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Contracts on an Entity's Own Equity
Convertible Debt
Current Expected Credit Losses
Debt
Distinguishing Liabilities From Equity
Earnings per Share
Environmental Obligations and Asset Retirement Obligations
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Equity Method Investees — SEC Reporting Considerations
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Non-GAAP Financial Measures and Metrics
Revenue Recognition
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Preface

The life sciences ecosystem encompasses a wide array of entities that discover, develop, and manufacture health care products. Such entities include pharmaceutical manufacturers; biotechnology companies; medical device, diagnostic, and equipment manufacturers; and service companies such as drug distributors, contract research organizations (CROs), contract manufacturing organizations (CMOs), and health technology companies.

Finance and accounting professionals in the industry face complex issues and must exercise significant judgment in applying existing rules to matters such as research and development (R&D) costs, acquisitions and divestitures, consolidation, contingencies, revenue recognition, income taxes, financial instruments, and financial statement presentation and disclosure. The 2021 edition of Deloitte’s Life Sciences Industry Accounting Guide (the “Guide”) addresses these and other relevant topics affecting the industry this year. It includes interpretive guidance, illustrative examples, recent standard-setting developments (through February 28, 2021), and key differences between U.S. GAAP and IFRS® Standards. In addition, this Guide discusses accounting and financial reporting considerations associated with the coronavirus disease 2019 (“COVID-19”) pandemic that apply specifically to the life sciences industry.

Appendix B lists the titles of standards and other literature we cited, and Appendix C defines the abbreviations we used.

We hope this Guide is helpful in navigating the various accounting and reporting challenges that life sciences entities face. We encourage clients to contact their Deloitte team for additional information and assistance.
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Chapter 11 — Leases

11.1 New Leasing Standard (Codified in ASC 842)

11.1.1 Background

In February 2016, the FASB issued ASU 2016-02 (the “new leasing standard,” which, as subsequently amended, is codified in ASC 842). The primary objective of the new standard was to address the off-balance-sheet financing concerns related to lessees’ operating leases. Accordingly, except for those leases that qualify for the short-term lease exemption under ASC 842 (i.e., certain leases with a lease term of 12 months or less), the standard’s lessee model requires lessees to adopt a right-of-use (ROU) asset approach that brings substantially all leases onto the balance sheet. Under this approach, a lessee records an ROU asset representing its right to use the underlying asset during the lease term and a corresponding lease liability in a manner similar to the current approach for capital leases.

The FASB also addressed questions such as:

- Whether an arrangement is a service or a lease.
- What amounts should be initially recorded on the lessee’s balance sheet for the arrangement.
- How to reflect the effects of leases in the statement of comprehensive income.
- How to apply the resulting accounting in a cost-effective manner.

The standard also aligns certain underlying principles of the new lessor model with those in ASC 606, the FASB’s new revenue recognition standard, including those related to the evaluation of how collectibility should be considered and the determination of when profit should be recognized.

11.1.2 Scope

The new leasing standard applies to leases, including subleases, of all property, plant, and equipment (PP&E). It does not apply to leases of or for the following:

- Intangible assets.
- Exploration for or use of minerals, oil, natural gas, and similar nonregenerative resources.
- Biological assets.
- Inventory.
- Assets under construction.
11.1.3 Definition of a Lease

The new leasing standard states that a contract is or contains a lease if the contract gives a customer “the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration.” Control is considered to exist if the customer has both of the following:

- “The right to obtain substantially all of the economic benefits from use of [an] identified asset.”
- “The right to direct the use of the identified asset.”

An entity is required at inception to identify whether a contract is or contains a lease. The entity will reassess whether the contract is or contains a lease only in the event of a modification to the terms and conditions of the contract.

The table below summarizes key concepts related to the definition of a lease.

<table>
<thead>
<tr>
<th>Concept</th>
<th>Requirement</th>
<th>Observation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Use of an identified asset</td>
<td>An asset is typically considered to be an identified asset if it is explicitly specified in a contract or implicitly specified at the time the asset is made available for use by the customer. However, if the supplier has substantive rights to substitute the asset throughout the period of use and would benefit economically from substituting that asset, the asset is not considered “identified,” and there is no lease for accounting purposes (see below).</td>
<td>This requirement is similar to the guidance in ASC 840-10-15 (formerly EITF Issue 01-8). An entity does not need to be able to identify the particular asset (e.g., by serial number) but must instead determine whether an identified asset is needed to fulfill the contract. Distinguishing between a lease and a capacity contract requires significant judgment. The standard clarifies that a capacity portion of an asset is an identified asset if it is physically distinct (e.g., a specific floor of a building). On the other hand, a capacity portion of a larger asset that is not physically distinct (e.g., a percentage of a pipeline) is not an identified asset unless that portion represents substantially all of the asset’s capacity.</td>
</tr>
</tbody>
</table>
| Substantive substitution rights| A supplier’s right to substitute an asset is substantive only if both of the following conditions exist:  
  - The supplier has the practical ability to substitute alternative assets throughout the period of use.  
  - The supplier would benefit economically from the exercise of its right to substitute the asset. | The FASB established this requirement because it reasoned that if a supplier has a substantive right to substitute the asset throughout the period of use, the supplier — not the customer — controls the use of the asset. It is often difficult for a customer to determine whether a supplier’s substitution right is substantive. A customer should presume that a substitution right is not substantive if it is impractical to prove otherwise. |
(Table continued)

