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Project **Leases**

Topic **Lessee Transition**

Objective

1. The purpose of this paper is to discuss the general transition requirements and general transition disclosures for lessees upon adoption of the proposed leases requirements. There are some specific transition issues that will need to be addressed for certain transactions which will be discussed in a separate memo. For example, this paper does not discuss transition requirements for sale and leaseback transactions, discount rate, etc.

2. The background section of this memo summarizes feedback received on the project about effective dates and transition and it has been considered in the staff analysis of transition. The effective date of the proposed leases guidance will be discussed at a future board meeting.

3. This paper is organized as follows:

   (a) Summary of staff recommendations

   (b) Background

   (c) Summary of feedback received

   (d) Staff analysis of transition requirements

   (e) Staff analysis of transition requirements for current capital/finance leases

This paper has been prepared by the technical staff of the IFRS Foundation and the FASB for discussion at a public meeting of the FASB or the IASB.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the FASB or the IASB.

Comments made in relation to the application of U.S. GAAP or IFRSs do not purport to be acceptable or unacceptable application of U.S. GAAP or IFRSs.

The tentative decisions made by the FASB or the IASB at public meetings are reported in FASB *Action Alert* or in IASB *Update*. Official pronouncements of the FASB or the IASB are published only after each board has completed its full due process, including appropriate public consultation and formal voting procedures.

(f) Staff analysis of transition disclosures

(g) Drafting discussion

(h) Appendix A— Disclosure requirements of Topic 250 and IAS 8.

4. Throughout this paper, the term *effective date* refers to the beginning of the period (which may be an interim period) in which an entity first applies the new standard. The *date of initial application* refers to the beginning of the first comparative year in the financial statements. For example, the effective date may be 1/1/2015, however, the date of initial application may be 1/1/2013, assuming that there is three years of profit and loss presented.

Summary of staff recommendations

5. Some staff members recommend that lessees should apply a full retrospective approach for transition of the new lease requirements. However, some staff members recommend a modified retrospective approach.

6. To ease the burden of applying the proposed standard in the first year of application, the staff recommends that the following reliefs should be provided:

   (a) Do not require restatement of contracts that finished before the effective date.

   (b) Do not require evaluation of initial direct costs for contracts that began before the effective date.

   (c) Allow the use of hindsight when preparing comparative information.

7. The staff also recommends that the transition requirement in paragraph 92 of the *Leases* Exposure Draft (ED) be extended to all leases currently classified as capital/finance leases. That is, for all leases currently classified as capital/finance leases, the carrying amount at the date of initial application of the right-of-use (ROU) asset and the liability to make lease payments (lease liability) should be the carrying amount of the lease asset and lease liability upon transition.

8. Lastly, the staff recommends that the Boards require transition disclosures consistent with IAS 8 and Topic 850. If an entity elects any of the available reliefs in paragraph 6 of this memo, the entity should disclose which reliefs have been elected.

Background

Summary of proposals in the ED

9. The ED proposes that an entity should recognize and measure all outstanding contracts within the scope of the standard as of the date of initial application using a simplified retrospective approach. Furthermore, the ED describes the date of initial application as the beginning of the first comparative period presented in the first financial statements in which the entity applied the guidance.

10. The simplified retrospective approach was described in the ED as follows:

> 90. Unless paragraphs 91-93 apply, at the date of initial application, a lessee shall:
>
> (a) recognize a liability to make lease payments for each outstanding lease, measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate on the date of initial application.
>
> (b) recognize a right-of-use asset for each outstanding lease, measured at the amount of the related liability to make lease payments, subject to any adjustments required to reflect impairment.
>
> 91. When lease payments are uneven over the lease term, a lessee shall adjust the right-of-use asset recognized at the date of initial application by the amount of any recognized prepaid or accrued lease payments.
>
> 92. For leases that were classified in accordance with Topic 840/IAS 17 as capital/finance leases and do not have options, contingent rentals, term option penalties or residual value guarantees, the carrying amount at the date of initial application of the right-of-use asset and the liability to make lease payments shall be the carrying amount of the lease asset and liability under that guidance.

