MINUTES

Financial Accounting Standards Board

To:	Board Members		
From:	Leases Team		
Subject:	Minutes of May 17, 2011, and May 19, 2011, Joint Board Meeting	**Date:**	May 23, 2011
cc:	FASB: Cosper, Bielstein, Lott, Proestakes, Stoklosa, Mechanick, Zeyher, Bauer, Helmus, Gonzales, Paul, Spreitzer, C. Smith, Brickman, Glotzer, Gabriele, Sutay, FASB Intranet, McGarity, Klimek; FASAC: Chookaszian, Posta, Guasp; GASB: Finden, Avis; IASB: Rees, Humphreys, Lian, Vatrenjak, Kim, Geisman, Davidson, Buchanan		

The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue an Accounting Standards Update or a Statement of Financial Accounting Concepts.

Topic: Leases

Basis for Discussion:

FASB Memo 167—Cover Memo

FASB Memo 169—Contract modifications or changes in circumstances after the date of inception of the lease

FASB Memo 170—Distinguishing between lease accounting approaches

FASB Memo 171—Lessee accounting – other-than-finance lease

FASB Memo 172—Lessor accounting: Finance leases – measurement and presentation

FASB Memo 173—Lessor accounting – other-than-finance lease

FASB Memo 174—Reassessment of options in a lease

FASB Memo 175—Reassessment of the discount rate in a lease

FASB Memo 176—Lessee accounting approach

Length of Discussion:	May 17: 11:45AM to 1:00PM EST May 19: 3:30AM to 8:00AM EST
Attendance:	
Board members present:	FASB: Buck, Golden, Linsmeier, Schroeder Seidman, Seigel, Smith IASB: Tweedie, Cooper, Danjou, Engström, Finnegan, Gomes, König, McGregor, Pacter, Scott, Smith, Yamada, Zhang
Board members participating via telephone:	McConnell
Board members absent:	Kalavacherla
Staff in charge of topic:	FASB: Zeyher IASB: Humphreys
Other staff at Board table:	FASB: Stoklosa IASB: Rees, Buchanan, Vatrenjak, Lian
Staff participating via video:	FASB: Stoklosa, Gonzales, Cappiello, Spreitzer, Paul
Outside participants:	None

<u>Type of Document and Timing Based on the Technical Plan</u>:

The Board met to discuss issues relating to the development of a final Accounting Standards Update addressing leases.

The Board's technical plan calls for that document to be issued in the third quarter of 2011.

<u>Summary of Decisions Reached</u>:

The IASB and the FASB continued their discussion on leases and discussed the following topics: lessee accounting, lessor accounting, contract modifications or changes in circumstances after the date of inception of the lease, reassessment of options in a lease, and reassessment of the discount rate in a lease.

Lessee Accounting

The Boards tentatively decided that lessees should apply a single accounting approach for all leases consistently with the approach proposed in the Leases Exposure Draft. This accounting approach would require a lessee to:

1. Initially recognize a liability to make lease payments and a right-of-use asset, both measured at the present value of the lease payments.
2. Subsequently measure the liability to make lease payments using the effective interest method.
3. Amortize the right-of-use asset on a systematic basis that reflects the pattern of consumption of the expected future economic benefits.

(FASB 5 to 2; IASB 10 to 4)

At a future meeting, the Boards will consider further:

1. The presentation and disclosure of additional information about amortization of the right-of-use asset, interest expense on the liability to make lease payments, total lease expense, and lease payment cash flows.
2. Short-term lease accounting.

Lessor Accounting

The Boards discussed the accounting by lessors under a right-of-use model.

The Boards discussed whether there should be one or two approaches to lessor accounting. The Boards will continue discussing this issue at a future meeting, at which they will consider the implications of their decision to require a single approach to lessee accounting. The Boards requested the staff to provide further analysis at a future meeting that compares the accounting described below with the accounting for lessors applying operating lease accounting in existing IFRS and U.S. GAAP.

Lessor accounting: one approach

The Boards discussed accounting for the underlying asset and the residual asset if there is a single approach to lessor accounting. If a single approach is used, the Boards tentatively decided that:

1. The lessor would derecognize a portion of the carrying amount of the underlying asset. (FASB: unanimous; IASB: 12 to 2)
2. The lessor would initially measure the residual asset as an allocation of the carrying amount of the underlying asset. (FASB: unanimous; IASB: unanimous).
3. The lessor would subsequently measure the residual asset by accreting the amount of the residual asset over the lease term, using the rate that the lessor charges the lessee. (FASB: 5 to 2; IASB: unanimous)

Lessor accounting: two approaches

The Boards tentatively decided that if there are two approaches to lessor accounting, distinguishing between those two approaches would be based on indicators relating to a definition of whether the lease transfers substantially all of the risks and rewards incidental to ownership of the underlying asset. These indicators would:

