FASB FINANCIAL ACCOUNTING STANDARDS BOARD

PUBLIC MARKETS ADVISORY COMMITTEE
801 Main Avenue, Norwalk CT
May 15th, 2025

10:40 a.m.	**Advisory Session Begins**
10:40-10:45 a.m.	**Introductions and Opening Remarks**
10:45-11:20 a.m.	**Topic 1: Recognition of Intangibles** *Session Objective:* To update and solicit feedback from PMAC members on the Invitation to Comment—Recognition of Intangibles.
11:20 a.m.-12:00 p.m.	**Topic 2: Post-Implementation Review on Leases** *Session Objective:* To update and solicit feedback from PMAC members on the Post-Implementation Review on Topic 842, Leases.
12:00-1:00 p.m.	**Lunch** *(1 hour)*
1:00-1:30 p.m.	**Topic 3: Debt and Equity** *Session Objective:* To solicit feedback from PMAC members on the prevalence and accounting challenges related to debt or equity instruments issued by smaller public companies.
1:30-1:50 p.m.	**Topic 4: Definition of a Public Business Entity** *Session Objective:* To solicit feedback from PMAC members on the staff's research.
1:50-2:30 p.m.	**Topic 5: Agenda Consultation** *Session Objective:* To solicit feedback from PMAC members on the FASB's future standard-setting agenda.
2:30 p.m.	**Meeting Adjourned**

Advisory Session

- Topic 1: Recognition of Intangibles
- Topic 2: Post-Implementation Review on Leases
- Topic 3: Debt and Equity
- Topic 4: Definition of a Public Business Entity
- Topic 5: Agenda Consultation

The views expressed in this presentation are those of the presenter. Official positions of the FASB are reached only after extensive due process and deliberations

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Topic 1: Recognition of Intangibles

10:45–11:20 a.m.

Jill Switter	Senior Project Manager
Aarika Friend	Senior Project Manager
Kitrina Pople	Practice Fellow

FASB FINANCIAL ACCOUNTING STANDARDS BOARD® GASB GOVERNMENTAL ACCOUNTING STANDARDS BOARD® FAF FINANCIAL ACCOUNTING FOUNDATION®

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Project Overview

2020

December — The FASB Chair expanded the research project on intangibles to include recognition.

2021

December — A summary of the 2021 Invitation to Comment, *Agenda Consultation*, feedback was presented to the Board.

The FASB Chair clarified that the research project includes:
- Software costs
- Internally developed intangibles
- Research and development (R&D).

2022

June — The Board discussed the pre-agenda research.

Board members provided suggestions on the focus and prioritization for continued research efforts.

The Board added a separate project to its technical agenda on software costs.

2024

December — The FASB staff issued an ITC, *Recognition of Intangibles*, soliciting broad stakeholder feedback on whether the Board should pursue a project.

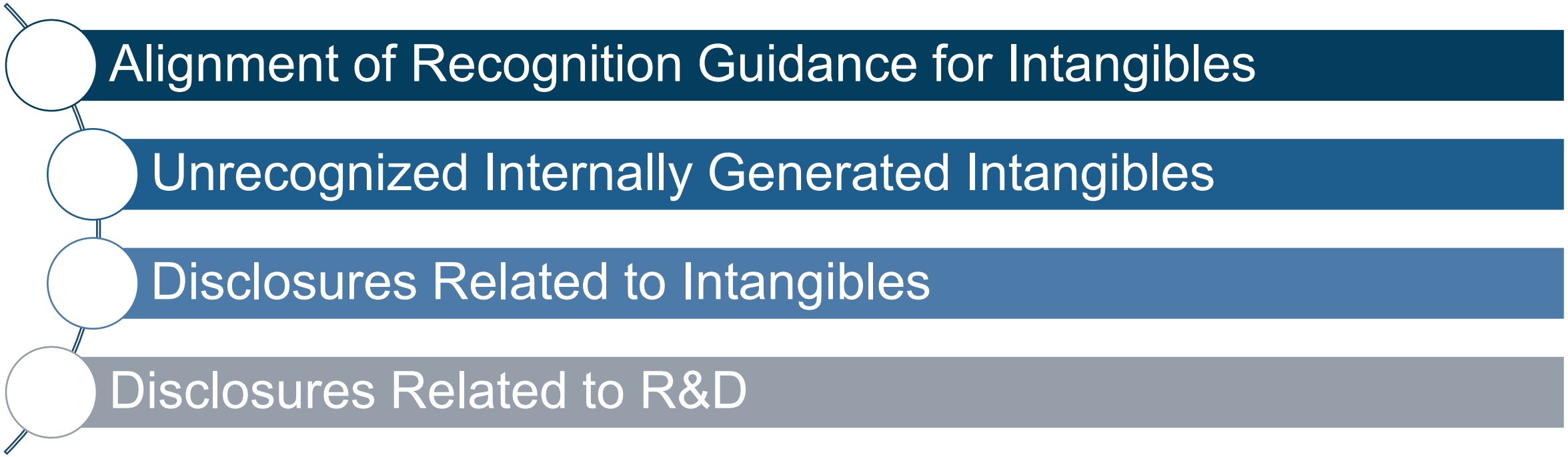
The ITC is seeking general feedback as well as feedback on specific areas within intangibles.

2025

May — Stakeholder feedback is due on May 30, 2025.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Highly Discussed Areas



Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

2024 Intangibles Invitation to Comment (ITC)

- **Objective:** Solicit broad stakeholder feedback on whether the Board should pursue a project on intangibles (link to ITC).
- The FASB staff would like to understand the following:

Is there a pervasive need to improve GAAP related to the accounting for and disclosure of intangibles?	What intangibles, or groups of intangibles, should the FASB consider addressing?	What potential solution(s) should the FASB consider, and what are the expected benefits and expected costs of the solution(s)?	Should the accounting for intangibles be different depending on how the asset is obtained?	What information do investors utilize (or would they utilize), and how does that information influence their resource allocation decisions?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Current GAAP

Intangible Assets Acquired in a Business Combination

Internally Developed Intangible Assets

- Asset Acquisition
- R&D
- Crypto Assets
- Internal-Use Software
- Industry-Specific Guidance
  - Extractive Activities
  - Entertainment & Media
  - Financial Services
  - External-Use Software
  - Regulated Operations
  - Transfers & Servicing



What type of intangible or groups of intangibles are most relevant to you?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Research & Development

The term *research and development* is defined in the Master Glossary as follows:

Research	Planned search or critical investigation aimed at discovery of new knowledge with the hope that such knowledge will be useful in development a new product or service or a new process or technique or in bringing about a significant improvement to an existing product or process.
Development	The translation of research findings or other knowledge into a plan or design for a new product or process or a significant improvement to an existing product or process whether intended for sale or use. It includes the conceptual formulation, design, and testing of product alternatives, construction of prototypes, and operation of pilot plants.

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Examples of Current GAAP

Intangible	Business Combination	Asset Acquisition	Internally Developed
Trademark / tradename	Recognized as an intangible asset if it meets the contractual-legal criterion or the separability criterion.	Recognized as an intangible asset.	Expensed as incurred.
In-process research and development (IPR&D)	Recognized as an intangible asset.	If there is no alternative future use, costs are expensed as incurred. If there is an alternative future use, recognized as an indefinite-lived intangible asset.	Expensed as incurred.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Examples of Current GAAP (continued)

Intangible	Business Combination	Asset Acquisition	Internally Developed
Assembled workforce	Not recognized as an intangible asset, subsumed into goodwill.	Generally recognized as an intangible asset.	Expensed as incurred.
External-use software	Recognized as an intangible asset if it meets the contractual-legal criterion or the separability criterion.	Generally recognized as an intangible asset (IPR&D if not completed).	All development costs incurred to establish the technological feasibility of external-use software are R&D costs that are expensed as incurred. Costs incurred after establishing technological feasibility are recognized as an intangible asset.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Discussion Questions

1. (Investors) Does the different treatment for intangibles (a) acquired as part of a business combination, (b) acquired in an asset acquisition, or (c) that are internally developed affect your analysis?

2. (Investors) Do the differences in the financial reporting results present challenges in evaluating organic growth versus inorganic growth?

3. (All) Should the Board consider aligning the recognition guidance for intangibles (a) acquired as part of a business combination, (b) acquired in an asset acquisition, or (c) that are internally generated, or develop new recognition criteria that can be applied to obtain consistent outcomes regardless of how an intangible is developed or acquired?