Interaction with other projects

Revenue recognition

11. The staff notes that in the revenue recognition project, the Boards have tentatively decided to affirm their decision in the Exposure Draft on revenue recognition that an entity should apply the proposed standard on a retrospective basis. However, to ease the burden of applying that proposed standard in the first year of application, the Boards tentatively decided to provide reliefs, detailed in paragraph 43 of this memo.

12. Additionally, an entity should apply any relief elected consistently to all transactions throughout the comparative periods.

13. The Boards also tentatively decided in the revenue recognition project that if an entity elects any of the available reliefs above, the entity should disclose the following information:

    (a) The reliefs that have been elected by the entity

    (b) To the extent reasonably possible, a qualitative assessment of the likely effect of applying those reliefs.

Effective dates and transition

14. Although the project on effective dates and transition focuses on effective dates and transition from a holistic perspective rather than focusing on individual projects, the staff notes the following observations from that project:

    (a) Most users prefer retrospective application and would rather the Boards defer the effective date to achieve that result. They also cited comparability issues associated with the prospective and modified retrospective approaches, and did not favor allowing companies to choose their transition method.

    (b) Many preparers favored prospective application (applying the new standard only to new contracts entered into after the effective date) of all standards because they don't think that the benefits of retrospective application justify the costs. They think that retrospective application will be very cumbersome and time consuming and that any

comparability benefit that a financial statement user may gain from this information will be overshadowed by the cost and time that will be required to prepare that information.

(c) Comment letter respondents preferred that the Boards have common transition methods for all standards. However, respondents were split as to whether all standards should have the same effective dates.

15. Regarding the leases project, in particular, many respondents stated that a full retrospective application should be permitted because it represents a more faithful comparative presentation of the economics than the proposed simplified transition method. Those respondents indicated that preparers want the option of being able to decide whether the cost of the full retrospective approach supports the benefit of mitigating the issues related to the income statement distortion that results from the pattern of expense recognition currently in the proposal. However, those respondents acknowledged that the simplified transition approach is necessary for entities that do not have the ability to retrospectively adjust their financial statements.

16. Other respondents questioned the benefits of retrospective transition in the leasing project because of the time and cost associated with preparing the following:

(a) Comparative statements, which require evaluation of leases that may have expired before the effective date.

(b) Recasting financial results, which will be affected by hindsight in estimates of expected terms of leases, values of underlying assets, ability to release or sell leased assets, and expectations used in evaluating variable lease payments.

Private company consideration

17. In the project on effective dates and transition, some comment letter respondents offered an alternative transition approach for private companies. Those respondents think that private entities should be given the option to apply the proposed standards on either a prospective or a retrospective basis. That approach would provide private companies with the flexibility to select the

transition method that is most appropriate for their circumstances. Additionally, supporters of that approach think that in some instances, retrospective application may have little benefit to users of private entity financial statements. Therefore, those proponents think that private companies should have the option to adopt the standards prospectively to limit the time and cost burdens that can be associated with retrospective transition.

Summary of feedback received on the *Leases* ED

18. Almost all respondents supported the proposal not to require entities to apply a fully retrospective approach on transition because of the cost and complexity for some preparers. However, many respondents identified concerns with the profit or loss 'front-loading' effect of the proposed simplified retrospective transition approach proposed in the ED.

> We believe that using a simplified retrospective approach (as defined within the ED) is reasonable as it results in comparable financial information about leases at a lower cost than requiring a full retrospective application of lease accounting. The costs of a full retrospective approach could be excessive for certain entities, and we believe that the benefits provided by the information obtained would not outweigh the costs. However, we do note that the simplified retrospective approach could result in an entity recognising a disproportionately high amount of lease expense/income in the periods immediately following the date of initial application as this approach has the effect of recognising all outstanding leases as if they commenced on the date of initial application. [CL #74]

19. Only a few user respondents commented on lessee transition. Of those respondents, concerns were raised about the usefulness of information that would be provided under the simplified retrospective transition approach and, specifically, identifying certain comparability concerns:

    (a) Between entities, if entities are permitted, but not required, to apply a fully retrospective transition approach. This may allow entities to chose a transition approach that provides them with a favored financial reporting outcome

(b) Between new and existing leases within an entity because the pre-transition period of existing leases is not considered in their post-transition accounting.

