IASB/FASB Joint Meeting
Week commencing March 14, 2011

FASB ED Session March 9, 2011

IASB Agenda reference **5A**

FASB Agenda reference **140**

Staff Paper

Project **Leases**

Topic **Accounting for short-term leases**

Objective

1. The purpose of this paper is to discuss the accounting for short-term leases. Agenda Paper (AP) 5B/FASB Memo 141 is a supplement to this paper that discusses the presentation and disclosure of short-term leases and includes an appendix of proposed amendments to the ED based on the staff recommendations.

2. This paper is structured as follows:

   (a) Summary of Staff Recommendations

   (b) Summary of Proposals in the ED

   (c) Summary of Feedback

   (d) Staff Analysis and Discussion of Approach

      (i) Accounting for Short-Term Leases

      (ii) Definition of a Short-Term Lease

      (iii) Short-Term Lease Guidance as an Election

      (iv) Pattern of Profit or Loss Recognition

Summary of Staff Recommendations

3. In this paper, the staff recommend the following:

   (a) A lessee and a lessor can elect to account for short-term leases in a manner consistent with current operating lease treatment. However, a minority of staff recommend that the Boards retain the guidance in the ED on short-term leases.

   (b) A short-term lease is defined as the following:

   > A lease that, at the date of commencement of the lease, has a maximum possible term, including any options to renew, of approximately 12 months or less.

   (c) Short-term lease accounting should be applied as an accounting policy election. It would therefore be applied to all, or none, of an entity's short-term leases, rather than on a lease-by-lease basis (as proposed in the ED).

   (d) Lease payments should be recognized on a straight-line basis over the lease term unless another systematic and rational basis is more representative of the time pattern in which use is derived from the underlying asset.

Summary of Proposals in the ED

Definition

4. Appendix A of the ED defines a short-term lease as:

   > A lease that, at the date of commencement of the lease, has a maximum possible lease term, including options to renew or extend, of 12 months or less.

Lessee and Lessor

5. The ED proposes a method of accounting for short-term leases by the lessee that is different than the method proposed for accounting for short-term leases by the lessor.

   (a) Paragraph 64 of the ED proposes the following for the *lessee*:

   > At the date of inception of a lease, a lessee that has a short-term lease may elect on a lease-by-lease basis to measure, both at initial measurement and subsequently, (a) the liability for lease payments at the undiscounted amount of the lease payments and (b) the right-of-use asset at the undiscounted amount of lease payments plus initial direct costs. Such lessees shall recognize lease payments in the income statement over the lease term.

   (b) Paragraph 65 of the ED proposes the following for the *lessor*:

   > At the date of inception of a lease, a lessor that has a short-term lease may elect on a lease-by-lease basis not to recognize assets or liabilities arising from a short-term lease in the statement of financial position, nor derecognize any portion of the underlying asset. Such lessors shall continue to recognize the underlying asset in accordance with other Topics and shall recognize lease payments in the income statement over the lease term.

6. The major difference proposed in the ED for the accounting for short-term leases by the lessor and by the lessee is that the lessor may elect to **not** recognize any asset (i.e., any lease receivable), liability (i.e., any performance obligation), or derecognize any portion of the underlying asset for short-term leases, whereas the lessee must always recognize a right-of-use asset and a liability for lease payments on its statement of financial position (albeit measured at undiscounted amounts).

Summary of Feedback

7. The ED included specific questions regarding the accounting for short-term leases by the lessor and the lessee as follows:

   > **Question 3: Short-term leases**
   >
   > Do you agree that a lessee or a lessor should account for short-term leases in this way? Why or why not? If not, what alternative approach would you propose and why?

General Feedback

8. Many respondents, including auditors, preparers, and industry organizations, were supportive of the Boards' proposal to introduce simplified accounting for short-term leases. Those respondents noted that:

   (a) The costs of the proposals in the ED may outweigh the benefits for a lease with a maximum possible lease term, including options to renew or extend, of 12 months or less and that simplified accounting methods would largely alleviate this cost burden.

   (b) Simplified accounting methods would improve the operationality of the proposals in the ED.

9. Respondents were especially supportive of the option proposed in the ED to avoid recognition of any asset or liability by the lessor for short-term leases.

