FASB FINANCIAL ACCOUNTING STANDARDS BOARD

MEMO

Memo No. **8**

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Project	**PCC Leases Research Project**
Project Stage	**Research**
Issue	**Update on Project Activities**

Memo Purpose

1. The purpose of this memo is to provide Private Company Council (PCC) members with an update on activities that have taken place since the discussion at the December 2025 PCC meeting on the PCC leases research project. This memo does not include staff analysis or recommendations.

2. This memo is organized as follows:

   (a) Background

   (b) Leases Working Group Meeting

   (c) Recent Stakeholder Feedback

   (d) Next Steps

   (e) Appendix A—Excerpts from Topic 840, Leases.

Question for the PCC

1. Do PCC members have any questions or concerns about the recommendations reached by the leases working group at its January 2026 meeting on the following areas (all from a lessee perspective)?

   a. Optional single lease classification accounting model

   b. Scope exception for low value leases

   c. Embedded leases

   d. Lease classification criteria

   e. Lease modifications

f. Weighted-average lease disclosures

g. Related party disclosures.

The leases working group recommendations are summarized as follows:

Discontinue research on:

(a) Optional single lease classification accounting model

(b) Scope exception for low value leases.

Continue research on:

(c) Embedded leases

(d) Lease classification criteria

(e) Lease modifications

Continue research on (combined with other lease accounting issues rather than as standalone projects):

(f) Weighted-average lease disclosures

(g) Related party disclosures.

Background

3. As private companies have implemented and continue to apply Topic 842, Leases (hereinafter referred to as the leases standard), PCC members have reported that certain areas of the guidance continue to be costly and overly complex. While the leases standard provides some relief for private companies, such as a lessee's determination of the discount rate and accounting for common control arrangements, PCC members have indicated that additional simplifications for private companies should be explored.

4. Since mid-2024, the PCC (through its leases working group) has been conducting research on the leases standard. The PCC has regularly discussed the continual progress made by the working group at its meetings.

5. During the December 2025 PCC meeting, members discussed the key takeaways from the December 2025 leases working group meeting and recent stakeholder feedback. PCC members provided input on the following areas: (a) an optional single lease classification accounting model, (b) a scope exception for low value leases, (c) lease modifications, (d) embedded leases, (e) lease classification criteria, (f) weighted-average lease disclosures, and (g) related party lease disclosures. PCC members encouraged the working group to continue to research certain areas for private company simplification and expressed the need to conduct further outreach with private company financial statement users and other private company stakeholders. Detailed information can be found in the December 2025 PCC meeting Memo 7D and the December 2025 PCC meeting minutes.

Leases Working Group Meeting

6. Taking into consideration the discussion among PCC members at their December 2025 meeting and private company stakeholder feedback, the leases working group met in mid-January 2026 and reached recommendations on whether the PCC should continue to research the specific areas included in Question 1 of this memo. A summary of those discussions is included in the paragraphs below.

7. Broadly, working group members highlighted a recent shift in stakeholder sentiment in which some stakeholders have indicated that significant or fundamental changes should not be made to the leases standard. Working group members discussed the following reasons for that stakeholder feedback:

   (a) For those private companies that have invested in updated systems and processes, significant changes to the leases standard could result in further updates that need to be made to systems and processes, which could create additional costs.

   (b) Private companies are becoming more comfortable in applying the leases standard.

   (c) Private companies are hesitant about further changes being made to the leases standard after experiencing significant challenges in adopting the standard.

   (d) Private company financial statement users have updated their financial statement analysis models and understand the financial reporting effects of the leases standard. Significant changes could necessitate additional changes to users' models and additional education.

8. Working group members expressed concerns that making significant changes to the leases standard could result in unintended consequences for those companies and users whose systems and processes are already in place. However, targeted private company simplifications to the leases standard and, in certain areas, further education on the leases standard, could be helpful for the private company community.

Optional Single Lease Classification Accounting Model

9. Working group members discussed stakeholder feedback from recent PCC liaison meetings, highlighting feedback from private company users (lenders) who indicated that they would not support an optional single lease classification accounting model for lessees. Those lenders view operating leases differently than finance leases and noted that a fundamental change to the lease accounting model would significantly affect their financial statement analyses.[1] The FASB staff notes that those users also expressed other concerns about an optional single lease classification accounting model, for example:

[1] The FASB staff notes that an overarching principle of the Private Company Decision-Making Framework (PCDMF) is that user relevance is a primary consideration in determining whether and in what circumstances to provide private company accounting alternatives.

