

Lessor Example – Performance Obligation Approach

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Leasing Example – Lessor Perspective – Performance Obligation

Subject:

ABC Corporation has entered into a lease to house operations.

Details:

The lease terms are as follows:

Tenant:	ABC Corporation (ABC)
Lessor:	General Properties, LLC (GP, LLC)
Premises:	Suite 100 of the 9999 Building, totaling 20,000 rentable square feet
Term:	10 years
Lease Date	November 1, 2009
Commencement Date:	January 1, 2010
Base Rental:	\$22 per square foot for 2010 with a 5% increase annually on January 1
Initial Direct Costs	ABC Corporation paid an attorney \$9,000 in general fees and \$1,000 for document preparation in conjunction with the lease process
Commissions	Commissions on the lease of \$50,000 are paid directly by the lessor
Security Deposit:	\$25,000
Free Rent Period:	No rent shall be due for January 1, 2010 through March 31, 2010
Option to Extend:	Lease may be extended for one (1) additional term of five (5) years with a significant termination penalty if not extended
% share Operating Costs:	Certain operating costs of the building will be allocated at \$25,000 annually for common area maintenance (“CAM charges”)
Subletting:	Not permitted
Build Out Allowance:	None at inception, \$50,000 build out allowance provided at the beginning of year 6 of the lease and at renewal, if extended
Residual Value Guarantees:	None
Purchase Option	None, but failure to renew does trigger a significant penalty in the contract

Other relevant assumptions:

Incremental borrowing:	The incremental borrowing rate of ABC Corporation is 7%
Rate charged by Lessor	This rate cannot be reliably determined by the lessee, but was computed at 8% for the lessor
Likelihood of extension:	More likely than not due to the termination penalty
Reassessment:	Throughout the period, no reassessment of contingent rentals, residual value guarantees or impairment occur
Amortization:	The Lease Liability (lessor) will be amortized using the straight line over the life of the lease

Comparison of Financial Statement Impact for Life of the Lease

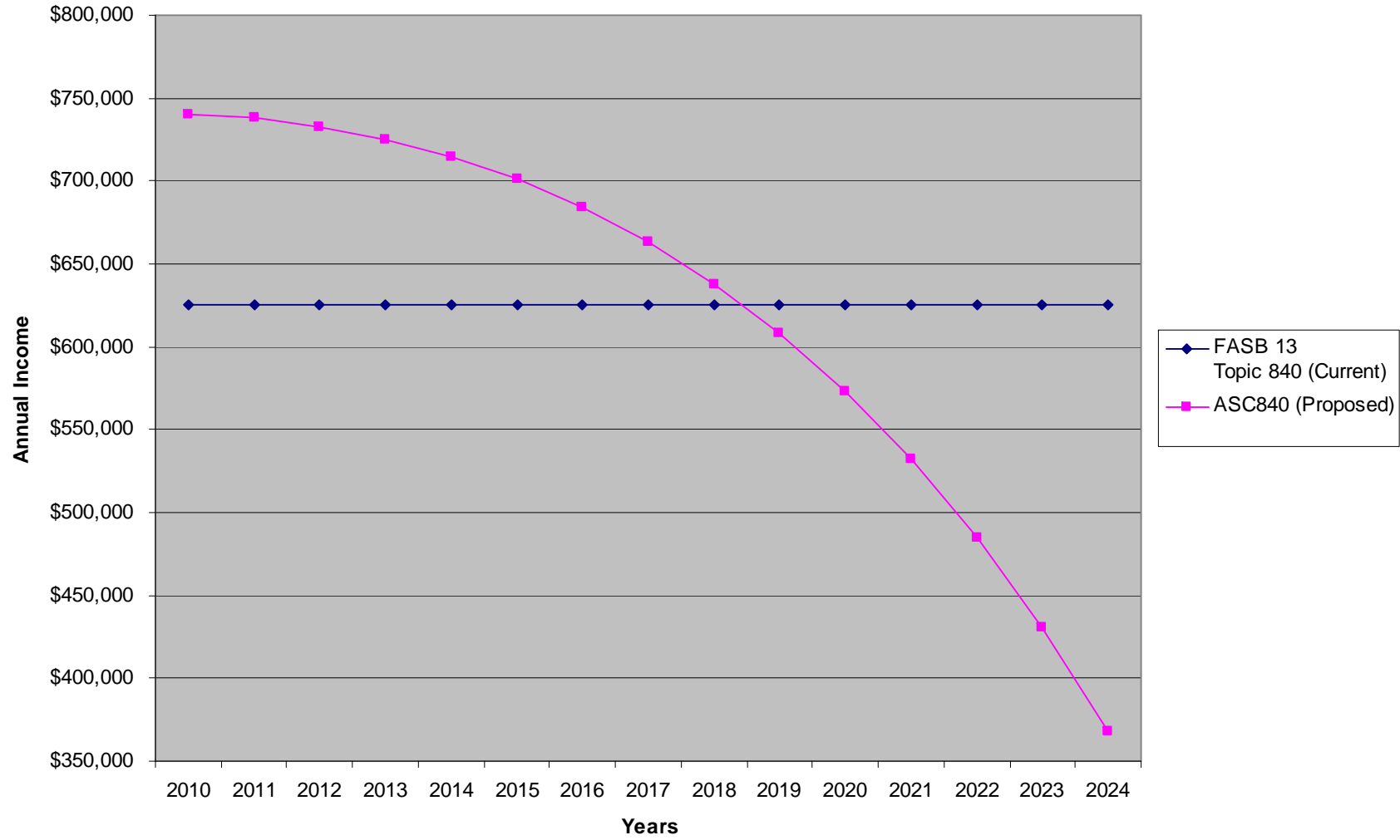
Detailed balance sheet comparisons follow, but the summary impacts of key elements are listed below:

Year	Lease Revenue / (Expense) vs. Interest Income and Lease Income		Straight Line Rent Receivable vs. Right to Receive Asset		Lease Liability (Not Recorded Under Current Accounting)	
	FASB 13 (Current)*	ASC840 (Proposed)*	FASB 13 (Current)	ASC840 (Proposed)	FASB 13 (Current)	ASC840 (Proposed)
2009	\$(50,000)	\$-	\$--	\$--	\$--	\$--
2010	\$625,653	\$740,322	\$295,653	\$5,106,905	\$--	\$4,646,583
2011	\$625,653	\$738,447	\$459,307	\$5,051,454	\$--	\$4,314,685
2012	\$625,653	\$732,975	\$599,760	\$4,967,330	\$--	\$3,982,786
2013	\$625,653	\$725,085	\$716,013	\$4,851,117	\$--	\$3,650,887
2014	\$625,653	\$714,487	\$806,867	\$4,698,905	\$--	\$3,318,988
2015	\$625,653	\$700,849	\$870,920	\$4,506,256	\$--	\$2,987,090
2016	\$625,653	\$683,809	\$906,974	\$4,268,566	\$--	\$2,655,191
2017	\$625,653	\$662,979	\$913,627	\$3,980,646	\$--	\$2,323,292
2018	\$625,653	\$637,919	\$889,280	\$3,636,667	\$--	\$1,991,393
2019	\$625,653	\$608,147	\$832,234	\$3,230,315	\$--	\$1,659,495
2020	\$625,653	\$573,138	\$741,187	\$2,754,754	\$--	\$1,327,596
2021	\$625,653	\$532,324	\$614,240	\$2,202,580	\$--	\$995,697
2022	\$625,653	\$485,084	\$449,694	\$1,565,565	\$--	\$663,798
2023	\$625,653	\$430,728	\$245,547	\$834,594	\$--	\$331,899
2024	\$625,653	\$368,505	\$--	\$--	\$--	
Totals	\$9,334,800	\$9,334,800				
Average Balance			\$622,760	\$3,443,710	\$--	\$2,323,292