> Full retrospective application would be an excessive requirement for most entities and allowing it as an option would only contribute to decreased comparability across companies. [CL #224]

Suggested approaches

20. The majority of other respondents (excluding users) supported permitting but not requiring entities to fully retrospectively apply the guidance, specifically as a way of overcoming the profit or loss 'front-loading' effect of the proposed simplified retrospective transition approach. Additionally, respondents noted that additional guidance would be needed for the extent of hindsight that should be applied on transition.

> We believe that the full retrospective approach should be permitted (but not required) because it is more representationally faithful and may be easier for some entities, particularly lessors, to apply. In addition, many lessees will desire the option of a retrospective approach as it will avoid "resetting" the front loaded expense impact of the right-of-use model. While we support the simplified retrospective approach as it provides some cost-benefit relief from full retrospective application, we strongly believe that full retrospective application should be provided as an option. [CL #364]

21. Other suggested approaches and relief for transition included:

(a) Grandfathering provisions for existing finance leases or for identifying whether a contract meets the definition of a lease (consistent with those included in current U.S. GAAP)

(b) Requiring fully retrospective transition, noting an expectation that users will be requesting the retrospective information regardless of whether or not it is included in the financial statements and that this may be simpler to prepare if the measurement proposals in the ED are simplified in the final standard

(c) Another simplified retrospective transition approach;

(d) Providing an exception for leases with a remaining term of 12 months or less at the effective date

(e) Allowing prospective application.

22. Respondents also identified situations, such as the following, where additional transition guidance is required:

    (a) Contracts considered as purchases, sales, or leases in accordance with previous U.S. GAAP and IFRSs, but not in accordance with the new guidance

    (b) Sale and leaseback transactions that meet the current criteria in IFRSs/U.S. GAAP but will not meet the criteria in the new guidance and deferred gains on arrangements that continue to be considered as sale and leaseback transactions

    (c) Build-to-suit leases

    (d) Treatment of prepaid and accrued amounts.

23. Due to the most recent tentative decisions regarding ‘in-substance purchase/sales’, the staff does not think that additional transitional guidance is necessary for the concern noted in paragraph 22(a) of this memo. The other items noted above are specifically addressed in separate memos.

Staff analysis of transition requirements

24. The staff has considered the following approaches for the general transition requirements:

    (a) Approach A: Full retrospective approach

    (b) Approach B: Modified retrospective approach

    (c) Approach C: Optional full retrospective approach, otherwise Approach B.

25. The staff has rejected the approach proposed in the ED for the transition requirements for lessees because of the “front-loading” of expenses and the feedback received from constituents.

26. Additionally, the staff has rejected a prospective approach (applying the standard only to leases entered into after the effective date) for the transition

requirements for lessees. That is because, although that approach would be less costly and easier to apply, any information provided would not be beneficial to users and would be inconsistent with the Boards' tentative decisions on revenue recognition.

Approach A: Full retrospective

27. Approach A would require entities to transition using a full retrospective approach consistent with the requirements in Topic 250 and IAS 8.[1] That is, entities would be required to calculate the carrying amounts of all outstanding leases as if those leases had always been accounted for in accordance with the proposed requirements.
28. The staff thinks that Approach A would provide the best comparative information and is the best starting point from which to apply the new requirements. However, it may be the most time consuming and burdensome for preparers. Nonetheless, the staff thinks that this concern could be reduced by allowing appropriate time between the final standard and the effective date.
29. The staff notes that some constituents (mostly preparers) think that the benefits of the information provided in Approach A would not outweigh the costs. Therefore, similar to the Boards' tentative decisions in the revenue recognition project, the staff thinks it would be possible to reduce the costs of transitioning by providing some relief (for example, not requiring restatement of arrangements that have ended prior to the effective date). Providing some reliefs would create consistent transition requirements between the leases project and the revenue recognition project. Possible relief options are analyzed further in paragraphs 43-44 of this memo.

