

Interpretation of the Emerging Accounting Issues Working Group

INT 02-15: EITF 00-11: Lessors' Evaluation of Whether Leases of Certain Integral Equipment Meet the Ownership Transfer Requirements of FASB Statement 13

ISSUE NULLIFIED BY SSAP NO. 22

INT 02-15 Dates Discussed

June 9, 2002; September 10, 2002

INT 02-15 References

SSAP No. 22—Leases (SSAP No. 22)

INT 02-15 Issue

1. Paragraph 2 of *FASB Interpretation No. 43, Real Estate Sales* (FIN 43) states that *FASB Statement No. 66, Accounting for Sales of Real Estate* (FAS 66), "...applies to all sales of real estate, including real estate with property improvements or integral equipment". Some have interpreted that guidance to mean that integral equipment (as defined in FIN 43) should be considered real estate for other accounting evaluations outside the scope of FAS 66, including, for example, lease accounting evaluations. For any lease of real estate to be classified as a sales-type lease by the lessor, paragraph 7.a. of *FASB Statement No. 13, Accounting for Leases* (FAS 13) must be met. Paragraph 7.a. of FAS 13 (as amended by *FASB Statement No. 98, Accounting for Leases*) states:

The lease transfers ownership of the property to the lessee by the end of the lease term. . . .*

*This criterion is met in situations in which the lease agreement provides for the transfer of title at or shortly after the end of the lease term in exchange for the payment of a nominal fee, for example, the minimum required by statutory regulation to transfer title. [Emphasis added.]

2. In the United States, real property (land and buildings) transfers are addressed in state law. Recording a document of transfer in local land records evidences transfer of ownership of real property. Transfers of personal property (tangible, moveable goods) are addressed in Article 2 of the Uniform Commercial Code (U.C.C.). Although Article 2 of the U.C.C. provides a set of guidelines for determining when title to personal property has passed, there is generally no system for recording or registering title. Fixtures are a hybrid form of property, defined as personal property that is closely associated with the real property to which it is attached. Transfers of fixtures without the concurrent transfer of the underlying real property may not be subject to either a statutory title registration system or Article 2 of the U.C.C.

3. The issues are:

Issue 1—Whether integral equipment subject to a lease should be evaluated as real estate under Statement 13

Issue 2—If integral equipment subject to a lease is evaluated as real estate under FAS 13, how the requirement in paragraph 7.a. of FAS 13 for the transfer of ownership should be evaluated when no statutory title registration system exists for the leased assets.

INT 02-15 Discussion

4. The working group reached a consensus to adopt the consensus positions of EITF 00-11, *Lessors' Evaluation of Whether Leases of Certain Integral Equipment Meet the Ownership Transfer Requirements of FASB Statement 13* with certain modifications for GAAP references and its effective date as follows:

a. Issue 1 – Integral equipment subject to a lease should be evaluated as real estate under SSAP No. 22. SSAP No. 22 was intended to conform the requirements of FAS 13 with respect to sales-type leases of real estate to the requirements of FAS 66 with respect to sales of real estate. In order to maintain that conformity, integral equipment should be evaluated as real estate for purposes of SSAP No. 22 (because *SSAP No. 77—Real Estate Sales – An Amendment to SSAP No. 40, Real Estate Investments* defines integral equipment as real estate for purposes of *SSAP No. 40—Real Estate Investments*).

b. Issue 2 – Integral equipment or property improvements for which no statutory title registration system exists, the criterion in SSAP No. 22 (that the lease transfers ownership of the property to the lessee by the end of the lease term) is met in lease agreements that provide that, upon the lessee's performance in accordance with the terms of the lease, the lessor shall execute and deliver to the lessee such documents (including, if applicable, a bill of sale for the equipment) as may be required to release the equipment from the lease and to transfer ownership thereto to the lessee. This criterion is also met in situations in which the lease agreement requires the payment by the lessee of a nominal amount (for example, the minimum fee required by statutory regulation to transfer ownership) in connection with the transfer of ownership. Notwithstanding the foregoing guidance, a provision in a lease agreement that ownership of the leased property is not transferred to the lessee if the lessee elects not to pay the specified fee (whether nominal or otherwise) to complete the transfer of ownership is a purchase option. Such a provision would not satisfy SSAP No. 22.

c. The consensuses in this Interpretation should be applied to (a) leases for which lease inception occurs after January 1, 2003, and (b) leases modified after January 1, 2003, that meet the criteria in paragraph 9 of FAS 13 to be considered as new agreements. Companies shall disclose the effect on the balance sheet and the income statement resulting from a change in lease classification under (b), above, for leases that at inception would have been classified differently had the guidance in this Issue been in effect at the inception of the original lease.

INT 02-15 Status

5. No further discussion planned.