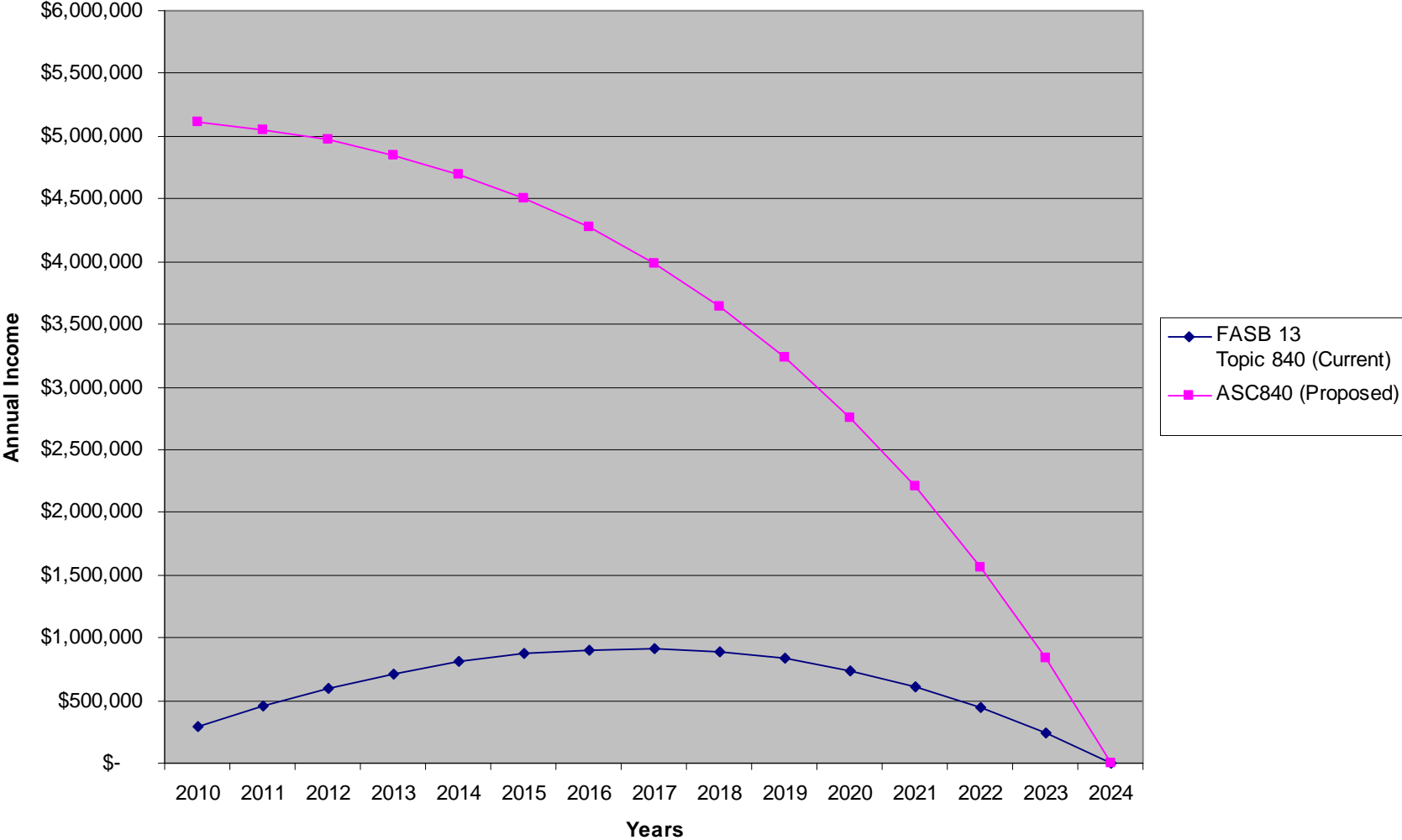
* Excludes CAM charges and Security Deposit

Note – as a result of the renewal penalty, the lease term under current standards is considered to include the renewal period, so the income is calculated over the 15 years (as the longest term more likely than not to occur). Without the renewal penalty, the income under current accounting would be higher toward the end of the lease term as the first 10 years would be calculated on an average monthly rental of \$45,202 (\$542,420 annually) and the last five years would be calculated on an average monthly rental of \$66,010 (\$792,120 annually).