[1] Topic 250 and IAS 8 provide guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. When it is impracticable to determine, the guidance requires that the new accounting principle be applied to the balances of assets and liabilities as of the beginning of the earliest period for which retrospective application is practicable and that a corresponding adjustment should be made to the opening balance of retained earnings for that period rather than being reported in an income statement. When it is impracticable to determine the cumulative effect of applying a change in accounting principle to all prior periods, the guidance requires that the new accounting principle be applied as if it were adopted prospectively from the earliest date practicable.

30. Some argue that applying a retrospective approach may be difficult when there are estimates and judgments involved. However, the staff thinks that it is important to note that, during redeliberations, the Boards have simplified the recognition and measurement requirements (for example, variable lease payments and lease term). Those simplifications should reduce the amount of judgment and costs associated with applying the new requirements retrospectively. That concern also can be mitigated by providing a relief similar to the relief tentatively decided for revenue recognition to allow the use of hindsight in estimating certain assumptions and judgments such as lease term and variable consideration.

Approach B: Modified retrospective approach

31. Approach B is a modified retrospective approach that allows preparers to approximate a full retrospective method without performing all of the costly calculations from the beginning of the lease term. This approach uses key inputs at the date of initial application to approximate the transition impact and calculates a ROU asset that approximates that ROU asset in a full retrospective approach. As a result of the modified retrospective approach, a cumulative catch-up adjustment would be recognized at the date of initial application in the amount of the difference between the recorded asset and liability.

32. Approach B calculates the lessee's liability in a manner consistent with the ED proposals to reflect the lessee's remaining liability to make lease payments at the date of initial application. However, the ROU asset is calculated in a modified manner. The asset calculation uses the same information as required in the liability calculation (discount rate, lease term, and lease payments) to approximate the ROU asset at the date of initial application on the proportion of the lease term remaining but does not require an entity to go back as if the standard had always been applied.

33. For example, if transitioning in the fourth year of a ten-year lease, with yearly payments of 1,000CU and a discount rate of 5.7%, the lessee would calculate the liability at the beginning of the lease term as 7,472CU. The lessee would then take the proportion of the term remaining (6 of the 10 years) to calculate the ROU asset at 4,483CU as described below.

Revised modified transition approach

This calculation derives the transition ROU asset (or an approximation thereof) that would be produced from full retrospective application but it only uses 4 pieces of data - the first three inputs are needed to calculate the transition liability (discount rate, term, lease payments) and the fourth input is the calculated liability itself. The transition liability is calculated the same as it would be under the simplified retrospective approach in the ED.

Proportion of term remaining = 6 / 10

a. Calculated liability at transition = 4,967
b. Discount rate = 5.7%
c. Amount of payment necessary to pay down calculated liability to zero = 1,000

Total liability at beginning of lease term, as derived only from inputs (a., b. and c.) above = 7,472

ROU Asset = 60% x 7,472 = 4,483

In this example, the calculation results in an identical ROU asset as calculated under the full retrospective transition because: (1) the lease payments are constant throughout the lease term and (2) the transition incremental borrowing rate is set equal to the rate implicit in the lease at inception. If one or both of these is assumptions is not true then the transition asset will be an approximation only.

The modified retrospective transition approach would serve to reduce the increase in expense (from lessee's perspective) in the periods immediately following transition as compared to the simplified retrospective approach in the ED.

34. The staff notes that if the lease payments are even over the lease term, the ROU asset recognized under Approach B may be similar to the asset recognized under Approach A, although the difference in discount rate may cause the results to differ. However, when the lease payments are not even over the lease term, the ROU asset is established as a proportion of the lease liability calculated for the remaining years of the lease term.