<table>
<thead>
<tr>
<th>Concept</th>
<th>Requirement</th>
<th>Observation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Right to obtain economic benefits from use of the identified asset</td>
<td>To control the use of an identified asset, a customer must have the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use. The term &quot;substantially all&quot; is generally 90 percent of the economic benefits of the asset.</td>
<td>The economic benefits from use of an asset include the primary output and by-products of the asset as well as other economic benefits from using the asset that could be realized from a commercial transaction with a third party.</td>
</tr>
<tr>
<td>Right to direct the use of the identified asset</td>
<td>A customer has the right to direct the use of an identified asset throughout the period of use if either of the following conditions exists: • The customer has the right to direct &quot;how and for what purpose&quot; the asset is used throughout the period of use. • The relevant decisions about how and for what purpose the asset is used are predetermined and (1) the customer has the right to operate (or direct others to operate) the asset throughout the period of use and the supplier does not have the right to change the operating instructions or (2) the customer designed the asset in a way that predetermines how and for what purpose the asset will be used.</td>
<td>The relevant rights to be considered are those that affect the economic benefits derived from the use of the asset. Customers' rights to direct the use of the identified asset include the rights to change: • The type of output produced by the asset. • When the output is produced. • Where the output is produced. On the other hand, rights that are limited to maintaining or operating the asset do not grant a right to direct how and for what purpose the asset is used.</td>
</tr>
</tbody>
</table>

### 11.1.4 Embedded Leases

Often, the assessment of whether a contract is or contains a lease will be straightforward. However, the evaluation will be more complicated when an arrangement involves both a service component and a leasing component or when both the customer and the supplier make decisions about the use of the underlying asset. An asset typically is identified by being explicitly specified in a contract. However, an asset also can be identified by being implicitly specified at the time the asset is made available for the customer's use.

**Connecting the Dots**

As discussed further in Chapter 16 of Deloitte's *A Roadmap to Applying the New Leasing Standard* ("Leasing Roadmap"), entities in transition to ASC 842 may elect a package of transition relief (commonly referred to as "the package of three") that, among other things, permits entities to retain historical assessments of whether contracts are or contain a lease. This means that on the effective date of the standard, for those contracts existing as of the date of adoption, the initial ASC 842 accounting is based on those contracts that meet the definition of a lease under ASC 840. Therefore, if entities elect the transition relief package, they should evaluate embedded leases that may not have been identified under legacy U.S. GAAP in accordance with ASC 840. If entities do not elect the transition relief package, they should evaluate whether contracts are or contain leases under ASC 842.
The following flowchart illustrates how to evaluate whether an arrangement is or contains a lease:

1. Start
2. Does the contract depend on the use of an identified asset? (Yes/No)
   - Yes: Go to 3.
   - No: Go to 5.
3. Does the customer have the right to obtain substantially all the economic benefits from use? (Yes/No)
   - Yes: Go to 4.
   - No: Go to 5.
4. Who has the right to direct how and for what purpose the asset is used? (Customer/Supplier/Neither)
   - Customer: Go to 6.
   - Supplier: Go to 7.
   - Neither: Go to 5.
5. Contract does not contain a lease.
6. Did the customer design the asset? (Yes/No)
   - Yes: Contract contains a lease.
   - No: Go to 7.
7. Did the customer have the right to operate the asset? (Yes/No)
   - Yes: Contract contains a lease.
   - No: Go to 5.

Flowchart: [Diagram of the flowchart with decision points and outcomes]
Example 11-1

Contract Manufacturing Arrangement

Entity A, a pharmaceutical company, enters into an arrangement with a contract manufacturer, Entity B, to purchase a particular type, quality, and quantity of active pharmaceutical ingredient (API) needed to manufacture drug compound X. Entity B has only one factory that can meet the requirements of the contract with A, and B is prohibited from supplying A through another factory or third-party suppliers. Entity A has not contracted for substantially all of B’s factory’s capacity.

The required quantities of API are established in the contract at inception. Entity B makes all of the decisions about the factory’s operations, including when to run the factory to satisfy the required quantities and which customer orders to fulfill.

The contract does not contain a lease. The factory is an identified asset because it is implicit that B can fulfill the contract only through the use of the specific factory. However, A does not have the “right to obtain substantially all of the economic benefits from use of [an] identified asset” since the amount of capacity A has contracted for does not represent substantially all of the factory’s capacity. In addition, A does not have the “right to direct the use of the identified asset.” While A may specify quantities of product, B has the right to direct the factory’s use because it can determine when to run the factory and which customer contracts to fulfill. As a result, A does not meet the new leasing standard’s criterion of directing “how and for what purpose” the factory is being used, and the arrangement does not contain a lease.

Q&A 11-1 Determining Whether a Service Arrangement Contains a Lease

Question
Does an entity need to evaluate a service arrangement that involves the use of PP&E to determine whether the arrangement contains a lease?

Answer
Yes. In accordance with ASC 842-10-15-2, an entity is required at contract inception to identify whether a contract contains a lease. Not all contracts that contain accounting leases will be labeled as such, and accounting leases may be embedded in larger service arrangements.

