

Leases (Topic 842) – Land Easement Practical Expedient for Transition to Topic 842

FASB Accounting Standards Update No. 2018-01 (Issue Date: January 2018)

[Link to Standard: Update No. 2018-01](#)

Overview

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-01, *Land Easement Practical Expedient for Transition to Topic 842*, in January 2018.

To assist entities with the transition to the new standard, the FASB issued a practical expedient for existing or expired easements not previously accounted for as leases under ASC 840. This update provides entities with the option to not evaluate existing or expired land easements under ASC 842 that were not previously accounted for as leases under current lease guidance in ASC 840. If an entity chooses to elect the optional practical expedient for transition, it will begin evaluating new or modified land easements under ASC 842 at the time of adoption. Conversely, if an entity does not elect this practical expedient, it will need to evaluate all existing or expiring land easements to determine whether they meet the definition of a lease.

Background

This update amends both ASC Topic 350, *Intangibles – Goodwill and Other*, and Topic 842, *Leases*. ASC 842 was issued in February 2016 to increase transparency and comparability among entities by requiring the recognition of a right-of-use asset and a lease liability for each lease, where appropriate. Stakeholders noted the diversity in accounting policies currently used to treat land easements and inquired about how land easements should be accounted for under the new lease requirements in ASC 842. Land easements, which the FASB has defined as “the right to use, access, or cross another entity’s land for a specified purpose,” are not currently accounted for in a consistent manner. For example, some companies treat prepaid land easements as costs incurred to bring the related asset to the condition necessary for its intended use under Subtopic 360-10, while other companies point to Subtopic 350-30 as guidance to account for land easements as intangible assets. The amendments in this update clarify that before an entity accounts for a land easement as an intangible asset under ASC 350, it must first apply the framework in ASC 842 to determine if the land easement is or contains a lease.

Entities that do not currently apply ASC 840 to account for land easements voiced confusion about whether they should evaluate existing and future land easements under ASC 842 upon adoption of that topic. These stakeholders also noted the high cost and complexity of evaluating all existing land easements under ASC 842. Additionally, many stakeholders noted that many of their easements are prepaid and, thus, are already recognized on the balance sheet. The FASB issued the amendments in this update to help alleviate some of the stakeholder concerns and confusion regarding the accounting treatment for land easements. By giving companies the option to elect the practical expedient, the FASB is allowing companies to continue with their current methods of accounting for land easements prior to adopting ASC 842. However, once a company

does adopt ASC 842, it must then evaluate all new or modified land easements to determine whether they meet the definition of a lease under ASC 842. Entities that decline the optional practical expedient should evaluate all existing and expired land easements under the standard to assess whether they are or contain leases.

Even though an entity may elect the optional practical expedient prior to adopting ASC 842, upon adoption it must apply the new guidance prospectively to all new or modified land easements. Prior to applying the lease evaluation framework, an entity should first determine the unit of account for land easements. In other words, first determine the number of unique land easement arrangements that exist. If more than one unit of account is identified, each unit will be evaluated separately to determine whether it constitutes a lease. Once the unit of account has been determined, an entity will then determine if the land easement should be accounted for under ASC 842, or if it would fall outside its scope. Under the new standard, to qualify as a lease, a land easement must convey the right to control an identified asset for a specified period of time. As such, land easements that provide for perpetual use rights would not qualify as a lease under the new guidance as the time is not specified. Leases of intangible assets are accounted for under guidance in ASC 350.

Insights

Many stakeholders noted that the cost of evaluating existing land easements under ASC 842 would exceed the expected benefits. Because many land easements are prepaid, they are already recognized on the balance sheet. Additionally, entities pointed out that many of their land easements do not meet the definition of a lease, limiting the benefits of applying the new lease standard requirements to existing land easements. Because of the cost and complexity associated with evaluating all existing land easements under ASC 842, we expect that many entities will find it beneficial to elect the optional practical expedient provided by the amendments in this update.

By electing the optional practical expedient, entities can save time and effort by continuing to use existing accounting methods for land easements until the time of adopting ASC 842. This allows entities to prepare and put in place the framework for assessing land easements under the new standard, once adopted. Entities that have early adopted the amendments must also adopt the amendments in this update upon issuance. As such, these entities must immediately assess whether all existing or land easements should be accounted for as leases under ASC 842.



Final Thoughts

Entities should apply the amendments in this Update in unison with the adoption of ASC 842, with the effective dates listed below for both public and non-public entities. Entities that early adopted the standard should apply the amendments in this Update upon issuance.

	<u>Effective Date</u>	
	<u>Public Entity</u>	<u>Non-Public Entity</u>
Interim Periods	Beginning after December 15, 2018	Beginning after December 15, 2020
Early adoption is permitted if financial statements were not issued.		
Annual Periods	Beginning after December 15, 2018	Beginning after December 15, 2019
Early adoption is permitted if financial statements were not made previously available for issuance.		



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