35. The staff notes that this approach may minimize the “front-loading” of expenses that result from the proposals in the ED and may be easier to apply than Approach A. Particularly in cases in which the original lease term is long (for example, leases greater than 25 years) or when an entity acquires a lease in a business combination when information on the original lease may be difficult to locate, the staff thinks that Approach B (modified retrospective approach) is preferable. However, Approach B may be difficult to calculate when there are rent escalators or other changes in payments during the lease term or the discount rate used at the date of commencement of the lease differs from the rate used at transition. The staff also thinks that Approach B may involve significant judgment in estimating the value of the ROU asset, which may lead to incomparability between entities.

Approach C: Optional full retrospective; otherwise, Approach B

36. Approach C allows preparers an option to choose either the modified retrospective approach or a full retrospective approach. This approach would be an election that would need to be applied consistently to all lease arrangements, rather than an option to just apply to some lease arrangements.

37. Although Approach C may provide relief for preparers, Approach C may create incomparability between entities that choose to apply a full retrospective approach and entities that choose to apply a modified retrospective approach. Feedback from users suggests that they are opposed to allowing a choice for transition because of comparability concerns.

38. Additionally, the staff notes that the impracticability guidance in Topic 250 and IAS 8 and thinks that any lack of information about old leases or leases acquired in a business combination would be covered by such a provision.

Staff recommendation

39. All staff members agree that a full retrospective approach gives users of financial statements the best and most comparative information.

40. Some staff members recommend that lessees should apply a full retrospective approach for transition of the new lease requirements (Approach A). Those staff members acknowledge the cost concerns of preparers but do not think that any form of a modified retrospective approach would be any less costly than a full retrospective approach. In addition, those staff members note the simplifications to the recognition and measurement requirements when compared to the proposals in the ED, which should reduce the burden of applying a full retrospective approach. Those staff members supporting a full retrospective approach also think that this approach would be consistent with the tentative decisions made in revenue recognition and that it is important to create consistency between projects (as noted in the feedback received in the project on effective dates and transition). Finally, those staff members also noted comments made by some respondents in which they expect users to request retrospective information regardless of whether it is included in the financial statements.

41. However, other staff members recommend a modified retrospective approach (Approach B). Those staff members think that a modified retrospective approach would be less costly than a full retrospective approach and would still provide users of financial statements with useful information. Additionally, those staff members point to differences between the shorter term nature of revenue contracts as compared to lease contracts as a distinction that should be considered in the transition method. While those staff members acknowledge the impracticability guidance in Topic 250 and IAS 8, the additional effort and cost associated with proving the impracticability of certain contracts may require almost as much effort as applying a full retrospective approach.

42. All staff members recommend that, for whichever approach the Boards decide is appropriate, transition reliefs should be granted, similar to those in the revenue recognition project. Those reliefs are discussed below in paragraphs 43-44 of this memo.

Question 1 – Transition requirements
Question 1 – Which transition approach do the Boards prefer?

Transition Reliefs

43. In the revenue recognition project, the Boards have tentatively decided to provide entities with the following reliefs:

    (a) An entity should not be required to restate contracts that begin and end within the same annual reporting period.

    (b) An entity should be permitted to use hindsight in estimating variable consideration in the comparative reporting periods.

    (c) An entity should be required to perform the onerous test only at the effective date unless an onerous contract liability was recognized previously in a comparative period.

    (d) An entity should not be required to disclose the maturity analyses of remaining performance for prior periods.

44. The staff thinks that, to ease the burden in the first year of transition, the Boards also should provide reliefs in the leases project. Possible reliefs are discussed below. Reliefs that are italicized are reliefs allowed by the Boards in the revenue recognition project.

