

# CB RICHARD ELLIS ENTERPRISE NOTES

April 2011

## Update on the IASB and FASB Proposals for Lessee Accounting

### Comments heard loud and clear – Boards considering revisions

The International Accounting Standards Board and the Financial Accounting Standards Board (the “Boards”) received a total of 785 comment letters, including **CBRE’s**, following the release of the August 2010 Exposure Draft (ED) detailing their proposed changes to lease accounting.

What they heard, loud and clear, from their stakeholders were significant concerns over the subjectivity, complexity and burden the proposed standard would impose on companies.

In response to these comments, the Boards are now seriously deliberating the revision of several of the more onerous provisions of the ED. From our perspective, these potential revisions are a positive sign for the real estate industry. Although far from being finalized, please see a detailed discussion of the Boards latest perspectives and guidance on several of the key areas in an updated CBRE ViewPoint on this important topic.

#### [Click here to download the Report](#)

A summary of the highlights of the ViewPoint discussion addressing **possible** changes to lessee accounting, include:

#### Profit & Loss Impact

- The ED requires all leases to be capitalized and expensed in an accelerated pattern involving a **combination of amortization expense** (related to the right-of-use asset) **and interest expense** (related to the corresponding liability).
- The Boards are **now contemplating classifying leases as either a “Finance Lease” or an “Other-Than-Finance Lease”** and are proposing a different pattern of profit and loss recognition in the income statement for each type.
- A **Finance Lease** is **one that includes a financing element to the lease**. The pattern of profit and loss recognition in this case would be consistent with the ED (i.e. interest would be calculated using the Effective Interest Method).
- In the case of an **Other-Than-Finance Lease**, a **financing component is not a significant component of the lease structure**. The timing of the profit and loss recognition for these leases may be structured to be consistent with current U.S. GAAP for operating leases (i.e. straight-line basis).
- The Boards have **developed preliminary criteria to distinguish between the two lease types**. Initial indications seem to generally favor real estate leases being classified as an Other-Than-Finance Lease.

## Balance Sheet Impact

- Whether a lease is classified as a Finance Lease or an Other-Than-Finance Lease, the **Boards will still require it to be capitalized** on a company's balance sheet.

## Lease Term

- The ED **proposes a “more likely than not” threshold** to be used in determining whether options to renew or terminate are to be taken into account in determining the amount to be capitalized on the balance sheet.
- The latest deliberations indicate the Boards are considering requiring the inclusion of **options only if 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.”

## Variable/Contingent Rent

- The ED proposes that percentage **rent be included in the capitalized value of the lease** and be determined based on a reasonably possible number of sales projections for the term of the lease and applying a weighted average probability to each (i.e. Expected Outcome Approach).
- The Boards have indicated that the requirement to include percentage rent in the amount to be capitalized may be based on a **higher threshold of being “reasonably certain”** of receiving the percentage rent.

## Implementation Timeframe

- Although no specific guidance has been provided, we believe implementation of the new standard will be **no earlier than 2014** and that 2015 is more likely.

We believe the Boards are moving in the right direction in their re-deliberations, and the final standard could ultimately be less impactful and burdensome than originally proposed in the ED. However, that being said, nothing is certain until the final standard is issued in mid- to late-2011.

The CB Richard Ellis Global Task Force on Lease Accounting is actively participating in the Boards' outreach program and will continue to be diligent in our efforts to support changes to the benefit of the real estate industry. We will continue to keep you apprised of future developments.

*The CB Richard Ellis Global Task Force on Lease Accounting is composed of the following team members:*

- [Jeff Beatty](#), Financial Consulting Group (Task Force Director)
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read the CB Richard Ellis Special Report entitled Upcoming Change in Accounting For Leases: A Series”.

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