R&D:

4. (All) Do the glossary terms discussed in the slides appropriately capture research and development (R&D) activities that should be expensed as incurred and considered for disclosure purposes? If not, how could those definitions be updated?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Discussion Questions (continued)

5. (Investors) Do current disclosures related to intangibles and R&D costs provide you with decision-useful information?
   - If not, what information currently provided is not decision useful or what additional information would be decision useful?
6. (All) Is there a pervasive need to improve GAAP related to the accounting for and disclosure of intangibles (that is, is there a case for change)?
7. (All) If the Board were to pursue a project on intangibles, how should the Board address the topic?
   - Should it be broad or narrow for a specific intangible(s)?
   - What potential solution(s) should the Board explore?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Next Steps



Comment period ends May 30, 2025



Board to consider comment letter feedback

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Topic 2: Post-Implementation Review on Leases

11:20 a.m.–12:00 p.m.

Chris Roberge	Senior Project Manager
Lauren Mottley	Supervising Project Manager
Jenifer Wyss	Supervising Project Manager

FASB FINANCIAL ACCOUNTING STANDARDS BOARD® GASB GOVERNMENTAL ACCOUNTING STANDARDS BOARD® FAF FINANCIAL ACCOUNTING FOUNDATION®

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

History of the Project

2006

July — The FASB and IASB initiated a joint project to improve financial reporting of leasing activities to meet the needs of investors.

This was largely in response to the U.S. Securities and Exchange Commission's (SEC) recommendation in the 2005 report on the implications of off-balance sheet activities.*

2009

March — The Boards issued a Discussion Paper with preliminary views on lessee accounting. It proposed a right-of-use lessee accounting model for all leases.

The Boards received 302 comment letters that were generally supportive, but stakeholders had broad concerns about implementation issues and complexity.

2010

August — The Boards issued the 2010 Exposure Draft which further developed the right-of-use accounting model for lessees and developed a fundamentally new model for lessors.

The Boards received 786 comment letters with general support for the lessee model, broad concerns about the lessor model, and concerns about cost and complexity of implementing the proposals.

2013

May — The Boards issued the 2013 Exposure Draft which proposed two accounting models for both lessees and lessors. Both distinguished between different lease types based on the level of a lessee's expected economic consumption.

The Boards received 657 comment letters with concerns about the proposed lessor and lessee accounting models.

2016

February — FASB issued Topic 842. The Update largely retained the Topic 840 dual classification model for lessees and required recognition of all leases on the balance sheet. The Update also substantively retained the lessor accounting model from legacy GAAP.

*The report was: *2005 Report and Recommendations Pursuant to Section 401(c) of the Sarbanes-Oxley Act of 2002 On Arrangements with Off-Balance Sheet Implications, Special Purpose Entities, and Transparency of Filings by Issuers.*

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Expected Benefits and Costs

Expected Benefits (Users)	Expected Costs (Preparers)
• Improve users' understanding about lessees' obligations under lease contracts • Provide a more faithful representation of the rights and obligations that arise from leases • Improve understanding and comparability of lessees' financial commitments • Clarify the definition of a lease to address practice issues • Align the lessor accounting in certain areas and the accounting for sale and leaseback transactions guidance with Topic 606, Revenue from Contracts with Customers	• Initial costs to educate employees about how to apply the new requirements and users about effects of the accounting changes • Costs related to identifying all leases and implementing more robust processes and controls • Ongoing costs were not expected to be significantly higher than applying previous GAAP

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Overall Discussion Questions

1. Do you have any overall observations about whether the objective of the standard was met or about the benefits or costs (including initial costs and recurring costs) of applying the leases standard?

2. What are your observations on the history of the FASB's leases project, including the standard-setting activities and joint deliberations with the IASB?

3. For lessee accounting:
   a) For investors, how did recognizing operating leases on the balance sheet change the benefits and costs of analyzing the effects of leases?
   b) For preparers and practitioners, how did recognizing operating leases on the balance sheet change the benefits and costs of applying the lease accounting guidance?

4. For preparers/practitioners, do you have additional observations to share on ongoing application costs to comply with Topic 842? If so, please describe the nature of those costs (for example, systems, processes, and applying certain areas of guidance).

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Lunch

1 hour

Topic 3: Debt and Equity

1:00–1:30 p.m.

Mary Mazzella	Assistant Director
Aarika Friend	Senior Project Manager
Kitrina Pople	Practice Fellow

FASB FINANCIAL ACCOUNTING STANDARDS BOARD® GASB GOVERNMENTAL ACCOUNTING STANDARDS BOARD® FAF FINANCIAL ACCOUNTING FOUNDATION®

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Stakeholder Feedback

- The liabilities and equity guidance is complex and costly to apply.
- This guidance is a frequent source of financial statement restatements:
  - Difficult to understand and operationalize
  - Often results in accounting conclusions that appear to be more form over substance.

The FASB has historically found it challenging to balance the request to reduce complexity in the guidance with stakeholders' desire to achieve certain financial reporting outcomes, such as liability or equity classification.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Derivative Scope Exception

- An entity does not consider* contracts issued or held by the reporting entity to be derivative instruments (commonly referred to as the derivative scope exception) if the following criteria are met:

Indexed to an entity's own stock

+

Classified in stockholders' equity in its statement of financial position

*Notwithstanding instruments subject to other criteria within the derivatives scope exception guidance

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Consequences of the Derivative Scope Exception

	Freestanding Financial Instruments	Embedded Features
Does not meet the derivative scope exception	• Asset or liability classification • Potentially accounted for as a derivative • Remeasured every period at fair value through net income	• Bifurcation from the host contract and liability classification as a derivative • Remeasured every period at fair value through net income
Meets the derivative scope exception	• Equity classification • No remeasurement	• No bifurcation from the host contract (either as liability or equity) • No separate accounting

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Contracts in Entity's Own Equity: Current Indexation Guidance

Step 1: Evaluate contingent exercise provisions, if any

- Precluded from being considered indexed to an entity's own stock if based on:
  - Observable market other than the market for the issuer's stock
  - Observable index other than by reference to issuer's own operations

Step 2: Evaluate settlement provisions

- Considered indexed to an entity's own shares if "fixed-for-fixed"
- In practice, provisions that adjust a settlement amount would not preclude the contract from being indexed to an entity's own shares if the variable is an **input to the fair value of a forward or option on equity shares**

Section 815-40-55 includes 20 distinct examples that entities leverage when determining whether a contract is indexed to an entity's own stock.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Example 1: Contract Indexed

Example	Step 1: Exercise Contingency	Step 2: Settlement Amount	Conclusion
Entity A issues warrants that permit the holder to buy 100 shares of its common stock for $10 per share. The warrants have 10-year terms; however, they only become exercisable after Entity A accumulates $100 million in sales to third parties.	The exercise contingency is an observable index - based on Entity A's sales.	The settlement amount equals the difference between the fair value of a fixed number of the entity's shares (100 shares) and a fixed strike price ($10 per share).	Therefore, the warrants meet the indexation criterion and are not precluded from equity classification. The entity must evaluate the equity classification criterion to determine classification.

Included as Example 3 in Subtopic 815-40 in paragraph 815-40-55-27

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Example 2: Contract Not Indexed

Example	Step 1: Exercise Contingency	Step 2: Settlement Amount	Conclusion
Entity A issues warrants that permit the holder to buy 100 shares of its common stock for an initial price of $10 per share. The warrants have 10-year terms and are exercisable at any time. However, the terms of the warrants specify that the strike price is reduced by $0.50 after any year in which Entity A does not achieve revenues of at least $100 million.	The instrument does not contain an exercise contingency.	The settlement amount would not equal the difference between the fair value of a fixed number of the entity's equity shares (100 shares) and a fixed strike price.	Therefore, the warrants do not meet the indexation criterion and are precluded from equity classification. The warrants are required to be asset or liability classified.

Included as Example 7 in Subtopic 815-40 in paragraph 815-40-55-31

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Contracts in Entity's Own Equity: Current Equity Classification Guidance

HOW Is the Contract Settled?

- Does the contract require net-cash settlement?
- Does the contract require settlement in shares?
- Could the contract be settled in cash or shares?

WHO Has the Choice to Settle?

- Does the counterparty have a choice of net-cash settlement?
- Does the issuer have a choice of net-cash settlement?

Are **ALL** Other Equity Classification Requirements Met?

- Does the contract have an explicit share limit?
- Does entity have sufficient and authorized shares to settle?
- Does the contract include either:
  - Required cash payment if the entity fails to file with SEC?
  - Cash-settled top-off or make whole provision?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Example 3: Equity Classification

Example	Analysis	Conclusion
Entity A issues warrants that require net share settlement. However, if either Entity A or the counterparty declares bankruptcy, the shares will be settled in cash. The chance of either party declaring bankruptcy is remote.	While the warrants could be settled in shares, there is remote possibility for cash settlement in the event of bankruptcy. Because current guidance does not consider probability of an event occurring for classification, net cash settlement must be assumed.	Therefore, warrants are precluded from being classified as equity; Entity A evaluates if the contract is a derivative. If the contract is a derivative, apply the guidance in Subtopic 815-10 and account for the contract as a derivative. If the contract is not a derivative, classify the contract as an asset or liability.