	Relief	Comments	Recommendation
1	Do not require restatement of contracts that finished before the effective date.	This relief would avoid an entity having to restate contracts that ended in the comparative periods. Only contracts that are active at the effective date would require restatement. The staff notes that this relief would ease the burden of transition. Although this relief may affect the comparability in comparative periods, the staff thinks it is more important to ensure comparability in periods after the effective date (which would not be affected by this relief). The staff thinks that the reduction in costs for preparers outweighs the benefit of having this comparative information.	Approach A – Yes Approach B – Yes
2	Do not require restatement of contracts	This relief would avoid an entity having to restate	Approach A – No Approach B – No

	that finished within some time period (for example, 12 months) after the effective date.	contracts that ended within some time period (for example, 12 months) after the effective date. The staff thinks that this relief may be useful if the period between publication of the final standard and the effective date is short. However, assuming there is sufficient time between publication and effective date, the staff does not think this relief would provide any additional benefit to preparers and would just extend the possible lack of comparability for some time after the effective date.	
3	Do not require evaluation of initial direct costs for contracts that began before the effective date.	This relief would avoid an entity having to evaluate initial direct costs of existing contracts under the guidance of the new standard. This may ease the burden of transition on the first year without significantly affecting comparability between reporting periods. This relief also prevents	Approach A – Yes Approach B – Yes

		previously expensed items from being capitalized upon transition.	
4	Do not require entities to retrieve discount rates for contracts that have been in effect over XX years.	This possible relief will be discussed in the memo on the discount rate for transition.	N/A
5	*Allow the use of hindsight in estimating the following:* • *Variable lease payments* • *Purchase options and renewal options* • *Residual value guarantees* • *Impairment* • *Revaluation (IFRS only)* • *Bifurcation of nonlease components* • *Contract modifications.*	Any retrospective application of the standard would require an entity to determine the estimates it would have made at each reporting date in the comparative periods. If the Boards allow a long period between the issuance of the standard and the effective date, this may not be impracticable; however, it increases complexity and costs of retrospective restatement. The Boards could reduce that complexity by allowing an entity to restate a contract with the benefit of hindsight. For instance, on a contract, if an entity knows that it ultimately exercised an option to extend a lease term but did not expect to do so in a	Approach A – Yes Approach B – Yes

		comparative period, it could reflect that information throughout the comparative periods. The use of hindsight also would be applicable to variable lease payments, residual value guarantees, impairment, revaluation, and the bifurcation of nonlease components.	
6	*Do not require disclosure for prior periods of the maturity analysis of remaining liabilities to make lease payments.*	This relief would avoid an entity having to prepare disclosures at the end of comparative reporting periods. However, the staff notes that because the maturity analysis only discloses undiscounted future cash flows as of the reporting date, there are no prior period amounts to be disclosed. Therefore, this relief is not necessary.	Approach A – No Approach B – No

Summary of staff recommendations

45. To ease the burden of applying the proposed standard in the first year of application, the staff recommends that the following reliefs should be provided:

    (a) Do not require restatement of contracts that finished before the effective date.

(b) Do not require evaluation of initial direct costs for contracts that began before the effective date.

(c) Allow the use of hindsight when preparing comparative information.

46. An entity would be able to select any, all, or none of the above reliefs.

Question 2 – Transition reliefs
Question 2 – Do the Boards agree with the staff recommendation in paragraph 45 of this memo? If not, then which relief options, if any, do the Boards wish to provide?

Staff analysis of transition requirements for current capital/finance leases

47. The staff notes that some constituents questioned the transition requirement in paragraph 92 of the ED that states:

> For leases that were classified in accordance with Topic 840/IAS 17 as capital/finance leases and do not have options, contingent rentals, term option penalties or residual value guarantees, the carrying amount at the date of initial application of the right-of-use asset and the liability to make lease payments shall be the carrying amount of the lease asset and liability under that guidance.

48. Those constituents questioned whether this requirement could be extended to all leases currently classified as capital/finance leases (for example, those including variable lease payments, options to extend or terminate, etc.) because the current accounting model is very similar to the proposed requirements, especially with the changes made to the recognition and measurement of variable lease payments and options to extend or terminate a lease. Therefore, requiring entities to restate these lease contracts may be burdensome without providing substantially better information to users.

49. However, some staff members are concerned that the liability recorded under current guidance may not be comparable to the liability to make lease payments that will be recorded under the proposed requirements. For example, the concept of economic incentive in determining the lease term is not included in current guidance, therefore, the lease term will not be estimated in the same way.

