A new lease accounting standard seeks to increase transparency and comparability with regard to one of the largest off-balance-sheet financing items.

This thought leadership paper, provides more details

The Financial Accounting Standards Board ('FASB') has followed the footsteps of the International Accounting Standards Board and issued its new standard on Leases on February 25, 2016. Lessees will now be required to record assets and liabilities emanating out of rights and obligations created by all leases with a term in excess of 12 months.

The previous accounting guidance on leases, only required capital or financing leases to be recognized on the balance sheet of lessees. The new Accounting Standards Update ('ASU') No 2016-02, Leases, will apply to both, capital leases and operating leases. Lessees will recognize a right-of-use asset and a lease liability. The accounting for lessors under the new GAAP is similar to that under current GAAP.

The primary intention of the new lease accounting standard is to increase transparency and comparability with regard to one of the largest off-balance-sheet financing items. The ASU will also require quantitative and qualitative disclosures, including information on the amount, timing and uncertainty of cash flows arising from leases.

The IASB and FASB have been working together on a convergence standard on leases. The IASB issued its leases standard in January, which requires all leases to be accounted as financing leases.

The FASB decided on a dual approach for lessee accounting, *with lease classification determined in accordance with the principle in existing lease requirements (that is, determining whether a lease is effectively an instalment purchase by the lessee)*.

Under this approach, a lessee would account for most existing capital leases as finance leases *(that is, recognizing amortization of the right-of-use asset separately from interest on the lease liability)* and most existing operating leases as operating leases *(that is, recognizing a single total lease expense).*

The IASB decided on a single approach for *lessee accounting. Under that approach, a lessee would account for all leases as finance leases (that is, recognizing amortization of the right-of-use asset separately from interest on the lease liability)*.

ASU 2016-02 will take effect for public companies for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. For all other organizations, the ASU on leases will take effect for fiscal years beginning after December 15, 2019, and for interim periods within fiscal years beginning after December 15, 2020. Early application will be permitted for all organizations.

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