Failure to identify accounting leases, including those embedded in service arrangements, could lead to a financial statement error. On the other hand, if a customer concludes that a contract is a service arrangement and that contract does not contain an embedded lease, the customer is not required to reflect the contract on its balance sheet (unless required to do so by other U.S. GAAP). The outcome of the accounting assessment of the contract may be more material to the financial statements under ASC 842 than under ASC 840 since the impact of operating leases on the financial statements is often the same as that of service arrangements under ASC 840.

Connecting the Dots
Historically, the accounting for operating leases under ASC 840 has generally not been materially different from the accounting for service contracts. However, under ASC 842, since most leases will be recognized on the balance sheet, the financial statement implications of not identifying a lease in a service contract could be more significant than under ASC 840.
For example, under ASC 840, “placed equipment” by a medical device entity may not have represented an identified asset if it was demonstrated that substitution rights existed, which could result in a conclusion that the placed equipment did not represent a lease. Under ASC 842, however, for a medical device entity to conclude that it has a substantive substitution right, it would have to demonstrate not only that it has the practical ability to substitute the placed equipment but also that it would benefit economically from the exercise of its right to substitute the asset. As a result, it is possible that more arrangements that allow for placed equipment will represent an identified asset under ASC 842.

### Example 11-2

**Placement of Medical Device With Sale of Consumables**

Entity C is a medical device manufacturer that supplies diagnostic kits to customers. The kits can be used only on instruments manufactured by C. Entity C provides its customers with the right to use its instruments at no separate cost to the customer in exchange for a multiyear agreement to purchase annual minimum quantities of diagnostic kits. The term of the agreement generally corresponds to the expected useful life of the instruments. Entity C retains title to the instruments and is permitted to substitute them under the terms of the contract, although historically these instruments have been substituted only when they malfunction since C does not benefit economically from the exercise of its right to substitute the asset.

The multiyear agreement to purchase diagnostic kits contains an embedded lease for the instrument system. The instrument system is an identified asset because it is implicit that C can fulfill the contract only through the customers’ use of the specific instruments. Although C has the right to substitute the instruments, the substitution right is not substantive because of the lack of economic benefit from doing so. In addition, customers have the right to control the instruments’ use because they have the right to obtain substantially all of the economic benefits from the use of the instruments during the multiyear term of the contract, which corresponds to the useful life of the instruments. Further, customers can make decisions about how and when the instruments are used when the customers perform diagnostic testing procedures.

### 11.1.5 Components of a Contract

A contract can contain both lease and nonlease components. Generally, the nonlease components are services that the supplier is also performing for the customer. For example, in a single contract, the supplier could be leasing a lab facility and related laboratory equipment to a biotechnology customer while also agreeing to provide ongoing maintenance services for the equipment throughout the period of use. Contracts may contain multiple lease components (e.g., leases of land, buildings, and equipment).

The graphic below outlines steps related to considering how to separate, and allocate consideration to, components in a contract under ASC 842.
Once an entity (a customer or supplier) determines that a contract is or contains a lease (i.e., part or all of the contract is a lease), the entity must assess whether the contract contains multiple lease components (i.e., when the contract conveys the rights to use multiple underlying assets). ASC 842-10-15-28(a) and (b) prescribe criteria for identifying whether one lease component is considered separate from other lease components in the contract.

However, land is considered an exception to the guidance in ASC 842-10-15-28. ASC 842-10-15-29 requires an entity to separate a right to use land from the rights to use other underlying assets (e.g., from the right to use a building that sits on top of the land) unless the effect of separating the land is insignificant to the resulting lease accounting.

**Connecting the Dots**

The new leasing standard indicates that it is important for an entity to identify the appropriate unit of account when applying the lessee or lessor accounting model since the unit of account can affect the allocation of consideration to the components in the contract. Paragraph BC145 of ASU 2016-02 states, in part:

> By way of example, regarding allocation, the Board noted that the standalone price (observable or estimated) for a bundled offering (for example, the lease of a data center) may be substantially different from the sum of the standalone prices for separate leases of the items within a bundled offering (for example, the lease of each asset in the data center). Given the substantially different accounting for lease and nonlease components in Topic 842, the allocation of contract consideration carries additional importance as compared with previous GAAP. Consequently, the Board concluded that including separate lease components guidance in Topic 842 will result in more accurate accounting that also is more consistent among entities.

The decision tree on the following page illustrates how an entity might think about identifying lease and nonlease components for each contract containing a lease.
The contract is, or contains, a lease.

Does the contract convey multiple rights of use (i.e., the rights to use multiple assets)?

Yes

Does the contract convey a right to use land along with the other assets?

Yes

Would the effect of accounting for the right to use land as a separate lease component be insignificant?

Yes

Can the customer benefit from the right of use on its own or together with other readily available resources?

No

Combine two or more rights of use and reevaluate the new bundle.

No

Account for the right of use as a separate lease component.

Yes

Evaluate each right of use (or bundle of rights of use) for separation from the other rights of use.

No

Separate the right to use land from the other rights of use. Continue evaluating the rights to use the other assets.

No

Do not separate the right to use land. Include the land when evaluating the rights to use the other assets.