(a) Terms and conditions of many private company debt arrangements would need to be modified because they currently differentiate between operating and finance leases, which would be costly for private companies. Additionally, debt covenant ratios could be affected by a single lease classification accounting model.

(b) A substantial amount of time was spent helping credit officers become familiar with the leases standard. A fundamental change to the leases standard would require additional training for credit officers.

(c) A single lease classification accounting model might reduce costs for preparers but would increase costs for users.

10. Working group members also cited the mixed feedback obtained from private company preparers and practitioners in this area. The FASB staff notes that some of those stakeholders stated that an optional single lease classification accounting model could reduce the cost and complexity in applying the leases standard and would increase convergence with International Financial Reporting Standards 16, *Leases* (IFRS 16). However, other stakeholders did not support a fundamental change to the lease accounting model for various reasons, including:

(a) A dual classification model retains the important distinction between arrangements that are ownership-like and those that are rent.

(b) There may not be a reduction in cost and complexity under an optional single lease classification model because private companies would still have to evaluate whether a lease exists and then would still need to account for the lease.

(c) Transitioning from a dual model to a single model could be costly and changing the standard again would result in a need for more education.

(d) Similar amounts of time are spent accounting for leases (whether financing or operating) and once systems and processes are established, that accounting becomes routine unless a lease modification occurs.

(e) During the development of the leases standard, there was significant stakeholder feedback obtained to retain a dual model and a single lease classification accounting model would be a difficult change.

11. Additionally, during the December 2025 PCC meeting, several members indicated that based on recent feedback from private company financial statement users, an optional single lease classification accounting model for lessees may not be a feasible alternative for private companies.

12. On the basis of stakeholder feedback and the December 2025 PCC meeting discussion, the working group recommended that an optional single lease classification accounting model for lessees should no longer be pursued, noting that there is no feasible path forward.

Scope Exception for Low Value Leases

13. Working group members discussed stakeholder feedback from recent PCC liaison meetings, noting that a majority of private company stakeholders indicated that private companies generally apply the materiality guidance[2] and capitalization thresholds in accounting for leases; therefore, an explicit scope exception for low value leases is unnecessary.

14. Working group members also discussed the potential challenges and unintended consequences of developing and providing a private company scope exception for low value leases, including (a) establishing a threshold that would be appropriate for all sizes of private companies to apply; (b) setting precedent in establishing materiality guidance for one area of GAAP and setting the stage for low-value exceptions to be established in other areas of GAAP, which may not be consistent with the general materiality guidance; and (c) introducing more complexity in applying the leases standard.

15. Additionally, during the December 2025 PCC meeting, there was mixed feedback among PCC members on whether to pursue a scope exception for low value leases. Some PCC members highlighted the expected challenges in developing an exception and considered whether educational materials in applying materiality could be provided instead.

16. On the basis of stakeholder feedback and the December 2025 PCC meeting discussion, the working group recommended that a scope exception for low value leases should no longer be pursued, noting that the materiality guidance in paragraph 105-10-05-6 already provides flexibility for private companies to establish capitalization thresholds, which is consistent with the basis for conclusions in Accounting Standards Update No. 2016-02, *Leases (Topic 842)*. The basis for conclusions explains the Board's rationale for not including a recognition and measurement exemption for leases of low value assets as follows:

> BC122. The Board observed that, in addition to accounting for some leases at a portfolio level, entities will likely be able to adopt reasonable capitalization thresholds below which lease assets and lease liabilities are not recognized, which should reduce the costs of applying the guidance. An entity's practice in this regard may be consistent with many entities' accounting policies in other areas of GAAP (for example, in capitalizing purchases of property, plant, and equipment).

17. Working group members discussed whether educational materials could be provided to remind stakeholders about the materiality guidance and provide illustrative examples on establishing reasonable capitalization thresholds. However, working group members noted that it could be difficult to develop educational materials because applying the materiality guidance is an entity-specific consideration that requires judgment and because of the interaction with auditing standards, which would be beyond the scope of an FASB staff educational paper.

[2] Paragraph 105-10-05-6 states that the provisions of the Codification need not be applied to immaterial items.

