leases and the lack of the straight lining effect on rent expense was tolerable.

87. Another user suggested that all of those adjustments should be provided in a table in the footnotes to arrive at an amount for rent expense. Other users felt that the users were capable of making the adjustment themselves as long as they had the information to do so.

Staff recommendation

88. Although the staff thinks users will not be able to adjust to a precise rent expense amount as is reported currently, the staff still thinks information about cash payments for interest and interest expense will allow the users of the financial statements to make meaningful adjustments to profit and loss. Therefore, the staff recommends that the Boards require interest expense and interest paid related to leases to be presented or disclosed separately.

Combining interest and amortization expense related to leases

89. Concerns have been expressed by comment letter respondents that the presentation of expense related to leases as amortization and interest will cause entities that have cost plus contracts, which provide for reimbursement from governmental organizations or through regulatory rate agreements, to encounter challenges in recovering costs they incur today for rent expense. One comment letter explains:

> The Federal Acquisition Regulations ("FAR") refer to current US GAAP with regard to leases. Under the FAR, the interest component of a capital lease is not an allowable cost. The provisions of the ED will effectively make all leases capital leases, and will result in an interest charge for all leases other than those that are short term. This accounting change will likely have an enormous financial impact on federal contractors even though

> there has been no change in the economics of the leases themselves. …The interest component of the lease payments could be disclosed in the notes to the financial statements... (CL#246)

90. IAS 1 requires a minimum line item for finance costs separate from other costs. Regulation SX Rule 5-03 also lists interest expense as a separate line item that should appear on the face of income statements filed.

91. The staff believes that the presentation of interest and amortization under lease contracts as rent expense within operating activities may address the concern in paragraph 89 of this memo. However, the presentation requirements of IAS 1 and Regulation S-X would indicate interest must be presented separately.

92. The staff also thinks that the rate of reimbursement would be accelerated under those types of contracts when recovery is based on reported lease expense because the total expense would not be recognized on a straight-line basis. That is, there would be more lease expense at the beginning of the lease and less at the end.

93. The staff also thinks that the disclosure of the interest component of lease or rent expense may result in the reimbursing entity scrutinizing the amount presented as rent expense and excluding the portion of rent or lease expense that is disclosed as interest expense in the notes.

94. Furthermore, the staff observes that allowing a single lease or rent expense for particular types of contracts or industries or leaving an open ended option on the presentation of the expense amounts would lead to comparability issues.

95. Therefore, the staff recommends that interest and amortization should be presented separately.

Question 4

Do the Boards agree with the staff recommendation that:

i) the interest expense and interest paid related to leases should be presented separately or disclosed?

ii) consistent with the proposals in the ED, interest and amortization should always be presented separately and not combined and presented as lease expense?

Other issues

96. Currently, IFRIC 4 and Topic 840 address the identification of arrangements that contain a lease. Furthermore, both apply the disclosure requirements of leases to the parts of those arrangements that are deemed to contain a lease.

97. The staff notes that, because of proposed changes to the definition of the lease, fewer arrangements are likely to be determined to contain a lease than under existing IFRSs and U.S. GAAP. As a result, some staff members are concerned about the loss of disclosures (specifically relating to future minimum contractual cash flows) relating to those arrangements that are determined to no longer contain a lease.

98. The staff has identified two approaches to addressing that concern:

    (a) Propose as part of the leases project a consequential amendment to non-leases guidance that requires that the existing disclosure requirements should remain for those arrangements, even though they will no longer be determined to contain a lease.

    (b) Acknowledge that disclosures relating to some arrangements will be reduced because they are no longer determined to contain a lease and instead are accounted for as executory contracts. However, disclosures relating to executory contracts should be addressed as part of a separate project and not as part of the consequential amendments proposed in finalising the leases standard.

99. The staff think that the lease project should not address arrangements that do not contain a lease. Therefore, the staff recommends approach (b).

Question 5
Do the Boards agree with the staff recommendation that disclosures relating to some arrangements that are no longer determined to contain a lease are outside of the scope of the leases standard?

Nonpublic entities (FASB only)

100. The FASB is not being asked to make any decisions about nonpublic entity disclosure exemptions at this time. The staff has considered the feedback received from nonpublic entity constituents and will provide the Board with a further analysis and its final recommendations about disclosure exemptions for nonpublic entities at a subsequent FASB Board meeting, subject to the Boards' decisions reached on the disclosure requirements for all entities.

101. Nonpublic entity constituents provided responses that are similar to those provided by public entity respondents. However, nonpublic respondents questioned whether providing the account roll forwards is necessary because the users of nonpublic entity financial statements have the ability to ask for that information if when needed. Given that the statement of cash flows and other disclosures would provide most of the relevant information required for many nonpublic entity financial statement users to understand significant changes in the ROU asset and the liability to make lease payments, nonpublic entity respondents questioned whether the benefits would justify the costs of preparing and auditing roll forwards. Under U.S. GAAP, nonpublic entities generally are not required to disclose roll forwards because their users often can obtain this information directly from management.

102. The staff is conducting additional targeted outreach with users of nonpublic entity financial statements to evaluate the usefulness of some of the other proposed disclosures. For example, because most users of nonpublic entity financial statements are focused on cash adjustments, the proposed disclosure about the assumptions and judgments relating to amortization methods may not provide relevant information. Given the ability of many users to access management and concerns about disclosure overload, the staff also may propose that nonpublic entities be exempt from providing some of the disclosures about assumptions and judgments required under paragraph 83 of the ED.

Appendix A

The following table details the disclosure requirements of the ED aligned with the corresponding requirements in current IFRSs and U.S. GAAP. Requirements not currently in IFRSs or U.S. GAAP are underlined. A change in current IFRSs or U.S. GAAP is bolded and italicized.