10. However, the majority of respondents disagreed with the proposed accounting for short-term leases by the lessee, largely because of the argument that the cost relief realized from the simplified accounting would not be significant enough:

> We consider that the so-called concession for lessees of short term leases does not provide this type of solution as the only simplification made is the omission of a present value calculation. The bulk of the burden involved in indentifying the large numbers of small, short term contracts that many companies are likely to have, and applying all of the other requirements of the proposals such as determining the lease term and lease payments, has not been alleviated. We therefore do not agree with the statement in BC 205 that the Boards have simplified the accounting for short term leases from the perspective of lessees. (CL #449)

11. Many respondents suggested that a more effective method of accounting for short-term leases by the lessee would be to allow the same option as available to the lessor in the ED.

> We believe that lessees should have the same options for accounting for short-term leases as those provided to lessors. Lessees should be able to choose on a lease-by-lease basis not to recognize assets or liabilities arising from a short-term lease in the statement of financial position. Instead of the proposed

> option to record undiscounted amounts, lessees should be able to recognize the cost of short-term leases on a straight-line basis consistent with current accounting guidance. This would align lease expense recognition with lease economics. (CL #565)

12. Other respondents suggested that a more effective method of accounting for short-term leases for both the lessor and the lessee would be to define a short-term lease by reference to the useful life of the underlying asset, such as a percentage of the useful life. These respondents suggested this definition approach instead of the proposed definition in the ED.

13. Respondents also observed that because the option provided to lessors is made on a lease-by-lease basis, different accounting could be applied to identical leases. A respondent therefore suggested an alternative approach in response to this issue:

> We also note that the election to apply the simplified model is on a lease-by-lease basis. Therefore, as written, an entity could apply different accounting to identical leases. As the simplified approach is intended only to be a practical exception, and is not based upon a specific concept or theory, we do not object to this election being made on a lease-by-lease basis. However, if the Boards would be opposed to an entity making inconsistent or varying elections regarding their accounting for short-term leases, we suggest refining the standard to instead require a related accounting policy election. (CL #74)

14. Additionally, respondents to the ED requested clarification on the pattern of income/expense recognition in profit or loss, specifically the meaning of, "recognize lease payments in the income statement over the lease term," as used in paragraphs 64 and 65 of the ED. Respondents were unclear if this meant that expense (lessee) or income (lessor) from leases should be recognized:

    (a) On a straight-line basis.

    (b) On a systematic and rational basis.

    (c) As lease payments became payable or receivable.

> We also note that the guidance as drafted in both paragraphs 64 and 65 require Lease payments to be recognised in profit or loss over the lease term, but provide no guidance for the pattern of recognition. ... We suggest that an explicit requirement is added to clarify that the charges/credits arising from short term leases

> should be recognised in profit or loss on a straight line basis over the lease term. (CL #540)

User Feedback

15. Users had mixed views on the proposed simplified accounting for short-term leases. Some users stated their preference for a scope exclusion from the ED proposals, while others stated that no exclusion should be granted.

> Short term leases (leases with a term or 12 months or less) are not common in the commercial rea1 estate industry, with the exception of residential real estate rental properties. We do not agree that short-term leases should be accounted for in the proposal as the administrative burden of accounting for these leases that turnover quite frequently could be significant. (CL#550)

> We stated in our comment letter response to the Lease Discussion Paper that the proposed standard should not provide exclusions for short-term leases and that the financial statements would be most informative and consistent if all material leases were subject to a single model without exception to avoid mixed-attribute accounting measures. We also stated our belief that exempting short-term leases could be an invitation to structuring contracts around the new model and that varied subjective interpretations as to what constitutes ”short-term” could lead to inconsistent treatment. We, therefore, support the Boards' decision to not provide a blanket exclusion for short-term leases. (CL #748)

16. Users echoed the issues observed in general comment letter feedback, including concern over the lessor assessing its option for short-term leases on a lease-by-lease basis.