No

Assess whether the contract contains any nonlease components.
Once the separate lease components are identified, entities must determine whether there are any nonlease components to be separated. An allocation of contract consideration is required for both lease and nonlease components since they transfer a good or service to the customer. However, allocation of contract consideration does not extend to activities that do not transfer a good or service to the customer, which are referred to as “noncomponents” (e.g., administrative tasks and reimbursement or payment of the lessor’s costs).

Understanding the difference between lease components, nonlease components, and noncomponents is critical. The table below outlines these concepts in greater detail.

| Lease Component | The right to use an underlying asset is considered a separate lease component if (1) a lessee can benefit from the use of the underlying asset either on its own or with other resources that are readily available and (2) the underlying asset is not highly dependent on or highly interrelated with other assets in the arrangement. |
| Nonlease Component | An activity that transfers a separate good or service to the customer is a nonlease component. For example, maintenance services consumed by the customer and bundled with the lease component in the contract would be a separate nonlease component because the performance of the maintenance transfers a service to the customer that is separate from the right to use the asset. |
| Noncomponent | Any activity in a contract that does not transfer a separate good or service to the lessee is neither a lease component nor a nonlease component; therefore, consideration in the contract would not be allocated to such an activity. For example, payments made by the customer for property taxes or insurance that covers the supplier’s interests would not represent a component in the contract. |

ASC 842 affords lessees a practical expedient related to separating (and allocating consideration to) lease and nonlease components. That is, lessees may elect to account for the nonlease components in a contract as part of the single lease component to which they are related. The practical expedient is an accounting policy election that must be made by class of underlying asset (e.g., vehicles, information technology [IT] equipment — see the Connecting the Dots discussion below). Accordingly, when a lessee elects the practical expedient, any portion of consideration in the contract that would otherwise be allocated to the nonlease components will instead be accounted for as part of the related lease component for classification, recognition, and measurement purposes. In addition, any payments related to noncomponents would be accounted for as part of the related lease component (i.e., the associated payments would not be allocated between the lease and nonlease components).

In addition to the practical expedient available to lessees, lessors can elect not to separate lease and nonlease components. This election is made by each class of underlying asset and can only be made if certain criteria are met. Specifically, a lessor can elect to combine a lease component with a nonlease component provided that (1) the timing and pattern of transfer for the lease component are the same as those for the nonlease component associated with that lease component and (2) the lease component would be classified as an operating lease if accounted for separately from the nonlease component. See ASU 2018-11 and Section 4.3.3.2 of Deloitte’s Leasing Roadmap for more information.
At this point, entities have identified their separate lease and nonlease components to which consideration in the contract will be allocated. Noncomponents have also been identified to ensure that consideration in the contract is not allocated to them. Next, entities must:

- Determine the consideration in the contract.
- Allocate the consideration in the contract to the separate lease and nonlease components.

**Example 11-3**

**Accounting for an Embedded Lease With Lease and Nonlease Components**

Entity A, a pharmaceutical company, enters into an arrangement with Entity B, a contract manufacturing organization, to produce a drug substance by using a dedicated production line designed specifically for the exclusive use of A. Assume that key operating decisions are predetermined by A and that A must approve any changes to production plans.

This arrangement is likely to contain a lease accounted for under ASC 842. The production line is an explicitly identified asset in the contract, there are no substitution rights, and A has the right to obtain substantially all of the economic benefit from the use of the identified asset. In addition, A directs the use of the identified asset because B does not have the right to make operating decisions without A’s prior approval.

As a result, A should allocate the expected consideration between the leased production line (the lease component) and the services required to produce the drug substance (the nonlease component) on the basis of their relative stand-alone selling prices at the inception of the contract. If the arrangement includes fixed consideration (including minimum monthly volumes at fixed prices), A would record on its balance sheet (1) a lease liability at the present value of the amount of fixed consideration allocated to the lease and (2) a corresponding ROU asset. If the contract contains no minimum volumes, the arrangement would still contain an embedded lease, but the consideration would be 100 percent variable. Because variable consideration is excluded from the measurement of the lease liability, there would be no initial accounting for this agreement. Instead, A would allocate and record a portion of each payment as variable lease expense for the embedded lease component and a portion as the cost of the contract manufacturing. Alternatively, A may elect to use the practical expedient in ASC 842 of not separating the lease component from the nonlease component and accordingly may account for the consideration in the arrangement entirely as lease expense.

**Connecting the Dots**

ASC 842 provides lessees with the following two practical expedients that may be elected as an accounting policy by “class of underlying asset”:

- ASC 842-10-15-37 allows lessees not to separate lease and nonlease components.
- ASC 842-20-25-2 allows lessees not to recognize lease liabilities and ROU assets for short-term leases (i.e., leases with a term of 12 months or less).
However, ASC 842 does not address what is meant by the phrase “class of underlying asset.” We have received a number of questions about this topic from various stakeholders, and two views have emerged:

- **View 1** — The class of underlying asset is determined on the basis of the physical nature and characteristics of the asset. For example, real estate, manufacturing equipment, and vehicles would all be reasonable classes of underlying assets given their differences in physical nature. Therefore, irrespective of whether there are different types of similar assets (e.g., within the real estate class, there may be retail stores, warehouses, and distribution centers), the class of underlying asset would be limited to the physical nature as described above.