Post-Implementation Review of IFRS 16—Low Value Lease Exemption

18. In connection with its post-implementation review of IFRS 16, the IASB staff published a memo in January 2026 (after the PCC leases working group meeting) that includes a summary of stakeholder feedback on the IFRS 16 low value lease exemption (see paragraphs 12 through 14 of the memo). To summarize, some IFRS stakeholders raised concerns that the exemption was not effective at reducing the ongoing costs of applying IFRS 16. Stakeholder comments included:

    (a) The existing guidance lacks clarity; for example, the threshold of $5,000 in paragraph BC100 of the Basis for Conclusions on IFRS 16[3] and the reference to cars in paragraph B6 of IFRS 16[4] are not helpful. In these stakeholders' view, this leads to diversity in practice, because the relationship between materiality and the threshold is unclear, which complicates discussions about materiality with auditors and generates costs, as well as reduces the comparability of information for users of financial statements.

    (b) The threshold of $5,000 is outdated. It has not been updated for inflation since IFRS 16 was issued 10 years ago and it does not adequately reflect changes in prices and exchange rates, which result in higher-than-expected costs because more items exceed the $5,000 threshold and therefore fall outside the scope of the recognition exemption.

    (c) The exemption creates structuring opportunities, such as disaggregating contracts into a number of low-value contracts below the threshold to manage balance sheet effects, which reduce the usefulness of information for users.

    IFRS stakeholders suggested that the IASB increase the $5,000 threshold on a regular basis (in line with changes in market prices) or remove the $5,000 threshold from the Basis for Conclusions in IFRS 16 and avoid including any specific amounts in future IFRS accounting standards.

Embedded Leases

19. Working group members discussed a potential simplification in accounting for embedded leases, noting that some private companies continue to find this area challenging. Consistent with past stakeholder feedback, the working group discussed researching an optional private company accounting simplification to forgo the recognition and measurement of an embedded lease included in a service arrangement in certain scenarios.

[3] Paragraph BC100 of the Basis for Conclusions in IFRS 16 states: "At the time of reaching decisions about the exemption in 2015, the IASB had in mind leases of underlying assets with a value, when new, in the order of magnitude of US$5,000 or less."

[4] Paragraph B6 of IFRS 16 states: "For example, leases of cars would not qualify as leases of low-value assets because a new car would typically not be of low value."

20. Members suggested that the optional simplification could include a qualitative threshold (rather than a bright line quantitative threshold) that would be used to evaluate whether an embedded lease included in a service arrangement would need to be recognized and measured. Some members noted that leveraging the revenue recognition guidance in paragraph 606-10-25-16A, which states that an entity is not required to assess whether promised goods or services are performance obligations if they are immaterial in the context of the contract with the customer, could be a good starting point for developing the qualitative threshold because private companies should already be familiar with applying the "immaterial in the context of a contract" notion. Other members suggested exploring a predominance principle supported by illustrative examples.

21. The working group recommended that the research on embedded leases should continue on the basis that an optional private company simplification would provide meaningful cost and complexity relief and could be achievable from a standard-setting perspective.

Lease Classification Criteria

22. Working group members discussed a potential simplification in the area of lease classification for certain real estate leases, noting that the lease classification criteria that requires an assessment of whether the present value of the sum of the lease payments equals or exceeds substantially all of the fair value of the underlying asset (referred to as the substantially all classification criteria) is costly and complex and may not result in decision-useful information.

23. Working group members noted that when applying the substantially all classification criteria, there are scenarios in which long-term land and/or real estate leases are classified as finance leases even though the lease arrangements do not include a bargain purchase option or a transfer of ownership to the lessee and that a finance lease classification does not reflect the underlying economics.

24. Working group members expressed interest in potentially bringing back an approach from Topic 840, Leases,[5] in which certain land and real estate leases that do not include transfer of ownership or bargain purchase option terms were automatically classified as operating leases, noting that such an approach would avoid applying the substantially all criteria. Members noted that providing private companies with an option to forgo the substantially all classification criteria and account for certain land and real estate leases as operating could reduce the cost and complexity of applying the guidance and would better reflect the economics of many transactions.

25. Working group members agreed that research and outreach are needed to identify the land and real estate leases that should qualify for the option and to evaluate whether a potential exception would improve consistency, reduce complexity, and increase decision-usefulness for users.