> We would prefer to see an accounting policy choice for asset categories rather than a lease-by-lease assessment as this is a pragmatic approach that will not compromise transparency or understandability. (CL #709)

Nonpublic Entity Feedback

17. Private company and not-for-profit respondents supported the application of simplified accounting for short-term leases and the Boards' acknowledgement that such provisions could lessen the cost burden associated with the proposals in the ED. However, many of these respondents acknowledged that the provisions, especially the accounting for short-term leases by the lessee, did not do enough to balance the costs of the proposals with the benefits of the information that would be provided.

> The exclusion of such leases from the scope of the standard would not, in our opinion, significantly impair the information offered to users of the financial statements, although it would lessen the administrative workload arising from applying the standard for the lessees. (CL #183)

Staff Analysis and Discussion of Approaches

Accounting for short-term leases

18. The staff is presenting the following three approaches to account for short-term leases:

    (a) **Approach A:** retain the simplified accounting for short-term leases as proposed in the ED.

    (b) **Approach B:** confirm the proposals in the ED for lessors but also permit lessees to account for short-term leases in a manner consistent with the present requirements for operating leases (that is, make the accounting for short-term leases by the lessee symmetrical to the accounting for short-term leases by the lessor as proposed in the ED).

    (c) **Approach C:** eliminate the exception for short-term leases.

Approach A*: retain the proposals in the ED*

19. Under Approach A, the proposed guidance in the ED for the accounting for short-term leases would be retained. That is, the lessor would continue to have the

option to **not** recognize an asset (that is, a lease receivable), a liability (that is, performance obligation), or derecognize any portion of the underlying asset for short-term leases (collectively the lessor's lease assets and liabilities). However, the lessee would be required to recognize a right-of-use asset and a liability to make lease payments (collectively the lessee's lease assets and liabilities) on its statement of financial position, measured at undiscounted amounts.

20. Supporters of Approach A acknowledge that there is no conceptual basis behind providing different accounting for a short-term lease, but recognize the costs imposed by the proposals in the ED and think that the short-term lease concept can serve as a practical expedient.

21. For the lessor, the short-term nature of these leases may make the recognition of lease assets and liabilities for the lessor insignificant to the statement of financial position of the lessor.

22. For the lessee, respondents noted that, because the definition of a short-term lease relates to a term of 12 months or less, any discounting effect of the lessee's lease assets and liabilities is unlikely to be material. Respondents also point to Accounting Standards Codification paragraph 835-30-15-3a (formerly APB 21, paragraph 3a), which does not require the interest method to be applied to "receivables and payables arising from transactions with customers or suppliers in the normal course of business that are due in customary trade terms not exceeding approximately one year." Similarly, paragraph 45 of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* only requires discounting to be applied when the effect of the time value of money is material. These respondents agree with the Boards' decisions in the ED that, due to the short-term (that is, current) nature of these transactions, discounting should not be required.

23. Those that do not support Approach A reject this approach because:

    (a) The simplified accounting does not provide lessees enough relief of the costs imposed by the proposed guidance;

(b) The accounting for short-term leases by the lessee is not aligned with the accounting for short-term leases by the lessor; or

(c) There should not be an exception provided for short-term leases for either the lessor or the lessee.

***Approach B**: align accounting for short-term leases for both lessees and lessors by allowing the lessee a similar option to lessors, as proposed in the ED*

24. Under Approach B, the proposed guidance in the ED for the accounting for short-term leases by *lessors* would be retained and the requirements for *lessees* would be amended to be consistent with the lessor requirements. That is, both the lessor and the lessee would be able to account for short-term leases in a manner consistent with the current requirements for operating leases.

25. Supporters of Approach B acknowledge that there is no conceptual basis behind differential accounting for a short-term lease, but recognize the costs imposed by the proposals in the ED, and think that the short-term lease concept can serve as a practical expedient. However, they think that the simplified accounting as proposed in the ED (and Approach A) does not go far enough to address the significant cost concerns identified by preparers. They do not think that the most significant costs and complexities of applying the proposed guidance derive from the discounting, but rather from getting the information that is necessary to apply the proposed guidance. Therefore, these supporters question whether the proposals for lease accounting for short-term leases provided any real relief to preparers and any real benefit to users of financial statements, especially as the effects of discounting would likely be immaterial.

