

Short Term Building Lease

**Disclaimer – The exposure draft received nearly 700 letters of comment through the comment period ended December 15, 2010. There is some expectation that key features of the standard will be modified as a result of constituent response. As a result, these illustrative examples will not likely be accurate or appropriate to rely upon after issuance of the final standard. We have provided these as an educational tool only and do not represent these examples to be accurate under current or future final standards. Any templates used in the examples below are for internal use only and are not available for distribution.

Leasing Example – **Short-Term Building Lease**

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:	1 year
Lease Date	July 1, 2010
Commencement Date:	July 1, 2010
Base Rental:	\$22 per square foot per annum
Initial Direct Costs	None
Commissions	None
Security Deposit:	None
Free Rent Period:	None
Option to Extend:	None
% share Operating Costs:	None
Subletting:	Not permitted
Build Out Allowance:	None
Residual Value Guarantees:	None
Purchase Option	None

Other relevant assumptions:

Incremental borrowing:	Not relevant for short-term lease
Rate charged by Lessor	Not relevant for short-term lease
Likelihood of extension:	Doubtful
Amortization:	The Right to Use Asset (lessee) and Lease Liability (lessor) will be amortized 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 impact of key elements are listed below:

Year	Lease Expense vs. Amort / Interest		Right To Use Asset at Year End, Net (not recorded under current accounting requirements)		Straight Line Liab vs. Lease Liability at Year End	
	FASB 13 (Current)*	ASC840 (Proposed)*	FASB 13 (Current)	ASC840 (Proposed)	FASB 13 (Current)	ASC840 (Proposed)
2010	\$220,000	\$220,000	\$--	\$220,000	\$--	\$220,000
2011	\$220,000	\$220,000	\$--	\$--	\$--	\$--
Totals	\$440,000	\$440,000				
Average Balance			\$--	\$110,000	\$--	\$110,000

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				
Operating Expense (Rent)	\$220,000		\$--	
Amortization Expense	\$--		\$220,000	
Interest Expense	\$--		\$--	
Impact on Net Income	\$220,000		\$220,000	
Balance Sheet				
<i>Assets</i>				
Right to Use Asset		\$--		\$440,000
Accm Amort – RTUAsset		\$--		\$(220,000)
<i>Liabilities</i>				
Lease Liability (St Line / Lease Ob)		\$--		\$(220,000)

December 31, 2011 – Final Year of Lease

	FASB 13 (Current)		ASC840 (ED - Proposed)	
	Income Stmt	Balance Sheet	Income Stmt	Balance Sheet
Income Statement				
Operating Expense (Rent)	\$220,000		\$--	
Amortization Expense	\$--		\$220,000	
Interest Expense	\$--		\$--	
Impact on Net Income	\$220,000		\$220,000	
Balance Sheet				
<i>Assets</i>				
Right to Use Asset		\$--		\$440,000
Accm Amort – RTUAsset		\$--		\$(440,000)
<i>Liabilities</i>				
Lease Liability (St Line / Lease Ob)		\$--		\$--

- Note that cash impacts are the same under both sets of accounting.
- Note that cash flows from leasing under current standards are part of operating income on the cash flow statement, but are separate out as financing cash flows under the proposed standard.

Lessee Current Accounting – Original Lease Term

Lease life Cycle		FASB 13 (Current)			ASC840 (ED - Proposed)		
<i>Date</i>	<i>Activity</i>	<i>Accounts</i>	<i>Debit</i>	<i>Credit</i>	<i>Accounts</i>	<i>Debit</i>	<i>Credit</i>
7/1/10	Recognition of Right to Use Asset and Liability	None			Right to Use Asset (RTU) Lease Liability	\$440,000	\$440,000
July, 2010 – June, 2011	Monthly Rental and Expenses	Rent Expense Cash	\$36,667	36,667	Lease Liability RTU Amortization Expense RTU Accm Amort Cash	36,667 36,667	36,667 36,667