This example was created for this presentation based on the guidance in Section 815-40-25

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Discussion Questions

1. What challenges do you encounter in applying the liabilities and equity guidance today?
   a) Are there challenges in interpreting the “fixed-for-fixed” guidance (in Section 815-40-15), such as in interpreting if a variable affecting settlement amount “is an **input to the fair value of a forward or option on equity shares**”?
   b) Are there challenges in applying the equity classification guidance (in Section 815-40-25)?
2. Would you be supportive of changes to the contracts in an entity’s own equity guidance (in Subtopic 815-40)?
   a) Would you still be supportive of changes to the guidance if they significantly changed current financial reporting outcomes?
   b) Would you support accounting for more contracts as equity?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Topic 4: Definition of a Public Business Entity

1:30–1:50 p.m.

Lauren Mottley Supervising Project Manager

FASB FINANCIAL ACCOUNTING STANDARDS BOARD® GASB GOVERNMENTAL ACCOUNTING STANDARDS BOARD® FAF FINANCIAL ACCOUNTING FOUNDATION®

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Overall Discussion Questions

1. Should the FASB consider amending the Master Glossary term public business entity (PBE)? If the FASB were to reconsider the Master Glossary term, which type of entities should be included or excluded and why?

2. Should the Board consider a project that seeks to reduce the number of definitions of a public entity and a nonpublic entity throughout GAAP? If so, what priority should the Board place on such a project?

3. If the Board were to pursue a project to reduce the number of definitions of a public entity and a nonpublic entity, should the Board consider replacing the various definitions of a public entity (and related terms) with the PBE definition? How should the Board consider the way the definitions are used (for example, definitions that establish scope versus definitions that relate to measurement and disclosure requirements)?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Topic 5: Agenda Consultation

1:50–2:30 p.m.

Alicia Manders	Assistant Director
Aarika Friend	Senior Project Manager
Tiffany Wyszkowski	Project Manager

FASB FINANCIAL ACCOUNTING STANDARDS BOARD® GASB GOVERNMENTAL ACCOUNTING STANDARDS BOARD® FAF FINANCIAL ACCOUNTING FOUNDATION®

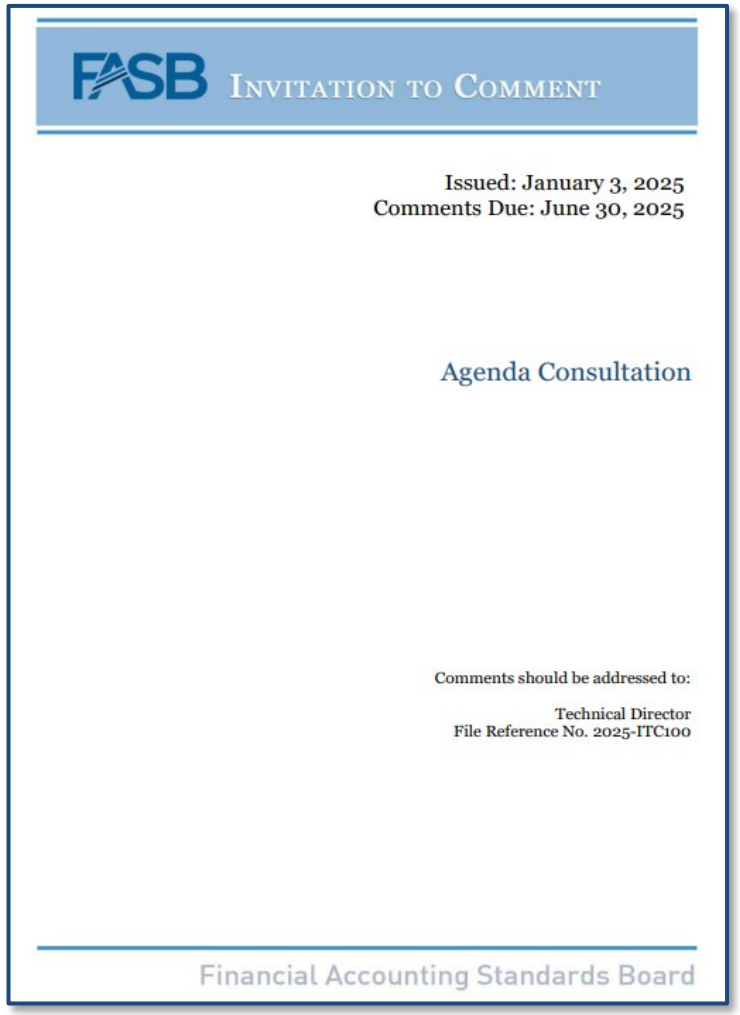
Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Background

In June 2022, the FASB issued the 2021 *Agenda Consultation Report*, which summarized the robust feedback obtained during our 2021 agenda consultation project and how that feedback has influenced the Board's technical and research agendas and standard-setting process.

Since then, there has been significant progress on the top priorities identified by stakeholders.

In January 2025, the FASB issued Invitation to Comment (ITC), *Agenda Consultation*, to understand the next priority areas that the Board should address.


FASB Invitation to Comment

Issued: January 3, 2025
Comments Due: June 30, 2025

Agenda Consultation

Comments should be addressed to:

Technical Director
File Reference No. 2025-ITC100

Financial Accounting Standards Board

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Themes in the ITC

- Stakeholders commended the Board on its significant progress on the priorities identified in the 2021 Agenda Consultation and expressed their appreciation that the Board listened to stakeholders and took timely action on the identified priorities.
- Because of this significant progress, most stakeholders, including many investors, said that there is not a case to make major changes to GAAP at this time.
  - This feedback also was received from investors that requested the Board make significant improvements to GAAP as part of the 2021 Agenda Consultation process.
- Many of the topics that were suggested for standard-setting efforts focus on targeted improvements to GAAP with the objective to either:
  - Reduce unnecessary complexity
  - Enhance the decision usefulness of information provided to investors.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Disclosure Related Topics - Overview

- The FASB has recently issued standards that enhance the disclosures for various areas, including revenue, leases, segments, income taxes, and income statement expenses.
- Investors and other stakeholders, in both the public and private company sectors, continue to request additional quantitative and/or qualitative financial reporting information about a range of areas. A list of potential disclosures are included in the ITC.
- Other stakeholders have indicated that certain disclosures have become outdated and questioned whether they continue to be relevant and/or cost beneficial.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Disclosure Related Topics – ITC Questions[1]

- **Question 44:** Should the FASB consider any additional disclosures? If so, how would that information better inform investment decisions? If these or similar disclosures are currently required outside of the financial statements, why should or shouldn't they be included in the financial statements? Are there other areas that need additional disclosures? Please explain.
- **Question 45:** Are there current disclosure requirements that do not provide meaningful information about an entity? If yes, please explain which disclosures are not decision useful and whether those disclosures should be removed or how they should be improved.

[1] Questions are from the 2025 Agenda Consultation ITC that is open for comment until June 30, 2025.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Cash Related Topics - Overview

- Definition of Cash Equivalents
  - The Master Glossary defines the term *cash equivalents* as short-term, highly liquid investments that are (1) readily convertible to known amounts of cash and (2) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates.
  - Stakeholders suggested expanding the definition to include other assets that are highly liquid but do not have a maturity date.
- Statement of Cash Flows
  - The statement of cash flows explains changes during the period in the total of cash, cash equivalents, and restricted cash. Typically, this is done using the direct and indirect methods.
  - Stakeholders have expressed a wide variety of views about potential improvements to the statement of cash flows.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Cash Related Topics – ITC Questions

- **Question 29:** Should the FASB reconsider the definition of cash equivalents and consider including other assets that are easily liquidated? If so, what types of assets should be added to the definition of cash equivalents? Please explain.
- **Question 52:** Should the FASB pursue a project on the statement of cash flows? If yes, which improvements, if any, are most important? Should the FASB leverage the current guidance in Topic 230, Statement of Cash Flows? If yes, would it be preferable to retain the direct method, the indirect method, or both? Should this potential project be a broad project applicable to all entities that provide a statement of cash flows or limited to certain entities or industries? Please explain.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Consolidation Related Topics - Overview

- Definition of Common Control
  - The term *common control* is not defined in the Master Glossary; however, examples are provided in Subtopic 805-50, Business Combinations—Related Issues.
  - Stakeholders stated that determining when separate entities are under common control can affect financial statements because some areas of GAAP (such as business combinations accounting) exclude, or require specific accounting for, transactions between entities that are under common control.
- Interaction of Consolidation Guidance and Other Transactions
  - The consolidation guidance interacts the accounting for asset acquisitions, recognition and measurement of acquisitions of variable interest entities, derecognition of nonfinancial assets, and the accounting for a sale and leaseback transaction.
  - Stakeholders noted that these interactions result in unnecessary complexity and diversity in practice.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Consolidation Related Topics – ITC Questions

- **Question 10**: Should the FASB consider defining the term *common control*? If yes, how should the term be defined and what would be the anticipated effect? Please explain.
- **Question 11**: Should the FASB prioritize a potential project to improve and align the guidance discussed on the previous slide? If yes, what should be included in the scope and what alternatives should be considered? Please explain.