- **View 2** — The class of underlying asset is determined on the basis of the risks associated with the asset. While an asset's physical nature may be similar to that of other assets (e.g., retail stores, warehouses, and distribution centers are all real estate, as discussed above), each has a different purpose and use to the lessee and would therefore have a separate risk profile. Therefore, for example, it could be appropriate for the lessee to disaggregate real estate assets into separate asset classes by “type” of real estate — to the extent that the different types are subject to different risks — when applying the practical expedients in ASC 842-10-15-37 and ASC 842-20-25-2.

To support their position, proponents of View 2 refer to paragraph BC341 of ASU 2016-02, which states:

> The Board decided that a lessor should treat assets subject to operating leases as a major class of depreciable assets, further distinguished by significant class of underlying asset. Accordingly, a lessor should provide the required property, plant, and equipment disclosures for assets subject to operating leases separately from owned assets held and used by the lessor. In the Board's view, leased assets often are subject to different risks than owned assets that are held and used (for example, the decrease in the value of the underlying asset in a lease could be due to several factors that are not within the control of the lessor), and, therefore, users will benefit from lessors segregating their disclosures related to assets subject to operating leases from disclosures related to other owned property, plant, and equipment. The Board further considered that to provide useful information to users, the lessor should disaggregate its disclosures in this regard by significant class of underlying asset subject to lease because the risk related to one class of underlying asset (for example, airplanes) may be very different from another (for example, land or buildings). [Emphasis added]

Views on these questions are still developing. Therefore, we recommend that entities with concerns about such matters discuss them with their accounting advisers.

Irrespective of the views noted above, we do not think that it would be appropriate to determine the “class of underlying asset” on the basis of the lease contract with which it is associated. For example, we believe that it would be inappropriate to break real estate assets into different classes on the basis of whether they are related to gross leases or triple net leases. In that situation, the asset underlying the contract could be the same while the contract terms differ. We do not believe that such an approach is consistent with the intent of the guidance in ASC 842-10-15-37 or ASC 842-20-25-2.
**11.1.6 Lease Classification — Lessee**

Under ASC 842, at lease commencement, a lease is classified as a finance lease (for a lessee) or a sales-type lease (for a lessor) if any of the following criteria are met:

- “The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.”
- “The lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise.”
- “The lease term is for the major part of the remaining economic life of the underlying asset.”
- “The present value of the sum of the lease payments and any residual value guaranteed by the lessee . . . equals or exceeds substantially all of the fair value of the underlying asset.”
- “The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.”

Finance leases are accounted for in a manner similar to how entities account for a financed purchase arrangement. The lessee recognizes interest expense and amortization of the ROU asset, which result in a greater expense in the early years of the lease than in the later years of the lease. The single lease cost related to an operating lease is recognized on a straight-line basis over the lease term unless another systematic and rational basis is more representative of the pattern in which benefit is expected to be derived from the right to use the underlying asset. Thus, the amortization of an ROU asset related to an operating lease takes into account the interest on the liability so that the expense amount remains constant. That is, the amortization of the ROU asset will increase or decrease proportionally to the change in interest expense on the liability to maintain a straight-line expense throughout the term of the lease. For both types of leases, the lessee recognizes an ROU asset for its interest in the underlying asset and a corresponding lease liability.

**Connecting the Dots**

While many aspects of the lease classification criteria under ASC 842 are consistent with legacy lease accounting guidance, bright-line tests (i.e., whether the lease term is for 75 percent or more of the remaining economic life of the asset or whether the present value of the lease payments, including any guaranteed residual value, is at least 90 percent of the fair value of the underlying asset) are noticeably absent. However, ASC 842-10-55-2 states that these tests are “one reasonable approach to assessing the criteria.” On the basis of this implementation guidance, entities often can use bright-line thresholds as policy elections when evaluating the classification of a lease arrangement under the new leasing standard. However, as with all policy elections, it is important for entities to consider the full range of impact and the need for policy elections to be consistently applied.

**11.1.7 Lessor Accounting**

After proposing different amendments to lessor accounting, the FASB ultimately decided to make only minor modifications to the lessor model. The most significant changes (1) align the profit recognition requirements under the lessor model with the new revenue standard and (2) amend the lease classification criteria for a lessor to make them consistent with those for a lessee. Accordingly, the new leasing standard requires a lessor to use the classification criteria discussed above to classify a lease, at its commencement, as a sales-type, direct financing, or operating lease.
Regarding leveraged leases (i.e., leases that met the criteria in ASC 840-10-25-43(c)), paragraph BC397 of ASU 2016-02 explains that the FASB decided to grandfather in existing leveraged leases given that “there would be significant complexities relating to unwinding existing leveraged leases” during transition. Therefore, a lessor must continue to apply the accounting in ASC 840 for such a lease (as carried forward in ASC 842) and classify the lease as a leveraged lease provided that it enters into the lease before the effective date of ASC 842. Otherwise, leveraged lease accounting is eliminated as of the date of adoption.

**Q&A 11-2 Commencement Loss Resulting From Significant Variable Payments in a Sales-Type or Direct Financing Lease**

While the FASB's goal was to align lessor accounting with the revenue guidance in ASC 606, an important distinction between the two may affect lessors in the life sciences industry. Under ASC 606, variable payments are estimated and included in the transaction price subject to a constraint. By contrast, under ASC 842, variable lease payments not linked to an index or rate are generally excluded from the determination of a lessor's lease receivable. Accordingly, sales-type or direct financing leases that have significant variable lease payments may result in recognition of a loss at commencement because the measurement of the lease receivable plus the unguaranteed residual asset is less than the net carrying value of the underlying asset.