ABC Corporation
Consolidated Balance Sheet
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	65,000	65,000
Total current assets	9,300,000	9,300,000
 Property and Equipment, At Cost		
Furniture and fixtures	345,000	345,000
Right of use assets	-	440,000
	345,000	785,000
Less accumulated depreciation and amortization	(100,000)	(320,000)
	245,000	465,000
Total assets	\$ 9,545,000	\$ 9,765,000

Liabilities and Stockholders' Equity

	FASB 13 (Current)	ASC840 (Proposed)
Current Liabilities		
Current maturities of long-term debt	\$ 100,000	\$ 100,000
Current maturities of lease liabilities	-	220,000
Accounts payable and accrued expenses	850,000	850,000
Total current liabilities	950,000	1,170,000
Long-term Debt	4,000,000	4,000,000
Stockholders' Equity		
Common stock	100,000	100,000
Retained earnings	4,495,000	4,495,000
Total stockholders' equity	4,595,000	4,595,000
Total liabilities and stockholders' equity	\$ 9,545,000	\$ 9,765,000

ABC Corporation
Consolidated Income Statement
For the Year Ended December 31, 2010

	FASB 13 (Current)	ASC840 (Proposed)
Net Sales	\$ 25,000,000	\$ 25,000,000
Cost of Goods Sold	<u>18,000,000</u>	<u>18,000,000</u>
Gross Profit	<u>7,000,000</u>	<u>7,000,000</u>
Operating Expenses		
Salaries	4,000,000	4,000,000
Rent expense	245,000	25,000
Depreciation and amortization	50,000	270,000
Other	<u>85,000</u>	<u>85,000</u>
	<u>4,380,000</u>	<u>4,380,000</u>
Operating Income	<u>2,620,000</u>	<u>2,620,000</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>\$ 2,237,000</u>	<u>\$ 2,237,000</u>

ABC Corporation
Consolidated Cash Flow Statement
For the Year Ended December 31, 2010

	FASB 13 (Current)	ASC840 (Proposed)
Operating Activities		
Net income	\$ 2,237,000	\$ 2,237,000
Items not requiring (providing) cash		
Depreciation	50,000	50,000
Amortization of right to use assets	-	220,000
Changes in		
Accounts receivable	(850,000)	(850,000)
Inventories	(500,000)	(500,000)
Accounts payable and accrued expenses	(627,017)	(627,017)
Net cash provided by operating activities	<u>200,000</u>	<u>420,000</u>
Investing Activities		
Purchase of property and equipment	<u>(50,000)</u>	<u>(50,000)</u>
Net cash used in investing activities	<u>(50,000)</u>	<u>(50,000)</u>
Financing Activities		
Cash payments for leases	<u>-</u>	<u>(220,000)</u>
Net cash used in financing activities	<u>-</u>	<u>(220,000)</u>
Increase in Cash and Cash Equivalents	150,000	150,000
Cash and Cash Equivalents, Beginning of Year	<u>85,000</u>	<u>85,000</u>
Cash and Cash Equivalents, End of Year	<u>\$ 235,000</u>	<u>\$ 235,000</u>
Supplemental Cash Flows Information		
Interest paid on long-term debt	\$ 246,000	\$ 246,000
Initial recognition of right to use asset and associated liability	\$ -	\$ 440,000

ABC Corporation
Consolidated Cash Flow Statement
For the Year Ended December 31, 2010

Note X: Lease Accounting

Amounts Recognized in the Financial Statements

The Company entered into a lease on July 1, 2010 for 20,000 square feet of space for a one year term with no renewal options.

Depreciation and amortization expense includes \$220,000 of amortization of the right to use asset.

The facility is amortized on a straight line basis over the one year life. 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 Use Asset	Lease Liability
Beginning balance	\$ -	\$ -
Recognition of present value of lease payments	440,000	(440,000)
Amortization of the right to use asset	(220,000)	
Cash payments	-	222,000
Ending balance	\$ 220,000	\$ (220,000)

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

Future minimum lease payments at December 31, 2010, were \$220,000 for 2011.