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Overall Questions

- Are there other topics that haven't been discussed today that the Board should consider prioritizing?
- Which financial accounting and reporting topics **should be a top priority** for the Board? This may include topics listed in the ITC or other topics beyond those.
- Are there financial accounting and reporting topics listed in the ITC that the Board **should not address** as part of its future standard-setting efforts?

Copyright 2025 by Financial Accounting Foundation, Norwalk CT. For non-commercial, educational/academic purposes only.

Meeting Adjourned

Thank you!

POST-IMPLEMENTATION REVIEW – LEASES
PUBLIC MARKETS ADVISORY COMMITTEE (PMAC)
MAY 2025

Session Background and Objective

The Post-Implementation Review (PIR) process is part of the Financial Accounting Foundation's (FAF) Board of Trustees' oversight responsibilities of the FASB. The PIR process assists the Trustees in evaluating the effectiveness of the standard-setting process for the FASB.

The PIR process is an evaluation of whether a standard is achieving its objective by providing investors and other allocators of capital (herein referred to as "investors") with relevant information in ways that justify the costs of providing it. It is an important quality control mechanism built into FASB's standard-setting process that begins after the issuance of select standards. During the PIR process, the FASB solicits and considers diverse stakeholder input and other research to evaluate whether a standard is accomplishing its stated purpose, to evaluate the standard's implementation and continuing compliance costs and related benefits, and to provide feedback to improve the standard-setting process.

The purpose of this session is to provide Committee members with an overview of the history of the leases project that led to the issuance of Accounting Standards Update No. 2016-02—*Leases (Topic 842)*, and significant PIR activities performed to date. This includes information about why the FASB launched a project on lease accounting in 2006 and summarizes the process that the FASB undertook in developing the leases standard and the stakeholder feedback received—including the significant input received on the various proposals for the recognition and measurement of lease contracts by entities that obtain or provide the right to use an underlying asset, referred to as lessees and lessors, respectively. Committee members have previously discussed the leases PIR and those discussions are summarized in Section 3.

In this session, PMAC members will be asked to provide insights and observations on the Board's activities during the leases project and any incremental observations about the benefits and costs of the leases standard.

Structure of these Materials

These materials are organized as follows:

- Section 1: History of the Leases Project
- Section 2: Expected Benefits and Expected Costs
- Section 3: Significant PIR Activities

Discussion questions are included on page 13.

Section 1: History of the Leases Project

The legacy accounting for leases in GAAP and International Financial Reporting Standards (IFRS) did not require a lessee to recognize the assets and liabilities arising from operating leases on its balance sheet, but it did require that recognition for capital leases (referred to in Topic 842 as finance leases). The FASB and the International Accounting Standards Board (IASB) (collectively, the "Boards") initiated a joint project in July 2006. The objective of that joint project was to improve the financial reporting of leasing activities in light of criticism that the legacy accounting for leases failed to meet the needs of investors. In particular, the U.S. Securities and Exchange Commission (SEC) in its 2005 *Report and Recommendations Pursuant to Section 401(c) of the Sarbanes-Oxley Act of 2002 On Arrangements with Off-Balance Sheet Implications, Special Purpose Entities, and Transparency of Filings by Issuers*, which was issued to the U.S. Congress, recommended that the accounting guidance for leases be reconsidered. The report observed that "[T]he current accounting for leases takes an "all or nothing" approach to recognizing leases on the balance sheet. This results in a clustering of lease arrangements such that their terms approach, but do not cross, the "bright lines" in the accounting guidance that would require a liability to be recognized." As a consequence, arrangements with similar economic outcomes are accounted for very differently.

In addition, feedback, including findings from academic studies, indicated that because leases classified as operating leases were not recognized on a lessee's balance sheet, most investors adjusted a lessee's financial statements to capitalize operating leases. In doing so, some tried to estimate the present value of future lease payments using disclosures of future minimum rental payments (limited to contractually required "fixed" payments). Many other investors used techniques—such as multiplying the lessee's annual lease expense (included contractually required fixed and variable payments) by a factor (often in the range of six to eight) to approximate the fair value of the lessee's obligations. This adjustment was used, for example, to assess total leverage and the capital employed in operations. Other investors were unable to make adjustments and

relied on other data sources, such as data aggregators, to make investing decisions.

When the Boards added the leases project to their agendas, they agreed that the project would consider both lessee accounting and lessor accounting. In 2006, the Boards set up their International Working Group on lease accounting (hereinafter referred to as the Working Group) that included investors, preparers, and auditors of both lessees' and lessors' financial statements. The Working Group provided comments on the early proposals to improve lease accounting (in February 2007) and its members contributed informally to the development of lease accounting models during 2007 and 2008.

In April 2008, the Boards announced their intention to produce a revised standard for lessees by mid-2011 and, in July 2008, the Boards tentatively decided to defer consideration of lessor accounting and concentrate on developing an improved lessee accounting model. The Boards further determined that the timing of any new lessor standard was to be decided after publishing the joint Discussion Paper: *Leases: Preliminary Views*, in March 2009.

2009 Discussion Paper

The Discussion Paper set out the Boards' preliminary views on lessee accounting, proposing a right-of-use accounting model. The Discussion Paper would have required lessees to account for all lease contracts as the acquisition of a right to use the leased item for the lease term. A lessee would have accounted for all leases by recognizing a lease liability and a related right-of-use asset, measured as the present value of the lease payments (fixed and variable). In addition, the lessee also would have amortized the right-of-use asset typically over the lease term and recognized interest on the lease liability, consistent with the accounting for capital leases under legacy GAAP. The Discussion Paper did not discuss lessor accounting in any detail.

The Boards received 302 comment letters on the Discussion Paper. Feedback was generally supportive of the right-of-use model (recognition of assets and liabilities arising from a lease) for lessees. In addition, the following broad concerns were raised by respondents:

1. The existing guidance is well understood by both preparers and investors, and the Boards should address implementation issues relating to the existing model rather than abandon a model that is not fundamentally flawed.
2. A right-of-use model would lead to recognizing assets and liabilities for all executory contracts, including purchase orders and long-term sales and supply agreements, which would inappropriately gross up a lessee's balance sheet.
3. The right-of-use model is too complex, and its benefits would not outweigh the costs.

In addition, many respondents suggested that the Boards develop a consistent accounting model for lessees and lessors.

2010 Exposure Draft

After considering the 2009 Discussion Paper feedback, as well as input obtained from the Working Group and from others who were interested in the financial reporting of leases, the Boards published a joint Exposure Draft, *Leases* (2010 Exposure Draft), in August 2010.

The proposed guidance in the 2010 Exposure Draft further developed the right-of-use accounting model for lessees in the Discussion Paper.

The 2010 Exposure Draft also proposed that lessors change their accounting to a dual model in which a lessor would recognize a lease receivable for all leases and depending on the lessor's exposure to the risks and benefits of the underlying asset, lessors would either (a) derecognize a portion of the underlying asset or (b) continue to recognize the underlying asset and recognize a performance obligation liability. The Boards decided to include lessor accounting in the 2010 Exposure Draft in response to respondents' comments on the Discussion Paper and because the Boards saw merit in developing proposals on lessor accounting and the recognition of revenue at the same time.

The Boards received 786 comment letters in response to the 2010 Exposure Draft from entities and organizations from a range of industries, including both public business entities and private companies.

The Boards also consulted extensively on the proposals in the 2010 Exposure Draft. Roundtable discussions were held in Hong Kong, the United Kingdom, and the U.S. Workshops were organized in Australia, Brazil, Canada, Japan, South Korea, the United Kingdom, and the U.S. Members of the Boards also participated in conferences, Working Group meetings, discussion forums, and one-on-one discussions that were held across all major geographical regions. In 2011 and 2012, while redeliberating the proposals in the 2010 Exposure Draft, the Boards conducted targeted outreach on specific issues with more than 100 organizations. The targeted outreach meetings involved Working Group members, representatives from accounting firms, local standard setters from other national and regional jurisdictions, investors, and preparers—particularly those from industries most affected by the lease accounting proposals.

The main feedback received on the 2010 Exposure Draft was as follows:

1. There was general support for the recognition of assets and liabilities arising from a lease by lessees, which was consistent with comments received on the Discussion Paper.