26. Those that do not support Approach B note that there is no conceptual basis for excluding short-term leases from the scope of the proposed guidance. The Boards expanded on similar arguments against a scope exclusion for short-term leases in paragraph BC43 of the Basis for Conclusions of the ED:

> Short-term leases could give rise to material assets and liabilities. If an entity did not account for the assets and liabilities arising from short-term leases, the assets and liabilities in the statement of financial position would be incomplete and would not be a faithful representation of those short-term leases. Furthermore, a scope exemption for short-term leases would introduce an artificial distinction between leases that are recognized and those that are not. Therefore, this exposure draft proposes that short-term leases are within the scope of the proposed guidance.

27. In addition, those not supporting Approach B think that it would not provide decision-useful information to users about potential future cash outflows in the next 12 months. Those not supporting Approach B also think that the combination of materiality considerations and capitalization thresholds in current practice would be sufficient to relieve short-term leases from the proposed guidance and its cost burden if the lease obligations were not material to the entity.

Approach C*: eliminate the exception for short-term leases*

28. Under Approach C, the concept of a short-term lease would be eliminated and all leases, including short-term leases, would be accounted for under the proposed leases guidance, subject to normal materiality thresholds. Leases would not be distinguished by the length of their terms, nor would the length of the term dictate the accounting.

29. Supporters of Approach C:

    (a) Place greater weight on the fact that there is no conceptual basis behind the idea of a short-term lease and think that the benefits of accounting for short-term leases under the proposed guidance outweigh the costs of doing so.

(b) Think that introducing the concept of a short-term lease creates another distinction between leases that, based on the Boards' tentative decisions in February 2011 joint meetings to continue with a two-model approach for accounting by the lessee, would otherwise generally be accounted for under the same model as other-than-financing leases. This may introduce new complexities and costs into the proposed guidance to track and make such a distinction.

(c) Think that the combination of materiality considerations and capitalization thresholds in current practice should be sufficient to ensure that many short-term leases would not need to be accounted for under the proposed guidance, thus minimizing the costs of the proposed guidance.

(d) Consider that specific guidance for accounting for short-term leases would not be required if the Boards appropriately distinguish a lease from a service, reduce some of the complexity proposed in the ED (for example, relating to the accounting for variable lease payments) and provide appropriate guidance for separating the lease and non-lease components of an arrangement.

30. Those that do not support Approach C think that the costs of accounting for short-term leases under the proposed guidance outweigh the benefits of doing so. They think that further relief of the costs of accounting for such transactions should be provided, although they note that the appropriate application of materiality by entities and simplifications made by the Boards during redeliberations on the project should reduce preparer costs.

Staff Recommendation

31. The staff acknowledges respondents' feedback to increase the amount of relief provided to lessees from accounting for short-term leases. This feedback has been presented in paragraphs 10 and 11 above and echoed by auditor respondents, including CL #367:

> While we support short-term lease relief for lessors, we note that the assets and liabilities that arise from short-term leases may be significant in aggregate for an entity that enters into many short-term leases in the normal course of its business. We believe the Boards should provide lessees with the same relief for short-term leases as is proposed for lessors (i.e. the ability to elect not to apply the proposed standard to short-term leases).

32. The staff has also heard similar feedback from private companies, as evidenced in paragraph 17 of this memo and in CL #686:

> On the basis of cost-benefit considerations, the PCFRC recommends that arrangements in which the most likely term, including renewal clauses, is twelve months or less should not be required to be capitalized. The pure volume of short-term arrangements can increase costs significantly if private companies are required to account for each short-term arrangement under the proposed ASU.

33. The majority of the staff thinks that the costs of recognizing lease assets and liabilities for short-term leases by both lessees and lessors outweigh the benefits of doing so and that relief of the cost burdens imposed by accounting for short-term leases under the proposed guidance should be provided. The majority of the staff recommends Approach B – that is, lessees and lessors can elect to account for short-term leases in a manner consistent with current operating lease treatment.

34. Other staff members recommend Approach A**.** Those staff members think that Approach A provides decision-useful information to users about potential future cash outflows in the next 12 months. Those staff members also think that the combination of materiality considerations and capitalization thresholds in current practice would be sufficient to relieve short-term leases from the proposed guidance and its cost burden if the lease obligations were not material to the entity.