Staff recommendation

50. The staff recommends that the transition requirement in paragraph 92 of the ED be extended to all leases currently classified as capital/finance leases. The staff notes that changes that have been made to the recognition and measurement of lease assets and liabilities during redeliberations will result in accounting by the lessee that is very similar to current capital/finance lease accounting (for example, the treatment of options). Therefore, the staff thinks that the transition relief should be extended to all capital/finance leases because the additional cost of analyzing such lease contracts on transition would outweigh any possible benefits. Therefore, the staff recommends the following changes to paragraph 92 of the ED:

> For leases that were classified in accordance with Topic 840/IAS 17 as capital/finance leases ~~and do not have options, contingent rentals, term option penalties or residual value guarantees~~, the carrying amount at the date of initial application of the right-of-use asset and the liability to make lease payments shall be the carrying amount of the lease asset and liability under that guidance.

Question 3 – Current capital/finance leases
Question 3 – Do the Boards agree that the transition requirement in paragraph 92 of the ED should be extended to all leases currently classified as capital/finance leases and with the drafting change as outlined in paragraph 50 of this memo? If not, why not?

Staff analysis of transition disclosures

Background

51. The staff notes that paragraph 96 of the IASB ED states that:

> An entity shall provide the transition disclosures required by IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, without the disclosure of adjusted basic and diluted earnings per share.

52. The Boards discussed transition disclosures in March 2010 and tentatively decided that transition disclosures should be required in accordance with the guidance in Topic 250 and IAS 8. However, the requirement for U.S. GAAP was not included in the ED.

Analysis and staff recommendations

53. The staff notes that no feedback was received on the transition disclosures, specifically. Therefore, the staff recommends that the Boards confirm their tentative decision to require an entity to provide transition disclosures required by IAS 8 for IFRS preparers and also include, for U.S. GAAP preparers, that an entity provide disclosures required by Topic 250. An excerpt of that guidance is included in Appendix A of this memo.

54. Additionally, if the Boards agree with the staff recommendation in Question 2 (to provide reliefs for transition), the staff thinks that it would be useful to provide transition disclosures about any of the reliefs in Question 2 elected by an entity. That is consistent with the revenue recognition proposals.

55. However, the revenue recognition proposals also include a requirement to disclose, to the extent reasonably possible, a qualitative assessment of the estimated effect of applying each of those reliefs. The staff has concerns with the application of such a disclosure requirement in the context of lease contracts because of the possible cost of providing that information. That is, although the staff recommends providing reliefs, requiring a qualitative assessment may be costly and may possibly remove much of the transition relief being provided to preparers. Therefore, the staff does not recommend that the Boards require a qualitative assessment of the likely effect of applying reliefs.

Question 4 – Transition disclosures
Question 4 – The staff recommends that the Boards require transition disclosures consistent with IAS 8 and Topic 250. Additionally, the staff recommends that, if an entity elects any of the available reliefs in Question 2, that entity should disclose which reliefs have been elected. Do the Boards agree with the staff recommendation? If not, why not?

Appendix A – Disclosure Requirements of Topic 250 and IAS 8

IAS 8, paragraphs 28-31

28. When initial application of an IFRS has an effect on the current period or any prior period, would have such an effect except that it is impracticable to determine the amount of the adjustment, or might have an effect on future periods, an entity shall disclose:

    (a) the title of the IFRS;

    (b) when applicable, that the change in accounting policy is made in accordance with its transitional provisions;

    (c) the nature of the change in accounting policy;

    (d) when applicable, a description of the transitional provisions;

    (e) when applicable, the transitional provisions that might have an effect on future periods;

    (f) for the current period and each prior period presented, to the extent practicable, the amount of the adjustment:

        (i) for each financial statement line item affected; and

        (ii) if IAS 33 *Earnings per Share* applies to the entity, for basic and diluted earnings per share;

    (g) the amount of the adjustment relating to periods before those presented, to the extent practicable; and

    (h) if retrospective application required by paragraph 19(a) or (b) is impracticable for a particular prior period, or for periods before those presented, the circumstances that led to the existence of that condition and a description of how and from when the change in accounting policy has been applied.