2. Some respondents said that leases are a source of financing for a lessee and should be accounted for accordingly. Consequently, they supported the proposed right-of-use model in which a lessee would recognize separately amortization of the right-of-use asset and interest on the lease liability.
3. Others disagreed with the 2010 Exposure Draft stating that the approach would not properly reflect the economics of all lease transactions. In particular, some respondents referred to shorter term property leases as examples of leases that, in their view, were not financing transactions from either the lessee's or the lessor's perspective.
4. Despite calls for consistency between lessor and lessee accounting, many respondents disagreed with the lessor accounting proposals. Some asserted that there are not significant issues with the legacy lessor accounting requirements, that they work well in practice, and, therefore, should be retained.
5. Almost all respondents were concerned about the costs and complexity of the proposals. In particular, the respondents raised concerns about the proposed measurement of the lessee's lease liability and the lessor's lease receivable, which would have required an entity to estimate all variable lease payments to be made during the noncancellable period of a lease and during any optional extension periods that the entity considered more likely than not to occur.
6. Many respondents also were concerned about the breadth of the proposed scope, indicating that the proposed definition of a lease had the potential to capture some arrangements that they considered to be service contracts rather than leases.

2013 Exposure Draft

The Boards considered all of the feedback received during the redeliberations of the proposals in the 2010 Exposure Draft and observed that it would not be possible to reflect the views of all stakeholders because stakeholders did not have a uniform view of the economics of leases. The Boards decided to expose for comment an alternative model that was intended to be responsive to those stakeholders who said that the economics vary among different types of leases. Consequently, in May 2013 the Boards published a second joint Exposure Draft, *Leases* (2013 Exposure Draft).

The 2013 Exposure Draft proposed two approaches to the recognition and measurement of expenses arising from a lease (along with still proposing that lessees be required to recognize a lease liability and right-of-use asset for all leases). The lessee model distinguished between different types of leases based on the level of the lessee's consumption of the economic benefits embedded in the underlying asset. That model was based on the view that the recognition of a single lease expense in a lessee's income

statement would provide better information about leases for which the lessee (a) pays only for the use of the underlying asset and (b) is expected to consume only an insignificant amount of the economic benefits embedded in the underlying asset itself. A lessee would have accounted for those leases for which it consumes *more than* an insignificant amount of the benefits embedded in the underlying asset by amortizing the right-of-use asset typically over the lease term and recognizing interest on the lease liability, consistent with the accounting for capital leases under legacy GAAP. Unlike the 2010 Exposure Draft, the measurement of the lease liability and right-of-use asset would have excluded variable lease payments (except for those based on an index or rate).

The 2013 Exposure Draft also proposed a lessor model that distinguished between different types of leases based on the lessee's level of consumption of the economic benefits embedded in the underlying asset. For leases in which the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset, the lessor would have been required to recognize its residual interest in the underlying asset separately from its right to receive lease payments (that is, its lease receivable). A lessor would account for all other leases in a similar manner to operating lease accounting in Topic 840 (that is, the lessor would (a) continue to recognize the underlying asset and (b) recognize lease income over the lease term typically on a straight-line basis). Consistent with the lessee model proposed in the 2013 Exposure Draft, the lease payments used for measuring the lease receivable or the total lease cost to be recognized over the lease term would have excluded most variable payments.

The Boards received 657 comment letters in response to the 2013 Exposure Draft from stakeholders from a range of industries. In addition, the Boards consulted extensively on the proposals in the 2013 Exposure Draft, including:

1. Consultations with more than 270 investors based in the U.S., the United Kingdom, Sweden, Switzerland, Belgium, the Netherlands, France, Australia, New Zealand, Hong Kong, Japan, and Canada.
2. Meetings with individual preparers from various industries including consumer goods, retail, aviation, oil and gas, telecommunications, and automotive. These meetings were held in Germany, France, Spain, the United States, the United Kingdom, Japan, and Brazil and included detailed discussions about the costs of implementation for those companies.
3. Roundtables held in London, Norwalk, Los Angeles, Singapore, and Brazil. These were attended by approximately 100 stakeholder representatives.
4. Meetings with all of the FASB's advisory groups—the Financial Accounting Standard Advisory Council (FASAC), the Investor Advisory Committee (IAC), the Not-for-Profit Advisory Committee (NAC), the Small Business Advisory Committee (SBAC), and the

Private Company Council (PCC).

5. Outreach meetings with various other individual preparers and groups of preparers, standard setters, and regulators. These meetings included presentations during accounting conferences, keynote presentations at industry forums, and meetings with individual organizations or groups.
6. Project webcasts that were attended by over 2,000 participants.

The main feedback received on the 2013 Exposure Draft was as follows:

1. Many stakeholders supported the recognition of a right-of-use asset and a lease liability by a lessee for all leases of more than 12 months (similar to feedback received on the 2010 Exposure Draft). Those stakeholders included most investors consulted.
2. Many stakeholders disagreed with the proposed lessee accounting model. Some of those stakeholders (a) said that the lessee accounting model in Topic 840 did not need to be changed or (b) supported expanding the lessee disclosure requirements instead of changing the recognition and measurement requirements. Other stakeholders disagreed with one or more specific lessee aspects in the 2013 Exposure Draft.
3. Many stakeholders said that there were significant improvements to the measurement proposals in the 2013 Exposure Draft, as compared with the 2010 Exposure Draft, especially relating to simplifications of variable lease payments and payments under renewal options and purchase options. Nonetheless, the majority of stakeholders still had concerns about the costs and complexity of the proposals in the 2013 Exposure Draft.
4. The majority of stakeholders disagreed with the proposed lessor accounting model because, in their view, it was not an improvement to the financial reporting for those transactions. Most of those stakeholders said that lessor accounting should not be changed substantially.

Topic 842 (Issued February 2016)

After considering all of the feedback received throughout the leases project, the Board decided that a lessee should be required to recognize right-of-use assets and lease liabilities for all leases (except for short-term leases). However, the Board sought to address many of the stakeholders' concerns about the costs and complexity of the lessee and lessor proposals (in the 2010 and 2013 Exposure Drafts) when finalizing Topic 842. Specifically, the Board:

1. Adopted a lessee accounting model that distinguishes between two lease types (finance leases and operating leases) using a classification approach that is substantially similar to legacy GAAP for distinguishing between operating leases and capital leases. The Board expected that this decision, along with other simplifications,

would result in many lessees using their existing systems and processes to apply Topic 842. Conversely, the IASB decided to require a single lessee accounting model in which a lessee accounts for all leases as finance leases, with an exemption for leases of "small assets" that are considered underlying assets of approximately $5,000 or less.

2. Substantively retained the lessor accounting model from legacy GAAP, including recognizing and distinguishing between sales-type leases, direct financing leases, and operating leases. In addition, certain of the lessor accounting requirements were aligned with revenue recognition (Topic 606).
3. Provided more robust guidance for identifying a lease, including determining whether a customer has the right to control the use of an underlying asset.
4. Allowed a lessee to not recognize assets and liabilities for short-term leases (leases with a lease term of 12 months or less). The IASB provided a similar exception.
5. Permitted a lessee to apply the leases standard at a portfolio level for leases with similar characteristics.
6. Largely aligned the requirements for determining the lease term, including the consideration of renewal, termination, and purchase options, with legacy GAAP.
7. Simplified the measurement of the lease liability by excluding variable payments other than those that depend on an index or a rate (initially measured using the index or rate at the commencement date).
8. Simplified lessee expense recognition and the process for subsequently measuring the right-of-use asset in an operating lease as compared with the proposed guidance in the Exposure Drafts.
9. Provided a practical expedient whereby a lessee may, as an accounting policy election by class of underlying asset, choose not to separate nonlease components from lease components and instead to account for each separate lease component and the nonlease components associated with that lease component as a single lease component.
10. Clarified the application of the sale guidance in revenue recognition (Topic 606) to sale and leaseback transactions and provided more robust guidance for determining when a lessee controls the underlying asset before the commencement date.

Section 2: Expected Benefits and Expected Costs

The following summarizes how the FASB considered the expected benefits and expected costs of the leases standard.

Expected Benefits for Users of Financial Statements

The basis for conclusions provides additional details about some of the expected benefits of the leases standard. An excerpt of paragraph BC8 states:

> BC8. The Board developed Topic 842 principally to improve users' understanding about lessees' obligations under lease contracts. Topic 842 provides transparent and economically neutral information about the assets and liabilities that arise from leases, which is in contrast to the incomplete information provided about leases in previous GAAP that did not recognize the assets and liabilities that arise from most leases. Topic 842 also provides improved financial information about a lessor's leasing activities. As such, Topic 842 results in more useful information being provided to users of financial statements. The requirements in Topic 842 will:
>
> a. Result in a more faithful representation of the rights and obligations arising from leases by requiring lessees to recognize the lease assets and lease liabilities that arise from leases in the statement of financial position and to disclose qualitative and quantitative information about lease transactions, such as information about variable lease payments and options to renew and terminate leases
> b. Improve understanding and comparability of lessees' financial commitments regardless of the manner they choose to finance the assets used in their businesses
> c. Clarify the definition of a lease to address practice issues that were raised about the previous definition of a lease and to align the concept of control, as it is used in the definition of a lease, more closely with the control principle in both Topic 606, Revenue from Contracts with Customers, and Topic 810, Consolidation
> d. More closely align the lessor accounting and sale and leaseback transactions guidance to the comparable guidance in Topic 606 and Topic 610, Other Income
> e. Provide users with additional information about lessors' leasing activities and lessors' exposure to credit and asset risk as a result of leasing
> f. Result in fewer opportunities for entities to structure leasing transactions to achieve a particular accounting outcome on the statement of financial position.