For example, it is not uncommon for a hospital to contract with a medical device owner for the use of specific medical equipment for a major part of the economic life of the equipment. This type of arrangement is often priced in such a way that the consideration is based entirely on the hospital's ongoing purchase of “consumables,” which allow the equipment to function as designed, and may have no minimum volume requirement. The medical device owner is willing to accept variable consideration in the arrangement because demand for the associated healthcare services suggests that a sufficient volume of consumables will be purchased by the hospital over the term of the contract to make the arrangement profitable.

**Question**

Should a lessor recognize a loss at lease commencement when its initial measurement of the net investment in a sales-type or direct financing lease is less than the carrying value of the underlying asset?

**Answer**

Yes. At the FASB's November 30, 2016, meeting, the Board acknowledged that a lessor's initial measurement of a sales-type or direct financing lease that includes a significant variable-lease payment component may result in a loss at lease commencement if the lease receivable plus the unguaranteed residual asset is less than the net carrying value of the underlying asset being leased. The Board discussed whether a loss at commencement would be appropriate in these situations or whether other possible approaches would be acceptable, such as (1) incorporating variable lease payments subject to a constraint (by reference to ASC 606) or (2) using a negative discount rate to avoid the loss at commencement. The Board expressed its belief that while stakeholders may disagree with the outcome of recognizing a loss at commencement, the new leasing standard is clear on how the initial measurement guidance should be applied to sales-type and direct financing leases. In addition, the Board disagreed with the use of a negative discount rate, which it believed to be inappropriate under ASC 842.
In October 2020, the FASB issued for public comment an exposure draft (ED) of a proposed ASU that addresses this issue. In the ED, the FASB recommends that leases with predominantly variable payments be classified as operating leases. If finalized, this proposed guidance would result in accounting that more faithfully represents the economics of the transaction and would increase alignment of ASC 842 and IFRS 16. For more information, see Deloitte’s November 2, 2020, Heads Up.

11.1.8 Lease Modifications

A lease modification is any change to the contractual terms and conditions of a lease. Under the new leasing standard, a lease modification is accounted for as follows:

- A lessee or lessor accounts for a lease modification as a separate contract (i.e., separate from the original lease) when the modification (1) grants the lessee an additional ROU asset and (2) the price of the additional ROU asset is commensurate with its stand-alone price.

- A lessee accounts for a lease modification that is not a separate contract by using the discount rate as of the modification’s effective date to adjust the lease liability and ROU asset for the change in the lease payments. The modification may result in a gain or loss if the modification results in a full or partial termination of an existing lease.

- A lessor accounts for a lease modification in a manner that is generally consistent with the contract modification guidance in ASC 606.

Example 11-4

Lease Modifications

Scenario 1 — Modification Resulting in a Separate Contract

Company A, a pharmaceutical entity (the lessee), enters into an arrangement to lease 15,000 square feet of office space in a complex for 20 years. At the beginning of year 10, A and the lessor agree to amend the original lease to include an additional 5,000 square feet of space adjacent to the existing space currently being leased when the current tenant vacates the property in 18 months. The increase in lease consideration as a result of the amendment is commensurate with the market rate for the additional 5,000 square feet of space in the complex. Company A would account for this modification (i.e., the lease of the additional 5,000 square feet) as a separate contract because the modification provides A with a new ROU asset at a price that reflects that asset’s stand-alone price. While A would be required to disclose certain information about the lease modification, it would not be required to separately record any amounts in its statement of financial position until the separate lease’s commencement date (i.e., 18 months from entering into the modification).

Scenario 2 — Modification Not Resulting in a Separate Contract

Company A, a pharmaceutical entity (the lessee), enters into an arrangement to lease 15,000 square feet of office space in a complex for 20 years. At the end of year 10, A and the lessor agree to amend the original lease by reducing the annual rental payments from $60,000 to $50,000 for the remaining 10 years of the agreement. Because the modification results in a change only to the lease consideration (i.e., the modification does not result in an additional ROU asset), A would remeasure its lease liability to reflect (1) a 10-year lease term, (2) annual lease payments of $50,000, and (3) A’s incremental borrowing rate (or the rate the lessor charges the lessee if such rate is readily determinable) as of the modification’s effective date. Company A would recognize the difference between the new and old lease liabilities as an adjustment to the ROU asset. Since the modification does not result in a full or partial termination of the lease, there is no gain or loss on the modification.
Connecting the Dots

In response to the COVID-19 pandemic, the FASB provided both lessees and lessors with relief related to accounting for rent concessions resulting from COVID-19. An entity that elects to apply the relief to qualifying concessions may choose to account for the concessions by either (1) applying the modification framework for these concessions in accordance with ASC 840 or ASC 842 as applicable or (2) accounting for the concessions as if they were made under the enforceable rights included in the original agreement and are thus outside of the modification framework. See Section 11.1.12 for more information.