Financial statements of subsequent periods need not repeat these disclosures.

29. When a voluntary change in accounting policy has an effect on the current period or any prior period, would have an effect on that period except that it is

impracticable to determine the amount of the adjustment, or might have an effect on future periods, an entity shall disclose:

(a) the nature of the change in accounting policy;

(b) the reasons why applying the new accounting policy provides reliable and more relevant information;

(c) for the current period and each prior period presented, to the extent practicable, the amount of the adjustment:

(i) for each financial statement line item affected; and

(ii) if IAS 33 applies to the entity, for basic and diluted earnings per share;

(d) the amount of the adjustment relating to periods before those presented, to the extent practicable; and

(e) if retrospective application is impracticable for a particular prior period, or for periods before those presented, the circumstances that led to the existence of that condition and a description of how and from when the change in accounting policy has been applied.

Financial statements of subsequent periods need not repeat these disclosures.

30. When an entity has not applied a new IFRS that has been issued but is not yet effective, the entity shall disclose:

(a) this fact; and

(b) known or reasonably estimable information relevant to assessing the possible impact that application of the new IFRS will have on the entity's financial statements in the period of initial application.

31. In complying with paragraph 30, an entity considers disclosing:

(a) the title of the new IFRS;

(b) the nature of the impending change or changes in accounting policy;

(c) the date by which application of the IFRS is required;

(d) the date as at which it plans to apply the IFRS initially; and either:

(i) a discussion of the impact that initial application of the IFRS is expected to have on the entity's financial statements; or

(ii) if that impact is not known or reasonably estimable, a statement to that effect.

Section 250-10-50

[General Note: Section 250-10-50 provides guidance on the disclosure in the notes to financial statements. In some cases, disclosure may relate to disclosure on the face of the financial statements.]

> Accounting Changes

> > Change in Accounting Principle

250-10-50-1 An entity shall disclose all of the following in the fiscal period in which a **change in accounting principle** is made:

a. The nature of and reason for the change in accounting principle, including an explanation of why the newly adopted accounting principle is preferable.

b. The method of applying the change, including all of the following:

1. A description of the prior-period information that has been retrospectively adjusted, if any.
2. The effect of the change on income from continuing operations, net income (or other appropriate captions of changes in the applicable net assets or performance indicator), any other affected financial statement line item, and any affected per-share amounts for the current period and any prior periods retrospectively adjusted. Presentation of the effect on financial statement subtotals and totals other than income from continuing operations and net income (or other appropriate captions of changes in the applicable net assets or performance indicator) is not required.
3. The cumulative effect of the change on retained earnings or other components of equity or net assets in the statement of financial position as of the beginning of the earliest period presented.

4. If **retrospective application** to all prior periods is impracticable, disclosure of the reasons therefore, and a description of the alternative method used to report the change (see paragraphs 250-10-45-5 through 45-7).

c. If indirect effects of a change in accounting principle are recognized both of the following shall be disclosed:

1. A description of the indirect effects of a change in accounting principle, including the amounts that have been recognized in the current period, and the related per-share amounts, if applicable

2. Unless impracticable, the amount of the total recognized indirect effects of the **accounting change** and the related per-share amounts, if applicable, that are attributable to each prior period presented. Compliance with this disclosure requirement is practicable unless an entity cannot comply with it after making every reasonable effort to do so.

Financial statements of subsequent periods need not repeat the disclosures required by this paragraph. If a change in accounting principle has no material effect in the period of change but is reasonably certain to have a material effect in later periods, the disclosures required by (a) shall be provided whenever the financial statements of the period of change are presented.

250-10-50-2 An entity that issues interim financial statements shall provide the required disclosures in the financial statements of both the interim period of the change and the annual period of the change.

250-10-50-3 In the fiscal year in which a new accounting principle is adopted, financial information reported for interim periods after the date of adoption shall disclose the effect of the change on income from continuing operations, net income (or other appropriate captions of changes in the applicable net assets or performance indicator), and related per-share amounts, if applicable, for those post-change interim periods.