Expected Costs for Preparers

The basis for conclusions in the leases standard provides additional details about the anticipated costs of the leases standard. Paragraph BC10 states:

> BC10. The Board understands that certain reporting entities will incur additional costs as a result of Topic 842. For example, entities will, in general, incur initial costs to educate employees about how to apply the new requirements, as well as how to explain the effects of the changes in

accounting for leases on the entity's financial statements to users of financial statements. In addition, many entities will need to undertake activities to ensure they have appropriately identified all of their leases and implement more robust processes and controls to ensure that they capture all material leasing activity going forward. However, the Board noted that once these implementation activities are completed, the ongoing costs for most entities of providing the information in Topic 842 are unlikely to be significantly higher than the costs of complying with the accounting model in previous GAAP. In previous GAAP, entities were similarly required to identify leases, evaluate each lease to determine the applicable accounting model to apply (capital or operating), and to subsequently account for each lease, including meeting the ongoing disclosure requirements about cash flows from leases. Topic 842 will not substantially change this level of effort, and the Board concluded that, based on substantial outreach with preparers of financial statements, many entities will be able to apply the requirements in Topic 842 using similar systems and processes to what they used in previous GAAP to meet those reporting and disclosure requirements

Compliance Costs for Preparers

Paragraph BC11 and an excerpt of BC14 describe some of the anticipated compliance costs for preparers of financial statements:

> BC11. The Board considered an entity's initial costs to comply with the requirements in Topic 842, and this affected its conclusions both on the lessee and lessor accounting requirements and on transition to the new requirements. Regarding the lessee and lessor accounting requirements, as outlined in paragraph BC10, the Board concluded that a substantial portion of all entities will be able to apply the new requirements using systems and processes similar to those used in previous GAAP. The Board decided that a modified retrospective approach for transition, as opposed to a full retrospective approach, provides an appropriate balance between minimizing costs of transition and providing users of financial statements with comparable financial information. The practical expedients related to transition, if elected, should further significantly reduce the costs associated with transitioning to the new requirements.
>
> BC14. The Board further considered the concern that the additional lease liabilities recognized as a result of adopting Topic 842 will cause some entities to violate debt covenants or may affect some entities' access to credit because of the potential effect on the entity's GAAP-reported assets and liabilities. Regarding access to credit, outreach has demonstrated that the vast majority of users, including private company users, presently adjust an entity's financial statements for operating lease obligations that are not recognized in the statement of financial position under previous GAAP and, in doing so, often estimate amounts significantly in excess of what will be recognized under Topic 842.

Expected Costs of Analysis for Users of Financial Statements

Paragraph BC13 describes the anticipated costs of analysis for investors:

> BC13. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new requirements are borne primarily by the preparers' current investors. The Board's assessment of the costs and benefits likely to result from issuing new requirements is unavoidably more qualitative than quantitative because there is not an identified method to objectively quantify the costs to implement new guidance or to quantify the value of expected, improved information in financial statements.

Section 3: Significant PIR Activities

Since the issuance of the leases standard, the FASB and its staff have been assisting stakeholders with the implementation and ongoing application of the leases standard. The Board did not create a transition resource group to analyze and discuss implementation issues that arise because many of the concepts in the leases standard are similar to legacy GAAP.[1] The FASB has been consistently working with stakeholders to understand implementation challenges, address their questions, and consider the need for subsequent amendments. The FASB staff has answered over 400 technical inquiries and has made certain modifications and clarifications to the leases standard to reduce the expected costs of applying that guidance.

For example, after learning from stakeholders about unanticipated costs and complexities of recognizing operating leases on the balance sheet using existing or new systems, the Board permitted entities to apply the leases standard at the adoption date as opposed to the earliest comparative period presented. That transition relief was widely used by most entities in their adoption of the leases standard. The FASB also has made several amendments to the lessor requirements to preserve the same financial reporting outcomes realized under legacy guidance.

During 2020[2] and after public entities implemented the FASB's leases standard, the staff conducted outreach with investors of public entity financial statements. The Board and the staff continue to perform outreach with investors to solicit feedback on costs and complexities in applying the leases standard and whether reported lease assets and lease liabilities and the related disclosures provide investors with decision-useful information.

For private companies and certain not-for-profit organizations, the Board deferred the

[1] See discussion at (among others): Summary of Update 2018-10; Remarks by Russell Golden at IMA 2019 Annual Conference; Speech by Sagar Teotia.
[2] The first round of outreach with public company investors was performed in 2020 and was summarized at the December 2, 2020 FASB Board meeting.

mandatory effective date for private companies and certain not-for-profit organizations twice (in November 2019 and again in June 2020) to help facilitate an effective adoption of the leases standard. In addition, the Board amended the lease guidance in response to certain private company stakeholder concerns, including about applying the guidance to related party arrangements between entities under common control.

The Board and the staff have had ongoing discussions on implementation with advisory groups and liaison meetings, including with the PCC and NAC, given the extended effective date. Recently, the PCC formed a Leases Working Group to understand private company challenges and determine whether any specific areas for simplification and identifiable solutions exist. The PCC Leases Working Group and FASB staff currently are soliciting feedback from private company preparers to identify areas of significant cost and/or complexity.

Prior SBAC/PMAC Discussion on Initial and Recurring Costs

On November 12, 2020, Small Business Advisory Committee (SBAC) members shared their implementation experiences and progress on the implementation of the leases standard. Members also discussed the complexities and challenges in certain areas, including the precision required to determine the incremental borrowing rate and getting the initial implementation infrastructure in place. Members observed that the subsequent application effort is expected to be much less significant going forward as sufficient processes are in place to comply with the leases standard.

On December 16, 2021, the SBAC held a joint meeting with the PCC and discussed implementation experiences, including systems and accounting resources, utilization of FASB educational materials, population of leases, and strategies for educating financial statement users. PCC and SBAC members who have experience implementing the leases standard discussed best practices such as proactively starting the implementation process to facilitate the transition and the importance of establishing communication between operational teams within an organization. Members also discussed considerations for a range of lease portfolio sizes when implementing the leases standard and accounting challenges such as embedded leases, determining the incremental borrowing rate, system challenges including considerable time needed to integrate the software, and a lack of accessibility to software vendors.

The minutes from these past discussions on leases standard are in Appendix A.

Discussion Questions

Question 1: Do you have any overall observations about whether the objective of the standard was met or about the benefits or costs (including initial costs and recurring costs) of applying the leases standard?

Question 2: What are your observations on the history of the FASB's leases project, including the standard-setting activities and joint deliberations with the IASB?

Question 3 (Lessee):

a) **(Investors)** How did recognizing operating leases on the balance sheet change the benefits and costs of analyzing the effects of leases?
b) **(Preparers/Auditors)** How did recognizing operating leases on the balance sheet change the benefits and costs of applying the lease accounting guidance?

Question 4 (Preparers/Practitioners): Do you have additional observations to share on ongoing application costs to comply with Topic 842? If so, please describe the nature of those costs (for example, systems, processes, and applying certain areas of guidance).

Appendix A: Excerpt from the Committee's Past Minutes on Leases

November 12, 2020 SBAC Session

The staff asked for feedback on key topics at a recent roundtable, including the lessee's use of the incremental borrowing rate to measure the lease liability, embedded leases, and lease modification guidance.

Three members (auditors and a preparer) commented about the challenges with the precision required in determining the incremental borrowing rate and predicted that private companies also will find that determination challenging. Another member (auditor) commented that there has been diversity in how auditors interpret companies' methodologies to determining the incremental borrowing rate.

The FASB staff asked whether a nonpublic entity should be allowed to elect to use the risk-free rate at the underlying class of asset level, rather than making an entity-wide election for all lease liabilities. Two members (auditor and preparer) commented that the nonpublic entity election to use the risk-free rate allows flexibility for those entities; however, the potential financial statement outcome of that election (that is, an inflated lease liability) is not favorable. They also noted that materiality contributes to the decision and sensitivity of what rate to use (risk-free rate or incremental borrowing rate).

Regarding identifying leases embedded in other contracts such as service contracts, multiple members (auditors, preparers) responded that the challenge for companies that have adopted the leases standard was initially establishing a process for identification and implementation. On an ongoing basis, given the processes that have been established, the costs and complexity of identifying and accounting for leases that are embedded in other contracts has decreased.