[5] See Appendix A of this memo for excerpts from Topic 840, Leases.

Lease Modifications

26. Working group members stated that it can be costly and complex to reassess the classification of a lease when a modification occurs and the modification does not meet the criteria to be accounted for as a separate contract. Members observed that the complexity involved in applying the "substantially all criteria," as noted in the lease classification discussion above, also applies to this issue.

27. As such, members suggested researching a private company simplification for "plain-vanilla" modifications that would not require a reassessment of certain items (for example, discount rate, fair value of the leased assets) in scenarios in which the modification does not include significant changes and instead, a private company would simply remeasure the lease liability to reflect the new lease term without reassessing lease classification. The lease classification reassessments for lease modifications that contain significant changes, such as the addition of a bargain purchase option or transfer of ownership, would be retained and would be unaffected by the simplification.

28. Members acknowledged that creating a narrow-scope private company simplification would be difficult because lease modifications vary widely and could produce unintended accounting outcomes if classification changes are overlooked. The working group recommended that this issue should be pursued and that research and outreach are needed to ensure that any private company simplification is clearly and narrowly defined.

Weighted-Average Lease Disclosures

29. The working group recommended that there could be merit in considering whether private companies should continue to be subject to the weighted-average lease disclosure requirements and that this issue should be combined with other lease accounting simplifications rather than being pursued as a standalone project.

30. Mixed feedback has been obtained in the past on the cost and complexity in gathering information for and preparing weighted-average lease disclosures (that is, weighted-average discount rates and weighted-average remaining lease term). Past feedback from private company financial statement users (albeit limited) indicated that those disclosures are useful.

Related Party Disclosures

31. Working group members discussed user feedback that indicated that enhanced disclosures about related party leases and their effect on the financial statements are needed. Members discussed several potential areas of missing or unclear disclosures, such as amounts of prepaid rent, underlying mortgages or owner guarantees, future cash outflows associated with a related party lease, and other related party lease amounts included in line items on the balance sheet.

32. The working group acknowledged that further input is needed from users about what specific information about related party leases is currently not being disclosed and whether users are seeking that information pertaining only to common control lease agreements or all related party lease agreements. Working group members suggested preparing a narrow set of example disclosures to help facilitate future outreach meetings with users.

33. The working group recommended that there is merit in conducting further research; however, this issue should be combined with other lease accounting issues rather than as a standalone project.

Recent Stakeholder Feedback

34. A verbal update of recent stakeholder feedback received since the December PCC meeting will be provided at the March PCC meeting.

Next Steps

35. The PCC leases working group will continue its research on potential private company lease accounting simplifications and will report back to the PCC at a future meeting.

Appendix A—Excerpts from Topic 840, Leases

A1. This Appendix includes excerpts from Topic 840, Leases, to help inform PCC members about the previous lease classification guidance.

840-10-25-1
A lessee and a lessor shall consider whether a lease meets any of the following four criteria as part of classifying the lease at its inception under the guidance in the Lessees Subsection of this Section (for the lessee) and the Lessors Subsection of this Section (for the lessor):

a. Transfer of ownership. The lease transfers ownership of the property to the lessee by the end of the lease term. This criterion is met in situations in which the lease agreement provides for the transfer of title at or shortly after the end of the lease term in exchange for the payment of a nominal fee, for example, the minimum required by statutory regulation to transfer title.

b. Bargain Purchase Option: The lease contains a bargain purchase option.

c. Lease Term: The lease term is equal to 75 percent or more of the estimated economic life of the leased property. However, if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease.

d. Minimum Lease Payments: The present value at the beginning of the lease term of the minimum lease payments, excluding that portion of the payments representing executory costs such as insurance, maintenance, and taxes to be paid by the lessor, including any profit thereon, equals or exceeds 90 percent of the excess of the fair value of the leased property to the lessor at lease inception over any related investment tax credit retained by the lessor and expected to be realized by the lessor. If the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease).

840-10-25-29 If at its inception a lease meets any of the four lease classification criteria in paragraph 840-10-25-1, the lease shall be classified by the lessee as a capital lease.

840-10-25-30 If none of the four criteria in paragraph 840-10-25-1 are met, the lease shall be classified by the lessee as an operating lease.