Impact on Net Income



Impact on Lease Receivable



Comparison of Financial Statement Impact for Life of the Lease – Detailed by Year

December 31, 2010 – Initial Lease Year End

	FASB 13 (Current)		ASC840 (ED - Proposed)	
	Income Stmt	Balance Sheet	Income Stmt	Balance Sheet
Income Statement				
Lease Income	\$650,653		\$331,899	
Interest Income	\$--		\$408,423	
Depreciation Expense	\$(1,250,000)		\$(1,250,000)	
Impact on Net Income	\$(599,347)		\$(509,678)	
Balance Sheet				
<i>Assets</i>				
Straight Line Lease Asset		\$295,653		\$--
Leased Asset (net of depreciation)		\$41,000,000		\$--
Net Leased Asset (right to receive asset, underlying leased asset, less lease liability)		\$--		\$41,460,322
<i>Liabilities</i>				
Security Deposit		\$25,000		\$25,000

- Depreciation expense represents the depreciation of the underlying asset only
- Note that cash payments received for leases are separated on the cash flow statement in operating activities.

December 31, 2014 – Middle of Original Lease Term Life

	FASB 13 (Current)		ASC840 (ED - Proposed)	
	Income Stmt	Balance Sheet	Income Stmt	Balance Sheet
Income Statement				
Lease Income	\$650,653		\$331,899	
Interest Income	\$--		\$382,589	
Depreciation Expense	\$(1,250,000)		\$(1,250,000)	
Impact on Net Income	\$(599,347)		\$(535,512)	
Balance Sheet				
<i>Assets</i>				
Straight Line Lease Asset		\$806,867		\$--
Leased Asset (net of depreciation)		\$36,000,000		\$--
Net Leased Asset (right to receive asset, underlying leased asset, less lease liability)		\$--		\$37,379,917
<i>Liabilities</i>				
Security Deposit		\$25,000		\$25,000

- Depreciation expense represents the depreciation of the underlying asset only

- Note that cash payments received for leases are separated on the cash flow statement in operating activities.

December 31, 2019 – End of Original Lease Term Life

	FASB 13 (Current)		ASC840 (ED - Proposed)	
	Income Stmt	Balance Sheet	Income Stmt	Balance Sheet
Income Statement				
Lease Income	\$650,653		\$331,899	
Interest Income	\$--		\$276,248	
Depreciation Expense	\$(1,250,000)		\$(1,250,000)	
Impact on Net Income	\$(599,347)		\$(641,853)	
Balance Sheet				
<i>Assets</i>				
Straight Line Lease Asset		\$832,334		\$--
Leased Asset (net of depreciation)		\$29,750,000		\$--
Net Leased Asset (right to receive asset, underlying leased asset, less lease liability)		\$--		\$31,320,821
<i>Liabilities</i>				
Security Deposit		\$25,000		\$25,000

- Depreciation expense represents the depreciation of the underlying asset only
- Note that cash payments received for leases are separated on the cash flow statement in operating activities.

December 31, 2020 – First Year of Renewal Term

	FASB 13 (Current)		ASC840 (ED - Proposed)	
	Income Stmt	Balance Sheet	Income Stmt	Balance Sheet
Income Statement				
Lease Income	\$650,653		\$331,899	
Interest Income	\$--		\$241,239	
Depreciation Expense	\$(1,250,000)		\$(1,250,000)	
Impact on Net Income	\$(599,347)		\$(676,862)	
Balance Sheet				
<i>Assets</i>				
Straight Line Lease Asset		\$741,187		\$--
Leased Asset (net of depreciation)		\$28,500,000		\$--
Net Leased Asset (right to receive asset, underlying leased asset, less lease liability)		\$--		\$29,927,159
<i>Liabilities</i>				
Security Deposit		\$25,000		\$25,000

- Depreciation expense represents the depreciation of the underlying asset only
- Note that cash payments received for leases are separated on the cash flow statement in operating activities.