11.1.9 Subleases

When the original lessee subleases the leased asset to an unrelated third party, the lessee becomes the intermediate lessor in the sublease arrangement. As the intermediate lessor of a leased asset, the entity would determine the classification of the sublease independently from its determination of the classification of the original lease (i.e., the head lease). Under the new leasing standard, the intermediate lessor would classify the sublease on the basis of the underlying asset (i.e., it would assess the term of the sublease relative to the remaining economic life of the underlying asset). When evaluating lease classification and measuring the net investment in a sublease classified as a sales-type or direct financing lease, the original lessee (as a sublessor) should use the rate implicit in the lease if it is determinable. If the implicit rate is not determinable, the original lessee would use the discount rate that it used to determine the classification of the original lease.

In addition, offsetting is generally prohibited on the balance sheet unless the arrangement meets the offsetting requirements of ASC 210-20. However, it may be appropriate in certain instances to net sublease activity in the income statement. See Q&A 14-4 of Deloitte’s Leasing Roadmap for additional considerations related to when net presentation in the income statement may be appropriate.

Example 11-5

Accounting for a Sublease Under ASC 842

As a lessee, Company A, a life sciences entity, enters into a building lease with a 30-year term. The building has an estimated economic life of 40 years. At the end of year 5, A enters into an agreement with Company B, a generics and consumer health entity, under which A subleases the building to B for 20 years. There is no residual value guarantee, and A determines that the present value of the sublease payments received from B does not represent substantially all of the fair value of the building.

As the lessor in its agreement with B, A would account for the lease to B (the sublease) as an operating lease because (1) the term of the sublease is not for a major part of the remaining life of the underlying asset of the sublease (i.e., the sublease term of 20 years represents only 57 percent of the remaining 35-year life of the building) and (2) A has concluded that no other classification criteria would result in the transfer of control of the underlying asset.

11.1.10 Sale-and-Leaseback Transactions

The seller-lessee in a sale-and-leaseback transaction must evaluate the transfer of the underlying asset (sale) under the requirements of ASC 606 to determine whether the transfer qualifies as a sale (i.e., whether control has been transferred to the customer). The existence of a leaseback by itself would not preclude the transaction from qualifying as a sale (i.e., it would not indicate that control has not been transferred) unless the leaseback is classified as a finance lease. In addition, if the arrangement includes
an option for the seller-lessee to repurchase the asset, the transaction would not qualify as a sale unless both of the following criteria are met:

- The option is priced at the fair value of the asset on the date of exercise.
- There are alternative assets that are substantially the same as the transferred asset and readily available in the marketplace (see Q&A 11-3 below regarding sale-and-leaseback transactions involving real estate).

If the transaction does not qualify as a sale, the seller-lessee and buyer-lessee would account for the transaction as a financing arrangement (i.e., the buyer-lessee would account for its payment as a financial asset and the seller-lessee would record a financial liability).

If the transaction qualifies as a sale, the leaseback is accounted for in the same manner as all other leases (i.e., the seller-lessee and buyer-lessee would account for the leaseback under the new accounting guidance for lessees and lessors, respectively).

Transactions in which a lessee controls an underlying asset before the commencement date of the lease are within the scope of the sale-and-leaseback guidance in ASC 842-40. These transactions include transactions in which the lessee is involved with an asset before that asset is transferred to the lessor and transactions in which the lessee is involved with the construction of the asset (e.g., build-to-suit arrangements). For further discussion of these transactions, see Chapter 11 of Deloitte’s Leasing Roadmap.

Q&A 11-3  Whether a Seller-Lessee Repurchase Option in a Sale and Leaseback of Real Estate Precludes Treatment of the Transfer as a Sale

**Question**

Would the inclusion of a seller-lessee repurchase option in a sale and leaseback of real estate preclude the transfer from qualifying as a sale under ASC 606?

**Answer**

Yes. Sale-and-leaseback transactions involving real estate that include a repurchase option will not meet the criteria of a sale under ASC 606 regardless of whether the repurchase option is priced at fair value. During the FASB’s redeliberations on ASU 2016-02, the Board noted that sale-and-leaseback transactions involving real estate that include a repurchase option would not meet the second criterion in ASC 842-40-25-3. Paragraph BC352(c) of ASU 2016-02 states, in part:

> When the Board discussed [ASC 842-40-25-3], Board members generally observed that real estate assets would not meet criterion (2). This is because real estate is, by nature, “unique” (that is, no two pieces of land occupy the same space on this planet) such that no other similar real estate asset is “substantially the same.”

Therefore, regardless of whether the repurchase option is priced at fair value, the unique nature of real estate would prevent a sale-and-leaseback transaction involving real estate that includes a repurchase option from satisfying the second criterion in ASC 842-40-25-3 since there would be no alternative asset that is substantially the same as the one being leased. Accordingly, in a manner similar to legacy U.S. GAAP, the new leasing standard would preclude sale-and-leaseback accounting for transactions involving any repurchase options on real estate.
### 11.1.11 Effective Date and Transition

For public companies, the new leasing standard is effective for fiscal years beginning after December 15, 2018 (i.e., calendar periods beginning on January 1, 2019), including interim periods therein.