1. Include a “fair value indicator”; (FASB: 4 to 3; IASB: 12 to 2)
2. Include a “variable rent indicator”; and (FASB: 5 to 2; IASB: unanimous)
3. Not include an “embedded or integral services indicator.” (FASB 4 to 3; IASB 13 to 1)

The Boards discussed the accounting for the underlying asset and the residual asset if there are two approaches to lessor accounting. If substantially all of the risks and rewards of ownership of the underlying asset are transferred to the lessee and the lessor does not apply operating lease accounting in existing IFRS and U.S. GAAP, the Boards indicated a preference that the lessor would:

1. Derecognize the entire carrying amount of the underlying asset. (FASB: unanimous; IASB: unanimous)
2. Initially measure the residual asset at the present value of the estimated value of the underlying asset at the end of the lease term, discounted using the rate that the lessor charges the lessee. (FASB: unanimous; IASB: unanimous)

3. Subsequently measure the residual asset by accreting the amount of the residual asset over the lease term using the rate the lessor charges the lessee. (FASB: 5 to 2; IASB: unanimous)

Accounting for the right to receive lease payments

The Boards indicated a tentative preference for measuring a lessor's right to receive lease payments in accordance with the requirements for other similar financial assets. The Boards nevertheless requested the staff to analyze whether this would create any unintended consequences, specifically if the Boards were to specify two approaches for lessor accounting.

Presentation of the lessor's right to receive lease payments and the residual asset

The Boards tentatively decided that a lessor should present its right to receive lease payments separately from any residual asset. The Boards will discuss the presentation of the residual asset at a future meeting. (FASB: unanimous; IASB: 7 agreed)

Contract Modifications or Changes in Circumstances after the Date of Inception of the Lease

The Boards tentatively decided to provide guidance on accounting for changes after the date of inception of the lease as follows:

1. A modification to the contractual terms of a contract that is a substantive change to the existing contract should result in the modified contract being accounted for as a new contract. The change is a substantive change if it results in a different determination of whether the contract is, or contains, a lease or, if applicable, whether the contract transfers substantially all of the risks and rewards incidental to ownership of the underlying asset.
2. A change in circumstances other than a modification to the contractual terms of the contract that would affect the assessment of whether a contract is, or contains, a lease should result in a reassessment as to whether the contract is, or contains, a lease.
3. A change in circumstances other than a modification to the contractual terms of the contract that would affect whether a lease transfers substantially all of the risks and rewards incidental to ownership of the underlying asset should not result in a reassessment or a change in the accounting approach.

(FASB: unanimous; IASB: unanimous)

Reassessment of Options in a Lease

The Boards discussed how lessees and lessors should reassess whether a lessee has a significant economic incentive to exercise:

1. An option to extend or terminate a lease, and
2. An option to purchase the underlying asset.

The Boards tentatively decided that a lessee and a lessor should consider contract-based, asset-based, and entity-based factors in reassessing whether a lessee has a significant economic incentive to exercise an option. The boards noted that all these factors should be considered together and the existence of only one factor does not necessarily, by itself, signify a significant economic incentive to exercise the option. (FASB: 5 to 2; IASB: 8 to 6).

The Boards tentatively decided that the thresholds for evaluating a lessee's economic incentive to exercise options to extend or terminate a lease and options to purchase the underlying asset should be the same for both initial and subsequent evaluation, except that a lessee and lessor should not consider changes in market rates after lease commencement when evaluating whether a lessee has a significant economic incentive to exercise an option. (FASB: unanimous; IASB: unanimous)

The Boards tentatively decided that changes in lease payments that is due to a reassessment in the lease term should result in:

1. A lessee adjusting its obligation to make lease payments and its right-of-use asset; and
2. A lessor adjusting its right to receive lease payments and any residual asset, and recognizing any corresponding profit or loss (pending the Boards' decision on lessor accounting).

(FASB: unanimous; IASB: unanimous)

Reassessment of the Discount Rate

The Boards discussed whether there are circumstances that would require a lessee or a lessor to reassess the discount rate that is used to measure the present value of lease payments.

The Boards tentatively decided that the discount rate should not be reassessed if there is no change in the lease payments.

The Boards tentatively decided that the discount rate should be reassessed when the changes below are not reflected in the initial measurement of the discount rate:

1. When there is a change in lease payments that is due to a change in the assessment of whether the lessee has a significant economic incentive to exercise an option to extend a lease or to purchase the underlying asset.
2. When there is a change in lease payments that is due to the exercise of an option that the lessee did not have a significant economic incentive to exercise.

The Boards also decided that a lessee or lessor should determine a revised discount rate using the spot rate at the reassessment date and should then apply that rate to the remaining lease payments (i.e. to the remaining payments due in the initial lease plus the payments due during the extension period or upon exercise of a purchase option).

(FASB: unanimous; IASB: unanimous)

General Announcements: None.