December 31, 2025 – Final Year of Renewal Term

	FASB 13 (Current)		ASC840 (ED - Proposed)	
	Income Stmt	Balance Sheet	Income Stmt	Balance Sheet
Income Statement				
Lease Income	\$650,653		\$331,899	
Interest Income	\$--		\$36,606	
Depreciation Expense	\$(1,250,000)		\$(1,250,000)	
Impact on Net Income	\$(599,347)		\$(881,495)	
Balance Sheet				
<i>Assets</i>				
Straight Line Lease Asset		\$--		\$--
Leased Asset (net of depreciation)		\$22,250,000		\$--
Net Leased Asset (right to receive asset, underlying leased asset, less lease liability)		\$--		\$22,250,000
<i>Liabilities</i>				
Security Deposit		\$--		\$--

- Depreciation expense represents the depreciation of the underlying asset only
- Note that cash payments received for leases are separated on the cash flow statement in operating activities.

Lessor Current Accounting – Original Lease Term

Lease life Cycle		FASB 13 (Current)			ASC840 (ED - Proposed)		
Date	Activity	Accounts	Debit	Credit	Accounts	Debit	Credit
11/30/09	Security Deposit	Cash Lease Deposit Liability	\$25,000	\$25,000	Cash Lease Deposit Liability	\$25,000	\$25,000
11/30/09	Commission Expense	Commission expense Cash	\$50,000	\$50,000	Right To Receive Asset Cash	\$50,000	\$50,000
1/1/10	Recognition of Right to Receive Asset and Liability	None			Right to Receive Asset (RTR) Lease Liability	\$4,978,482	\$4,978,482
Jan – Mar, 2010	Monthly Rental and Income	S-L Lease Asset Straight Line Rent Income	\$52,138	\$52,138	Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$34,035 \$27,658	\$34,035 \$27,658
Apr – Dec, 2010	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$36,667 \$15,471	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$36,667 \$27,658	\$2,632 \$34,035 \$27,658
12/31/10	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2011	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$38,500 \$13,638	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$38,500 \$27,658	\$4,621 \$33,879 \$27,658
12/31/11	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2012	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$40,425 \$11,713	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$40,425 \$27,658	\$7,002 \$33,423 \$27,658
12/31/12	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000

2013	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$42,446 \$ 9,692	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$42,446 \$27,658	\$9,680 \$32,766 \$27,658
12/31/13	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2014	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$44,569 \$ 7,569	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$44,569 \$27,658	\$12,687 \$31,882 \$27,658
12/31/14	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
1/1/15	Build out allowance	None			None		
2015	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$46,797 \$ 5,341	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$46,797 \$27,658	\$16,051 \$30,746 \$27,658
12/31/15	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2016	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$49,137 \$ 3,001	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$49,137 \$27,658	\$19,811 \$29,326 \$27,658
12/31/16	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2017	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$51,594 \$ 544	\$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$51,594 \$27,658	\$24,004 \$27,590 \$27,658
12/31/17	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2018	Monthly Rental and Income	Cash S-L Lease Asset	\$54,173	\$2,035	Cash Right To Receive Asset	\$54,173	

		Straight-Line Rent Income		\$52,138	(RTR) Lease Liability	\$27,658	\$28,671
					Interest Income		\$25,502
					Lease Income		\$27,658
12/31/18	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2019	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$56,882	\$ 4,744 \$52,138	Cash Right To Receive Asset (RTR) Lease Liability	\$56,882 \$27,658	\$33,861
					Interest Income		\$23,021
					Lease Income		\$27,658
12/31/19	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000