On the lease modification guidance, one member (auditor) described challenges with diversity in practice, specifically related to real estate leases, as well as a few experiences with small changes to the lease terms that have affected the timing or amount of certain lease payments (which then triggered conversations around whether to apply the lease modification guidance).

Members (auditor and preparers) then put additional emphasis on the initial challenge with establishing the proper processes and commented that the effective date delays were useful. Another member (auditor) also commented about the significant changes to the built-to-suit guidance under Accounting Standards Update No. 2016-02, *Leases (Topic 842).* The member observed that the changes were necessary and useful; however, it can be complex to determine whether control has transferred from the supplier to the customer in certain circumstances.

The FASB staff also asked whether public companies would elect to use the risk-free rate, if that option was provided. Two members (auditor and user) commented that while companies would prefer the simplicity of the optionality, it would be likely

less useful and decrease comparability.

November 12, 2020 Joint SBAC/PCC Session

The FASB staff solicited feedback from SBAC and PCC members to facilitate dialogue among the advisory groups about their experiences in implementing Topic 842, Leases, including observations, best practices, system and resource needs, and the use of FASB educational materials.

A PCC member who is a preparer and whose company early adopted Topic 842 discussed his implementation experiences. He noted that implementation required significant resources and changes to processes and systems because of the large volume and materiality of his company's leases and the application of new software. That member explained that some areas of Topic 842 did not change appreciably from prior guidance (Topic 840, Leases), including understanding the reasonably assured lease term, determining future lease payments, and lease classification requirements. That member noted that his company held several education sessions and trainings and utilized large firm publications when implementing the leases guidance. That member also noted that his company had several conversations with their financial statement users, particularly creditors, to educate those users about changes to their financial statements resulting from adopting Topic 842 (for example, changes in lease classification from operating to finance). That member asserted that the challenges and complexities of implementing and applying Topic 842 will become more apparent to the Board as the FASB's post-implementation review efforts progress.

An SBAC member who is a preparer also discussed her company's Topic 842 implementation experience. She noted that although her company does not have many leases, the most notable change when implementing Topic 842 was considering other agreements that may not have been considered to have a lease component, such as in data and vendor agreements. That member also discussed how a significant amount of resources were needed to evaluate those agreements, including collaboration with technological and operational teams, to ascertain whether a lease component existed. That member commented that from a user perspective, the most notable change is balance sheet recognition. She noted that after initially applying the guidance, application became more straightforward. That member also noted that the FASB resources and large firm publications were helpful in applying the guidance. An SBAC member who is a practitioner also noted that many firm publication interpretations are consistent and helpful in aligning preparer policies and procedures.

That practitioner member further noted that a common theme is that Topic 842 has made many entities more aware of certain aspects of historical lease accounting, such as renewal options, because operating leases are now recognized on the balance sheet. That member expressed the view that implementation required significant time and resources, primarily because it required data gathering and the involvement of several departments. He noted that implementing and

understanding the accounting has resulted in many benefits, including increasing internal controls and more readily identifying lease transactions. That member specifically identified the determination of the incremental borrowing rate as an area of the guidance that requires a significant amount of time and effort.

An SBAC member who is a user noted that his company has always adjusted the company's financial statements and included leases on the balance sheet in their analyses. He also noted that his company discusses how to evaluate contracts that include both an asset and a service agreement, in their analyses. That member recognized that determining the appropriate discount rate is challenging for preparers and users and leads to comparability difficulties.

An SBAC member who is a preparer encouraged private companies to begin the implementation process as early as possible. He noted that much time is spent by practitioners and preparers documenting procedures used to adopt Topic 842. He observed that outcomes (identifying a lease and lease classification) of applying Topic 842 were not significantly different from those reached under Topic 840 but noted that determining whether a lease exists in another contract (embedded lease) required more time. He also discussed how new software systems are typically needed for entities that have a larger lease portfolio. An FASB Board member expressed the importance of considering the portfolio size of leases when determining whether sophisticated software is needed. A PCC member who is a preparer noted that several controllers and chief financial officers of a trade organization with whom she is associated with expressed that it is difficult to access software vendors, leading to implementation challenges. The PCC Chair inquired about ideas on how to encourage entities to start the implementation process. Another SBAC member who is a preparer expressed that explaining the importance of the guidance is helpful in getting the cooperation of those involved.

An FASB Board member discussed the identification of embedded leases and noted that the guidance did not significantly change from Topic 840 but, rather, the requirement to recognize operating leases on the balance sheet may be drawing more attention to the lease identification evaluation. A PCC member who is a preparer responded to the FASB Board member stating that there are ongoing embedded lease challenges and specifically mentioned that the challenges include analyzing supply arrangements and data arrangements.

DEFINITIONS OF A PUBLIC ENTITY AND PUBLIC BUSINESS ENTITY
PUBLIC MARKETS ADVISORY COMMITTEE (PMAC)
MAY 2025

Session Objective

The Accounting Standards Codification (the Codification) was established in 2009 and is the single official source of authoritative generally accepted accounting principles (GAAP). The Codification introduced a new structure for GAAP by:

- Reorganizing thousands of pronouncements into roughly 90 accounting topics (including legacy literature inherited from Accounting Principles Board Opinions (1959-1973), Accounting Research Bulletins (1939-1959), and AICPA Statements of Position (started in 1974) and incremental accounting guidance from Audit and Accounting Guides (started in 1950s, updates published periodically)
- Eliminating the hierarchy of GAAP
- Displaying all topics using a consistent structure
- Requiring users of the Codification to consider analogies within the Codification for similar transactions or events before looking to nonauthoritative guidance for transactions and events not specified within the Codification.

Since 2009, the FASB has continued to improve and maintain GAAP by amending the Codification through the issuance of Accounting Standards Updates. Given the cumulative development of GAAP over time and by different standard-setters, different definitions of a nonpublic entity and public entity exist within the Codification that effect the measurement and disclosure requirements for certain sets of entities that prepare and provide GAAP financial statements.

For this session, PMAC members will be asked for their views on whether the Board should prioritize a future technical project that seeks to reduce the number of definitions of a public entity and nonpublic entity throughout GAAP by replacing the definitions with the public business entity definition in the Master Glossary; and whether the FASB should reconsider the definition of public business entity.

Overview of Materials

These materials include the following:

1. Definitions of a Public Entity and Public Business Entity
2. Discussion Questions
3. Appendix A: (Full Description) Definitions of a Public Entity and Nonpublic Entity

Definitions of a Public Entity and Public Business Entity

Stakeholders[1] provided feedback that the FASB should reconsider the definition of the Master Glossary term public business entity. Stakeholders noted that the term public business entity is expansive and, therefore, it can be costly for certain types[2] of closely held entities (such as nonissuer broker dealers) to apply the accounting and disclosure requirements for public business entities.

The Codification includes multiple definitions of a *nonpublic entity* and *public entity*, which were developed to establish recognition, measurement, disclosure, and effective date requirements for certain sets of reporting entities (see Appendix A for the definitions). In the past, some stakeholders have suggested that the FASB should reduce the number of definitions to minimize confusion and misunderstanding by investors, preparers, and practitioners when applying GAAP.

In December 2013, the FASB issued Accounting Standards Update No. 2013-12, *Definition of a Public Business Entity: An Addition to the Master Glossary*. The amendments in Update 2013-12 revised the Master Glossary to include a definition of a public business entity (PBE) for prospective use in GAAP. It did not affect the requirements that existed in 2013 or the definitions of a nonpublic entity and public entity. Having one PBE definition was intended to reduce the complexity of multiple definitions of a nonpublic entity and public entity within GAAP on a going-forward basis. Furthermore, the PBE definition clarifies which nonpublic entities potentially qualify for alternative financial accounting and reporting guidance as a private company.

A PBE is defined as:

> [A] business entity meeting any one of the criteria below. Neither a not-for-profit entity nor an employee benefit plan is a business entity.
>
> a. It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements (including voluntary filers), with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
>
> b. It is required by the Securities Exchange Act of 1934 (the Act), as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency other than the SEC.

[1] This feedback was provided during the development of the FASB's Invitation to Comment, Agenda Consultation, which was issued for public comment on January 3, 2025.

[2] The staff has also heard feedback from certain private company stakeholders that private companies that are conduit bond obligors should not be included in the definition of *public business entity* (those entities are currently PBEs because of item (d) in the PBE definition).

c. It is required to file or furnish financial statements with a foreign or domestic regulatory agency in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.

d. It has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market.

e. It has one or more securities that are not subject to contractual restrictions on transfer, and it is required by law, contract, or regulation to prepare U.S. GAAP financial statements (including notes) and make them publicly available on a periodic basis (for example, interim or annual periods). An entity must meet both of these conditions to meet this criterion.