The disclosure objectives were not included in the table as there is no corresponding objective in either IFRSs or U.S. GAAP.

The requirements below only include those required of the lessee.

<u>**Exposure Draft**</u>	<u>**IAS 17**</u>	<u>**Topic 840**</u>
Information that identifies and explains the amounts in the financial statements 73. An entity shall disclose: (a) the nature of its lease arrangements, including:		
73. (i) a general description of those lease arrangements.	(d) A general description of the lessee's significant leasing arrangements including, but not limited to, the following:	10-50-2(a) general description of its leasing arrangements including, but not limited to, all of the following:
73.(ii) the basis <u>and terms</u> on which contingent rentals are determined.	(i) the basis on which contingent rent payable is determined;	10-50-2 (a). The basis on which contingent rental payments are determined
73.(iii) the existence and terms of options, including for renewal and termination. 73.(iv) the existence and principal terms of any options for the lessee to purchase the underlying asset.	(ii) the existence and terms of renewal or purchase options and escalation clauses;	10-50-2(b). The existence and terms of renewal or purchase options and escalation clauses
<u>73.(iii)A lessee shall provide narrative disclosure about the options that were recognized as part of the right-of-use asset and those that were not.</u>		
<u>73.(v) information about assumptions and</u>		See paragraph 460-10-50-4 for required disclosures of

judgements relating to amortization methods and changes to those assumptions and judgements. (vi) the existence and terms of residual value guarantees. (vii) initial direct costs incurred during the reporting period and included in the measurement of the right-of-use asset or right to receive lease payments.		guarantees.
(viii) the restrictions imposed by lease arrangements, such as those relating to dividends, additional debt and further leasing.	(iii) restrictions imposed by lease arrangements, such as those concerning dividends, additional debt and further leasing.	c. Restrictions imposed by lease agreements, such as those concerning dividends, additional debt, and further leasing.
(b) information about the principal terms of any lease that has not yet commenced if the lease creates significant rights and obligations for the entity.		
74. An entity shall identify the nature and amount of significant subleases included in the disclosures provided in accordance with paragraph 73.	35. Lessees shall, in addition to meeting the requirements of IFRS 7, make the following disclosures for operating leases: (b) the total of future minimum sublease payments expected to be received under non-cancellable subleases at the end of the reporting period.	840-30-50-1 c The total of minimum sublease rentals to be received in the future under noncancelable subleases as of the date of the latest balance sheet presented.
	(c) Lease and Sublease payments recognized as an expense in the period, with separate amounts for minimum lease payments, contingent rents, and sublease payments.	
75. An entity that accounts for short-term leases in accordance with paragraphs 64 and 65 shall disclose that fact and, for lessees, the amount recognized in the statement of financial position for such short-term leases. 76. A lessee that enters into a sale and leaseback		

transaction shall disclose that fact, disclose the terms and conditions for that transaction and identify any gains or losses arising from such transactions separately from gains or losses on other disposals of assets.		
77. A lessee shall disclose a reconciliation of opening and closing balances of right-of-use assets and liabilities to make lease payments, disaggregated by class of underlying asset. The reconciliation shall separately show the total cash lease payments paid during the period.		840-30-50-1a. The gross amount of assets recorded under capital leases as of the date of each balance sheet presented by major classes according to nature or function. This information may be combined with the comparable information for owned assets.
Information about the amount, timing and uncertainty of cash flows arising from leases 83. An entity shall disclose information about significant assumptions and judgements and any changes in assumptions and judgements relating to renewal options, contingent rentals, term option penalties, residual value guarantees and the discount rate used when determining the present value of lease payments. 84. (FASB) An entity shall disclose information in accordance with the proposed Accounting Standards Update, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities—Financial Instruments (Topic 825) and Derivatives and Hedging (Topic 815)*. 84. (IASB) Except as described in paragraphs 85 and 86, an entity shall disclose information relating to risks		

arising from a lease required by paragraphs 31–42 of IFRS 7 *Financial Instruments: Disclosures*. …		
85. ***A lessee shall disclose a maturity analysis of the liabilities to make lease payments showing the undiscounted cash flows on an annual basis for the first five years and a total of the amounts for the remaining years. The maturity analysis shall distinguish the minimum obligations specified in the lease (that is, excluding contingent rentals and expected payments under term option penalties and residual value guarantees) and the amounts recognized in the statement of financial position.*** (IASB begins) ***In place of the maturity analyses required by paragraph 39(a) and (b) of IFRS 7…***	35. Lessees shall, in addition to meeting the requirements of IFRS 7, make the following disclosures for operating leases: (a) the total of future minimum lease payments under non-cancellable operating leases for each of the following periods: (i) not later than one year; (ii) later than one year and not later than five years; (iii) later than five years.	840-30-50-1 b. Future minimum lease payments as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding fiscal years, with separate deductions from the total for the amount representing executory costs, including any profit thereon, included in the minimum lease payments and for the amount of the imputed interest necessary to reduce the net minimum lease payments to present value (see paragraphs 840-30-30-1 through 30-4).
		Total contingent rentals actually incurred for each period for which an income statement is presented.
		For all operating leases, the lessee shall disclose rental expense for each period for which an income statement is presented, with separate amounts for minimum rentals, contingent rentals, and sublease rentals. Rental payments under leases with terms of a month or less that were not renewed need not be included. For operating leases having initial or remaining noncancelable lease terms in excess of one year, the lessee shall disclose both of the following: a. Future minimum rental

		payments required as of the date of the latest balance sheet presented, in the aggregate and for each of the five succeeding fiscal years b. The total of minimum rentals to be received in the future under noncancelable subleases as of the date of the latest balance sheet presented.