Question 1 – Accounting for short-term leases
Which approach do the Boards support for accounting for short-term leases?

Definition of a Short-Term Lease

35. Should the Boards choose either Approach A or Approach B above, the staff thinks that the Boards must decide upon the definition of a short-term lease. This determination should be made in light of the proposed definition of *lease term* that the Boards tentatively decided in the February 2011 joint meeting. The Boards have tentatively decided at the February 2011 meeting that the definition of lease term is as follows:

> The **lease term** is the non-cancellable period for which the lessee has contracted with the lessor to lease the underlying asset, together with any options to extend or terminate the lease when there is a significant economic incentive for an entity to exercise an option to extend the lease, or for an entity not to exercise an option to terminate the lease.

36. The ED defined a short-term lease as:

> A **lease** that, at the **date of commencement of the lease**, has a maximum possible **lease term**, including options to renew or extend, of 12 months or less.

37. The ED short-term lease definition was consistent with the ED definition of lease term as “the longest possible term that is more likely than not to occur.” Using the definition of lease term in paragraph 35, the staff thinks that this definition should be revised.

38. The staff presents the following two revised definitions of short-term lease for the Boards to consider:

(a) **Definition A:** different from the definition of lease term in paragraph 35 and aligned with the definition in the ED as, "A **lease** that, at the **date of commencement of the lease**, has a maximum possible ~~lease term~~ term, including any options to renew ~~or extend~~, of approximately 12 months or less".

(b) **Definition B:** aligned with the definition of lease term in paragraph 35 and adjusted from the definition in the ED as, "A **lease** that, at the **date of commencement of the lease**, has a ~~maximum possible~~ **lease term** ~~including options to renew or extend~~ of 12 months or less."

39. The staff acknowledges that an alternative to Definition A and Definition B is to define a short-term lease in reference to or as a percentage of the useful life of the underlying asset. However, the staff disagrees with this approach and rejects it as a possible definition because it would:

(a) Create inconsistency for lease arrangements within entities, within industries, and across industries. For example, if a percentage threshold of 10 percent were used, a three-year lease of office space with a useful life of 35 years may meet the definition of a short-term lease, but a four-year lease by the same entity of identical office space would not meet the definition of a short-term lease.

(b) Allow application of simplified accounting for leases of underlying assets with long useful lives and material lease terms, but restrict application for leases of underlying assets with short useful lives and immaterial lease terms. For example, if a percentage threshold of 10 percent was used, a lease of corporate office space for 3 years may meet the definition of a short-term lease (assuming the building's useful life is 35 years), but a 6 month lease of a photocopier with a 3 year useful life would not meet the definition of a short-term lease.

40. The staff presents the following example to be used in the analysis of Definition A and Definition B

> A lease contract with a non-cancellable lease term of 364 days and includes 1-year renewal options at market rates for the next 9 years.

41. Under Definition A, the definition of short-term lease is **not** linked to the definition of lease term as defined in paragraph 35. Therefore, no assessment of "significant economic incentives" is required to determine which options to renew should be considered in identifying a short-term lease. The term of the lease under Definition A includes *any* option to renew, resulting in a much narrower scope to which the accounting for short-term leases may be applied.

    (a) The lease in the example in paragraph 40 would **not** be accounted for as a short-term lease because the maximum possible term for this example is 10 years.

    (b) The staff notes that, although the lease in this example would not be a short-term lease under Definition A, the lease term under the model and as defined in paragraph 35 would be only 364 days because there is no economic incentive (that is, renewal is at market rates) to exercise the option.

    (c) Additionally, under Definition A, initial and any subsequent assessment of a lease as short-term would yield the same conclusions.

42. Under Definition B, the definition of short-term lease is linked to the definition of lease term as defined in paragraph 35; an option to renew would be included in the lease term only if there are "significant economic incentives" to exercise the option. Therefore, the lease term for short-term leases is assessed the same as any lease term would be under the proposed guidance. This results in a broader scope to the accounting for short-term leases.

    (a) The lease in the example in paragraph 40 would be accounted for as a short-term lease under Definition B if it were determined that there are no significant economic incentives to exercise. The lease term for this example would be 364 days and meets the definition of a short-term lease under Definition B.