Lessor Current Accounting – Extended Lease Term

Lease life Cycle		FASB 13 (Current)			ASC840 (ED - Proposed)		
Date	Activity	Accounts	Debit	Credit	Accounts	Debit	Credit
2020	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$59,726	\$ 7,588 \$52,138	Cash Right To Receive Asset (RTR) Lease Liability	\$59,726 \$27,658	\$39,623
					Interest Income		\$20,103
					Lease Income		\$27,658
12/31/20	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2021	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$62,712	\$10,754 \$52,138	Cash Right To Receive Asset (RTR) Lease Liability	\$62,712 \$27,658	\$46,010
					Interest Income		\$16,702
					Lease Income		\$27,658
12/31/21	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2022	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$65,848	\$13,710 \$52,138	Cash Right To Receive Asset (RTR) Lease Liability	\$65,848 \$27,658	\$53,083
					Interest Income		\$12,765
					Lease Income		\$27,658
12/31/22	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000

2023	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$69,140	\$17,002 \$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$69,140 \$27,658	\$60,904 \$ 8,236 \$27,658
12/31/23	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
2024	Monthly Rental and Income	Cash S-L Lease Asset Straight-Line Rent Income	\$72,597	\$20,459 \$52,138	Cash Right To Receive Asset (RTR) Lease Liability Interest Income Lease Income	\$72,597 \$27,658	\$69,546 \$3,051 \$27,658
12/31/24	Annual CAM Charges	Cash CAM Income	\$25,000	\$25,000	Cash CAM Income	\$25,000	\$25,000
12/31/24	Recovery of Deposit	Lease Deposit Liability Cash	\$25,000	\$25,000	Lease Deposit Liability Cash	\$25,000	\$25,000

General Properties, LLC
Consolidated Balance Sheet
For the Year Ended December 31, 2010

Assets

	FASB 13 (Current)	ASC840 (Proposed)
Current Assets		
Cash and cash equivalents	\$ 235,000	\$ 235,000
Accounts receivable, net	3,250,000	3,250,000
Inventories	5,750,000	5,750,000
Prepaid expenses and other	<u>65,000</u>	<u>65,000</u>
Total current assets	<u>9,300,000</u>	<u>9,300,000</u>
Property and Equipment, At Cost		
Land and buildings	50,000,000	
Furniture and fixtures	25,000,000	25,000,000
Less accumulated depreciation and amortization	<u>(21,500,000)</u>	<u>(12,500,000)</u>
	<u>53,500,000</u>	<u>12,500,000</u>
Underlying leased assets, net of accumulated depreciation of \$9,000,000		41,000,000
Right to receive assets		5,106,905
Less lease liabilities		<u>(4,646,583)</u>
Net lease asset		41,460,322
Straight Line Lease Asset	295,653	
Total assets	<u>\$ 63,095,653</u>	<u>\$ 63,260,322</u>

Liabilities and Stockholders' Equity

	FASB 13 (Current)	ASC840 (Proposed)
Current Liabilities		
Current maturities of long-term debt	\$ 100,000	\$ 100,000
Accounts payable and accrued expenses	<u>850,000</u>	<u>850,000</u>
Total current liabilities	<u>950,000</u>	<u>950,000</u>
Long-term Debt	<u>4,000,000</u>	<u>4,000,000</u>
Stockholders' Equity		
Common stock	100,000	100,000
Retained earnings	<u>58,045,653</u>	<u>58,210,322</u>
Total stockholders' equity	<u>58,145,653</u>	<u>58,310,322</u>
Total liabilities and stockholders' equity	<u>\$ 63,095,653</u>	<u>\$ 63,260,322</u>

General Properties, LLC
Consolidated Income Statement
For the Year Ended December 31, 2010