An entity may meet the definition of a public business entity solely because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements that are filed or furnished with the SEC.

In developing the Master Glossary definition of a PBE, the Board discussed replacing the definitions of a public entity and nonpublic entity throughout GAAP but decided not to at that time. Instead, the Board observed that it may consider a project in the future that evaluates replacing the definitions of a public entity and nonpublic entity by using the PBE definition.

The definition of PBE differs from some of the definitions of nonpublic entity and public entity in the Codification. Some examples from the Codification where various definitions of a nonpublic entity and a public entity are used to establish different measurement and disclosure requirements include the following. The full definitions are all listed in Appendix A:

- **Segment Reporting (Topic 280):** Requires *public entities* (with certain exceptions) to identify and disclose information about their operating segments. This topic uses Public Entity (Definition 1), which is used in four other Topics.
- **Debt (Topic 470):** Requires *public entities* to disclose the amount by which an instrument's if-converted value exceeds its principal amount for convertible debt instruments with cash conversion (paragraph 470-20-50-5). This topic uses Public Entity (Definition 3), which is used in one other Topic.
- **Compensation—Retirement Benefits** (**Topic 715):** A *nonpublic entity* that sponsors a defined benefit pension plan or other defined benefit postretirement plan is exempt from certain disclosures, as compared to a public entity (paragraph 715-20-50-5). This topic uses Nonpublic Entity (Definition 1), which is used in nine

other Topics.

- **Compensation—Stock Compensation (Topic 718):** *Nonpublic entities* are exempt from certain disclosure requirements and are permitted to use a different measurement attribute than public entities for certain equity instruments and liabilities arising from share-based payment arrangements. This topic uses Nonpublic Entity (Definition 1), which is used in nine other Topics.
- **Business Combinations (Topic 805):** A *public entity* that is an acquirer is required to disclose the amounts of revenue and earnings of the acquiree since the acquisition date included in the consolidated income statement for the reporting period, certain comparative information, and material nonrecurring pro forma adjustments directly attributable to the business combination(s) included in the supplemental pro forma information (paragraph 805-10-50-2(h)), unless impracticable. Similar disclosures are required for healthcare and not-for-profit entities that are *public entities* (Sections 954-805-50 and 958-805-50). This topic uses Public Entity (Definition 1), which is used in four other Topics.
- **Extractive Activities—Oil and Gas (Topic 932):** *Publicly traded companies* with significant oil and gas activities are required to disclose supplementary information including proved oil and gas reserve quantities; capitalized costs and results of operations for oil- and gas-producing activities; costs incurred for property acquisition, exploration, and development; and standardized measures of discounted future net cash flows (paragraph 932-235-50-2). This Topic uses Publicly Traded Company (Definition 2), which only is used in this Topic.

Discussion Questions

Question 1: Should the FASB consider amending the Master Glossary term public business entity (PBE)? If the FASB were to reconsider the Master Glossary term, which type of entities should be included or excluded and why?

Question 2: Should the Board consider a project that seeks to reduce the number of definitions of a public entity and a nonpublic entity throughout GAAP? If so, what priority should the Board place on such a project?

Question 3: If the Board were to pursue a project to reduce the number of definitions of a public entity and a nonpublic entity, should the Board consider replacing the various definitions of a public entity (and related terms) with the PBE definition? How should the Board consider the way the definitions are used (for example, definitions that establish scope versus definitions that relate to measurement and disclosure requirements)?

Appendix A: Definitions of a Public Entity and a Nonpublic Entity

Full Description of Each Definition

Public Entity (Definition 1)

A business entity or a not-for-profit entity that meets any of the following conditions:

1. It has issued debt or equity securities or is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).
2. It is required to file financial statements with the Securities and Exchange Commission (SEC).
3. It provides financial statements for the purpose of issuing any class of securities in a public market.

See Topic(s): 280, 740, 805, 954, 958

Public Entity (Definition 2)[3]

An entity that meets any of the following criteria:

a. Its debt or equity securities are traded in a public market, including those traded on a stock exchange or in the over-the-counter market (including securities quoted only locally or regionally).
b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).
c. Its financial statements are filed with a regulatory agency in preparation for the sale of any class of securities.

See Topic(s): 740

Public Entity (Definition 3)

An entity that meets any of the following criteria:

a. Has equity securities that trade in a public market, either on a stock exchange (domestic or foreign) or in an over-the-counter market, including securities quoted only locally or regionally
b. Makes a filing with a regulatory agency in preparation for the sale of any class of equity securities in a public market
c. Is controlled by an entity covered by the preceding criteria. That is, a subsidiary of a public entity is itself a public entity.

An entity that has only debt securities trading in a public market (or that has made a filing with a regulatory agency in preparation to trade only debt securities) is not a public entity.

[3] This Master Glossary term for Topic 740 will be superseded as a result of the amendments in Accounting Standards Update No. 2023-09, *Income Taxes (Topic 740)—Improvements to Income Tax Disclosures*, which are effective for public business entities for annual periods beginning after December 15, 2024, and for entities other than public business entities for annual periods beginning after December 15, 2025.

See Topic(s): 470, 718

Nonpublic Entity (Definition 1)

Any entity that does not meet any of the following conditions:

a. Its debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in an over-the-counter market, including securities quoted only locally or regionally.

b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

c. It files with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market.

d. It is required to file or furnish financial statements with the Securities and Exchange Commission.

e. It is controlled by an entity covered by criteria (a) through (d).

See Topic(s): 105, 220, 350, 360, 405, 715, 718, 820, 830, 954

Nonpublic Entity (Definition 2)

Any entity other than one that meets any of the following criteria:

a. Has equity securities that trade in a public market either on a stock exchange (domestic or foreign) or in an over-the-counter market, including securities quoted only locally or regionally

b. Makes a filing with a regulatory agency in preparation for the sale of any class of equity securities in a public market

c. Is controlled by an entity covered by the preceding criteria.

An entity that has only debt securities trading in a public market (or that has made a filing with a regulatory agency in preparation to trade only debt securities) is a nonpublic entity.

See Topic(s): 480, 718

Nonpublic Entity (Definition 3)

Any entity other than one with any of the following characteristics:

a. Whose debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally

b. That is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets)

c. That makes a filing with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market

d. That is controlled by an entity covered by a., b., or c.

Conduit debt securities refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing financing for a specific third party (the conduit bond obligor) that is not a part of the state or local government's financial reporting entity. Although conduit debt

securities bear the name of the governmental entity that issues them, the governmental entity often has no obligation for such debt beyond the resources provided by a lease or loan agreement with the third party on whose behalf the securities are issued. Further, the conduit bond obligor is responsible for any future financial reporting requirements.

See Topic(s): 715

Nonpublic Entity (Definition 4)

Any entity that does not meet any of the following conditions:

a. Its debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally.

b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

c. It files with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market.

d. It is controlled by an entity covered by the preceding criteria.

NO INCOMING LINKS

Nonpublic Entity (Definition 5)

An entity that does not meet any of the following criteria:

a. Its debt or equity securities are traded in a public market, including those traded on a stock exchange or in the over-the-counter market (including securities quoted only locally or regionally).

b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

c. Its financial statements are filed with a regulatory agency in preparation for the sale of any class of securities.

See Topic(s): 715, 740

Publicly Traded Company (Definition 1)

A publicly traded company includes any company whose securities trade in a public market on either of the following:

a. A stock exchange (domestic or foreign)

b. In the over-the-counter market (including securities quoted only locally or regionally), or any company that is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

Additionally, when a company is required to file or furnish financial statements with the SEC or makes a filing with a regulatory agency in preparation for sale of its securities in a public market it is considered a publicly traded company for this purpose.

Conduit debt securities refers to certain limited-obligation revenue bonds, certificates of participation, or similar debt instruments issued by a state or local governmental entity for the express purpose of providing financing for a specific third party (the conduit bond obligor) that is

not a part of the state or local government's financial reporting entity. Although conduit debt securities bear the name of the governmental entity that issues them, the governmental entity often has no obligation for such debt beyond the resources provided by a lease or loan agreement with the third party on whose behalf the securities are issued. Further, the conduit bond obligor is responsible for any future financial reporting requirements.

See Topic(s): 220, 270

Publicly Traded Company (Definition 2)

A business entity that has any of the following characteristics:

a. Whose securities are traded in a public market on a domestic stock exchange or in the domestic over-the-counter market (including securities quoted only locally or regionally)

b. That is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets)

c. Whose financial statements are filed with a regulatory agency in preparation for the sale of any class of securities in a domestic market.

See Topic(s): 932

Publicly Traded Entity (or Public Entity) [Only one definition]

Any entity that does not meet the definition of a nonpublic entity [Linked to nonpublic entity-3]

See Topic(s): 715