Staff Recommendation

43. The staff recommends Definition A, to **not** link the definition of short-term lease to the definition of lease term in paragraph 35 and remain consistent with the ED. The staff recommends the definition of short-term lease as follows (marked for changes to the ED):

> A **lease** that, at the **date of commencement of the lease**, has a maximum possible ~~lease~~ term, including <u>any</u> options to renew ~~or extend~~, of <u>approximately</u> 12 months or less.

44. The staff acknowledges that, as noted in paragraph 40, this may result in a narrower application of the maximum possible term when identifying short-term leases than the definition of a lease term applied when accounting for a lease that does not meet the short-term definition. However, the staff is not opposed to the treatment that results from the example; more lease assets and liabilities are recognized on the statement of financial position.

45. In contrast, the staff thinks that the broader Definition B provides significant structuring opportunities to avoid capitalizing lease assets and liabilities under the proposed guidance. Leases such as the one in the example in paragraph 40 could very easily be structured for contracts that would otherwise include 5-, 10-, or 20-year lease terms so that the lease may fall under short-term lease accounting (and the capitalization of lease assets and liabilities may be avoided for the entire of the lease term). Whereas under the main model, reassessment of the lease term would have to be considered for such leases if circumstances change that a significant economic incentive to renew exists.

46. Also, the staff thinks that Definition A follows the cost/benefit considerations for accounting for short-term leases. The approach to considering options to renew for a short-term lease in Definition A may be simpler and less costly than in

Definition B – if there is an option to renew (with or without an evaluation of economic incentives), it is included it in the maximum possible term.

Question 2 – Confirmation of the definition of short-term lease
Do the Boards agree with the staff recommendation to **not** link the definition of short-term lease to the definition of lease term and to amend the definition of a short-term lease to, "A **lease** that, at the **date of commencement of the lease**, has a maximum possible term, including any options to renew, of approximately 12 months or less"? Why or why not?

Short-Term Lease Guidance as an Election

47. Should the Boards choose either Approach A or Approach B in Question 1 above, the Boards must decide how an entity should apply the election to use simplified accounting for short-term leases. The staff have identified the following alternatives for how the election for short-term lease accounting could be made:

(a) **Approach D:** on a lease-by-lease basis (that is, retain the proposals in the ED)

(b) **Approach E:** as an accounting policy election (that is, the choice to apply short-term lease accounting would be made on an entity-wide basis as an accounting policy election)

(c) **Approach F:** not as an election, but as a requirement that the short-term lease guidance is applicable to all entities, at all times, for all short-term leases.

48. Supporters of Approach D think that the election should be made on a lease-by-lease basis because the nature of a short-term lease should be assessed based on the individual circumstances unique to that lease. Consequently, the election to follow the short-term lease guidance should be made based on the nature of that short-term lease.

49. Supporters of Approach E think that short-term lease transactions that are the same or similar in nature should be accounted for by an entity in a similar manner.

To ensure this, an entity should make an accounting policy election whether to follow the guidance provided for short-term leases for all short-term leases.

50. Those that support Approach E also note concerns that Approach D might provide structuring opportunities. An auditor respondent noted that because the proposed guidance would allow election on a lease-by-lease basis (that is, Approach D), it would be possible to apply different accounting to identical leases. Therefore, Approach D may provide a means to avoid representational faithfulness on the statement of financial position and profit or loss. The staff notes that the Boards do not wish to make decisions based strictly on abuse prevention. However, the staff thinks that the arguments made in this paragraph may be used to strengthen the arguments in paragraph 49 and the support for Approach E.

51. Supporters of Approach F think that the guidance for short-term leases should be applied if the definition of a short-term lease is met; that is, an entity should not be able to elect to apply short-term accounting either as an accounting policy choice or on a lease-by-lease basis. They think that this would enhance comparability across, and not just within, entities. They may also support Approach F to avoid opening structuring opportunities, similar to the arguments discussed in paragraph 50.

52. Those that do not support Approach F think that such a requirement unnecessarily restricts those entities that may want to account for short-term leases consistently with all other leases (that is, entities that may not want to use short-term lease accounting). They think that the proposed guidance to accounting for leases is superior to the accounting for short-term leases and, therefore, it is inappropriate to prevent entities from applying this accounting.