Lessee Classification of a Lease Involving Real Estate

840-10-25-36 This guidance on a lessee's application of the four lease classification criteria in paragraph 840-10-25-1 to leases involving real estate is organized as follows:

a. Lease involving land only
b. Lease involving both land and buildings
c. Lease involving only part of a building.

Lease Involving Land Only

840-10-25-37 If land is the sole item of property leased and either the transfer-of-ownership criterion in paragraph 840-10-25-1(a) or the bargain-purchase-option criterion in paragraph 840-10-25-1(b) is met, the lessee shall account for the lease as a capital lease. Otherwise, the lessee shall account for the lease as an operating lease.

Lease Involving Both Land and Buildings

840-10-25-38 A lessee shall account for leases involving both land and building(s) as follows:

a. If the lease meets either the transfer-of-ownership criterion in paragraph 840-10-25-1(a) or the bargain-purchase-option criterion in paragraph 840-10-25-1(b), the land and building shall be separately capitalized by the lessee. For this purpose, the present value of the minimum lease payments after deducting executory costs, including any profit thereon, shall be allocated between

the two elements in proportion to their fair values at lease inception. If the lease agreement or commitment, if earlier, includes a provision to escalate minimum lease payments for increases in construction or acquisition cost of the leased property or for increases in some other measure of cost or value, such as general price levels, during the construction or preacquisition period, the effect of any increases that have occurred shall be considered in the determination of fair value of the leased property at lease inception for purposes of this paragraph.

b. If the lease does not meet either the transfer-of-ownership criterion in paragraph 840-10-25-1(a) or the bargain-purchase-option criterion in paragraph 840-10-25-1(b):

    1. If the fair value of the land is less than 25 percent of the total fair value of the leased property at lease inception, the lessee shall consider the land and the building as a single unit for purposes of applying the lease-term criterion in paragraph 840-10-25-1(c) and the minimum-lease-payments criterion in paragraph 840-10-25-1(d). For purposes of applying the lease-term criterion of paragraph 840-10-25-1(c), the estimated economic life of the building shall be considered as the estimated economic life of the unit. If either the lease-term criterion in paragraph 840-10-25-1(c) or the minimum-lease-payments criterion in paragraph 840-10-25-1(d) is met, the lessee shall capitalize the land and building as a single unit and amortize it in accordance with the guidance in paragraph 840-30-35-1(b), otherwise, the lease shall be accounted for by the lessee as an operating lease.

    2. If the fair value of the land is 25 percent or more of the total fair value of the leased property at lease inception, the lessee shall consider the land and the building separately for purposes of applying the lease-term criterion in paragraph 840-10-25-1(c) and the minimum-lease-payments criterion in paragraph 840-10-25-1(d). The minimum lease payments after deducting executory costs, including any profit thereon, applicable to the land and the building shall be separated by the lessee by determining the fair value of the land and applying the lessee's incremental borrowing rate to it to determine the annual minimum lease payments applicable to the land element; the remaining minimum lease payments shall be attributed to the building element. The lessee shall account for the building and land elements as follows:

        i. If the building element of the lease meets the lease-term criterion in 840-10-25-1(c) or the minimum-lease-payments criterion in paragraph 840-10-25-1(d), the building element shall be accounted for by the lessee as a capital lease and amortized in accordance with the guidance in paragraph 840-30-35-1(b). The land element of the lease shall be accounted for separately by the lessee as an operating lease.

        ii. If the building element of the lease meets neither the lease-term criterion in 840-10-25-1(c) nor the minimum-lease-payments criterion in paragraph 840-10-25-1(d), both the building element and the land element shall be accounted for by the lessee as a single operating lease.

Lease Involving Only Part of a Building

840-10-25-39 Unless both the cost and the fair value of the leased property are objectively determinable (as discussed in paragraph 840-10-25-23), a lease involving only part of a building shall be classified and accounted for by the lessee as follows:

a. If the fair value of the leased property is objectively determinable, the lessee shall classify and account for the lease according to the guidance in paragraph 840-10-25-38.

b. If the fair value of the leased property is not objectively determinable, the lessee shall classify the lease according to the lease-term criterion in paragraph 840-10-25-1(c) only, using the estimated economic life of the building in which the leased premises are located. If the lease-term criterion is met, the leased property shall be capitalized as a unit and amortized in accordance with the guidance in paragraph 840-30-35-1(b).