	<u>FASB 13 (Current)</u>	<u>ASC840 (Proposed)</u>
Net Sales	\$ 27,000,000	\$ 27,000,000
Cost of Goods Sold	<u>18,000,000</u>	<u>18,000,000</u>
Gross Profit	<u>9,000,000</u>	<u>9,000,000</u>
Lease income	625,653	
Operating Expenses		
Salaries	4,000,000	4,000,000
Depreciation and amortization	3,750,000	2,500,000
Other	85,000	85,000
Lease income		(331,899)
Interest income		(408,423)
Less depreciation expense on underlying leased asset		<u>1,250,000</u>
Net lease expense		509,678
	<u>7,835,000</u>	<u>7,094,678</u>
Operating Income	<u>1,790,653</u>	<u>1,905,322</u>
Other Expense		
Interest expense	246,000	246,000
Other	<u>137,000</u>	<u>137,000</u>
	<u>383,000</u>	<u>383,000</u>
Net Income	<u>\$ 1,407,653</u>	<u>\$ 1,522,322</u>

General Properties, LLC
Consolidated Cash Flow Statement
For the Year Ended December 31, 2010

	FASB 13 (Current)	ASC840 (Proposed)
Operating Activities		
Net income	\$ 1,407,653	\$ 1,522,322
Items not requiring (providing) cash		
Depreciation	3,750,000	3,750,000
Cash payments received for leases		330,000
Changes in		
Accounts receivable	(850,000)	(850,000)
Inventories	(500,000)	(500,000)
Straight line lease asset	(295,653)	
Right to receive lease payments asset		(408,423)
Lease liabilities		(331,899)
Accounts payable and accrued expenses	(627,017)	(627,017)
Net cash provided by operating activities	2,884,983	2,884,983
Investing Activities		
Purchase of property and equipment	(3,000,000)	(3,000,000)
Net cash used in investing activities	(3,000,000)	(3,000,000)
Financing Activities		
Payment of dividends	265,017	265,017
Net cash used in financing activities	265,017	265,017
Increase in Cash and Cash Equivalents	150,000	150,000
Cash and Cash Equivalents, Beginning of Year	85,000	85,000
Cash and Cash Equivalents, End of Year	\$ 235,000	\$ 235,000
Supplemental Cash Flows Information		
Interest paid on long-term debt	\$ 246,000	\$ 246,000

General Properties, LLC
Notes to Consolidated Financial Statements
December 31, 2010

Note X: Lease Accounting

Amounts Recognized in the Financial Statements

The Company entered into a lease on November 1, 2009 for 20,000 square feet of space commencing on January 1, 2010 for a ten year term with one optional renewal period of five years. The lease includes a significant penalty for non-renewal, resulting in an assessment that the longest term more likely than not to occur is the entire 15 years, including the renewal period. Initial direct costs consist of commission expense of \$50,000 incurred in conjunction of entering the lease.

Net lease expense on the income statement of \$509,678 consists of interest income related to the right to receive lease payments of \$408,423, lease income earned from satisfaction of the lease liability of \$331,899 less depreciation expense of \$1,250,000 on the underlying leased asset.

The facility is amortized on a straight line basis over a 40 year life, as this best reflects the pattern of use of the benefit of the space. There are no significant limitations imposed on the Company as a result of entering this lease.

The right to use assets and liabilities to make payments changed during the period as follows:

	Right to Receive Asset	Lease Liability
	<u> </u>	<u> </u>
Beginning balance	\$ 50,000	\$ 0
Recognition of present value of lease payments	4,978,482	(4,978,482)
Interest income on right to receive lease payments	408,423	
Lease income earned from satisfaction of lease liability		331,899
Cash payments	<u>(330,000)</u>	<u> </u>
Ending balance	<u>\$ 5,106,905</u>	<u>\$ (4,646,583)</u>

Lease Impact on Amount, timing and Uncertainty of Future Cash Flows

The rate charged to the lessee for the facility lease at inception was indeterminable, so the discount rate used to compute the present value of lease payments was the best estimate of the Company's incremental borrowing rate of 7%.

Future minimum lease payments to be received, including the renewal term, at December 31, 2010, were:

2011	\$ 462,000
2012	\$ 485,200
2013	\$ 509,400
2014	\$ 534,800
2015	\$ 561,600
Later years	<u>6,501,800</u>
	<u>\$ 9,054,800</u>