Staff Recommendation

53. The staff acknowledges comment letter respondents' concerns that considering an election, on a lease-by-lease basis, to use the short-term lease guidance could afford, or at minimum not address, the opportunities for structuring and abuse described in paragraph 50. Thus, the staff does not recommend Approach D.

54. The staff recommends Approach E, that the election to apply short-term lease guidance be made as an accounting policy election. The staff thinks that Approach E would improve the simplified accounting for short-term leases as compared to Approach D; the application of accounting methods from period to period would be more consistent on an entity's statement of financial position and the income statement; and the relative decision usefulness of short-term lease information would be increased, as echoed by a user in CL #709 (cited in paragraph 16 above) and a preparer industry organization in CL #716:

> Providing an election for the "simplified" approach on a lease-by-lease basis to either lessees or lessors does not appear to be the best way to achieve comparability or a reduction in complexity. If the Board wishes, however, to continue with this proposal, it could, in our view, enhance clarity and comparability if it were to offer this as an accounting policy election for all such leases rather than on a lease-by-lease basis.

55. The staff thinks that Approach E appropriately allows entities to account for short-term leases under superior guidance (that is, the proposed guidance to accounting for leases), should they elect. This is unlike Approach F. However, the staff acknowledges in its recommendation that comparability across entities may be greater under Approach F than Approach E.

56. The staff notes that should the Boards accept the majority staff recommendation of Approach B in Question 1, then its recommendation of Approach E would be applicable to accounting by both the lessor and the lessee. That is, the election to follow the guidance for short-term leases would be an accounting policy choice for both the lessor and the lessee and would apply to all of an entity's lease arrangements.

Question 3 – Accounting for short-term leases on a lease-by-lease basis
The staff recommends Approach E, that the election to apply the guidance for short-term leases be made as an accounting policy choice. Do the Boards agree with the staff recommendation? Why or why not?

Pattern of Profit or Loss Recognition

57. Should the Boards choose either Approach A or Approach B in Question 1 to account for short-term leases, the staff thinks it is necessary to clarify the proposals as written in the last sentences of both paragraphs 64 and 65 of the ED:

> Such lessees/lessors shall recognize lease payments in the income statement over the lease term.

58. As presented in paragraph 14 and in CL #364 below, the staff received feedback requesting clarification on the interpretation of this sentence and its effects on the pattern of profit or loss recognition for short-term leases.

> We also recommend that the Boards clarify whether recognising lease payments in the income statement "over the lease term" (for both lessees and lessors) requires recognising expense or income on a straight-line basis or another systematic and rational basis, or whether rentals may be recognised as expense or recognised as income over the lease term as it becomes payable/receivable.

59. The staff presents the following alternatives to addressing this issue:

    (a) **Approach G:** retain the proposals as written in paragraphs 64 and 65 of the ED:

> Such lessees/lessors shall recognize lease payments in the income statement over the lease term.

(b) **Approach H:** clarify paragraphs 64 and 65 by adopting the guidance for the pattern of profit or loss recognition currently used for operating leases in Topic 840 and IAS 17:

> Lease payments shall be recognized as profit or loss on a straight-line basis over the lease term unless another systematic and rational basis is more representative of the time pattern in which use is derived from the underlying asset.

Staff Recommendation

60. The staff acknowledges the concerns raised by constituents in response to the ED relating to the lack of clarity provided in the ED as to the appropriate method to "recognize lease payments in the income statement over the lease term".

61. Thus, the staff recommends Approach H, to clarify paragraphs 64 and 65 by adopting the guidance for the pattern of profit or loss recognition currently used for operating leases in Topic 840 and IAS 17. The staff thinks that Approach H will satisfactorily address constituents' concerns over the pattern of profit or loss recognition and clarify the Boards' intent to allow straight-line or another, more representative systematic basis of recognition into profit or loss.

Question 4 – Pattern of profit or loss recognition
The staff recommends Approach G, to clarify paragraphs 64 and 65 to explicitly reflect the pattern of profit or loss recognition currently used for operating leases in Topic 840 and IAS 17. Do the Boards agree with the staff recommendation? Why or why not?