For all other entities, the amendments in ASU 2016-02 were originally effective for annual periods beginning after December 15, 2019 (i.e., calendar periods beginning on January 1, 2020), and interim periods beginning after December 15, 2020. However, in November 2019, the FASB issued ASU 2019-10, which (1) provides a framework for staggering the effective dates of future major accounting standards and (2) amends the effective dates of certain major new accounting standards to give implementation relief to certain types of entities. In June 2020, the FASB issued ASU 2020-05, which further amends the effective dates to give implementation relief to certain types of entities in response to the COVID-19 pandemic. ASU 2020-05 amends the effective dates of ASU 2016-02 as follows:

<table>
<thead>
<tr>
<th>Public Companies</th>
<th>Public NFPs</th>
<th>All Other Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td>As originally issued (ASU 2016-02)</td>
<td>Fiscal years beginning after December 15, 2018, and interim periods therein</td>
<td>Fiscal years beginning after December 15, 2018, and interim periods therein</td>
</tr>
<tr>
<td>As amended by ASU 2019-10</td>
<td>No changes</td>
<td>No changes</td>
</tr>
<tr>
<td>As amended by ASU 2020-05</td>
<td>No changes</td>
<td>Fiscal years beginning after December 15, 2019, and interim periods therein</td>
</tr>
</tbody>
</table>

Entities are required to use a modified retrospective transition method of adoption. The FASB also issued ASU 2018-11 so that entities may elect not to recast their comparative periods in transition (the “Comparatives Under 840 Option”). For more information, see Section 16.1 of Deloitte’s Leasing Roadmap.

### 11.1.11.1 Additional Implementation Considerations

Discussed below are some of the additional implementation considerations that life sciences entities should thoughtfully address while transitioning to ASC 842. For further discussion, see Deloitte’s July 1, 2019; October 17, 2018; August 7, 2018; April 25, 2017; and July 12, 2016, Heads Up newsletters.

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1. That is, (1) PBEs; (2) NFPs that have issued, or are conduit bond obligors for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market; and (3) employee benefit plans that file or furnish financial statements with or to the SEC.
2. See footnote 1.
3. The deferral in ASU 2020-05 applies to public NFPs that have not issued financial statements or made financial statements available for issuance as of June 3, 2020. Public NFPs that have issued financial statements or have made financial statements available for issuance before that date must comply with the effective dates prescribed for public companies above.
11.1.11.1.1 Operational Considerations

For the lessee accounting requirements to be implemented, information about all individual contracts and arrangements will need to be collected, maintained, and evaluated, including information related to real estate contracts and equipment contracts (e.g., manufacturing equipment, laboratory equipment). In addition, it may be necessary to obtain information outside of contractual arrangements, including (1) the fair value of an asset, (2) the asset’s estimated useful life, (3) the incremental borrowing rate, and (4) certain judgments related to lease options. The ability to acquire such data may be particularly challenging when contract documentation is prepared in a foreign language and could vary as a result of local business practices.

11.1.11.1.1.1 Materiality Threshold

When implementing the lessee accounting requirements, life sciences companies are likely to consider a materiality threshold, especially for high-volume, low-value leased assets (e.g., laptops). As discussed further in Q&A 2-1 of Deloitte’s Leasing Roadmap, ASC 842 does not contain a “small-ticket item” exception similar to that in IFRS 16. Although materiality is generally a consideration in the application of all accounting standards, life sciences entities should not simply default to their existing capitalization threshold for PP&E for the following reasons:

- The existing capitalization threshold for PP&E is unlikely to include the effect of the additional asset base introduced by the new leasing standard. That is, the addition of another set of ROU assets not previously recognized on an entity’s balance sheet may require a refreshed analysis of the entity’s capitalization thresholds to ensure that the aggregated amounts will not become material.
- The existing capitalization threshold for PP&E does not take into account the liability side of the balance sheet. Under ASC 842, if an entity wishes to establish a threshold that will be used to avoid accounting for both ROU assets and lease liabilities on the balance sheet, it must consider the materiality, in the aggregate, of all of its ROU assets and related lease liabilities that would be excluded when it adopts such a threshold.

One reasonable approach to developing a capitalization threshold for leases may be to use the lesser of the following:

- A capitalization threshold for PP&E, including ROU assets (i.e., the threshold takes into account the effect of leased assets determined in accordance with ASC 842).
- A recognition threshold for liabilities that takes into account the effect of lease liabilities determined in accordance with ASC 842.

Another reasonable approach to developing a capitalization threshold for leases may be to record all lease liabilities but to subject the related ROU assets to such a threshold. Under this approach, if an ROU asset is below the established capitalization threshold, it would immediately be recognized as an expense. In subsequent periods, entities would amortize the lease liability by using the effective interest method, under which a portion of the periodic lease payments would reduce the liability and the remainder would be recognized as interest expense.

11.1.11.1.1.2 Variable Expense

Life sciences entities will mostly likely have contracts with variable lease payments (e.g., international real estate contracts with index-based payment escalations). Entities may find it necessary to create a new general ledger account to track variable lease costs for disclosure purposes in accordance with ASC 842-20-50-4 and to consider impacts of variable lease payments on the accounts payable process.
11.1.11.1.2 Application of Judgment and Estimation

Entities must use judgment and make estimates under a number of the new as well as legacy lease accounting requirements. Judgment is often required in the assessment of a lease's term, which would affect whether the lease qualifies for the short-term exemption and therefore for off-balance-sheet treatment. In addition, since almost all leases will be recognized on the balance sheet, judgment in distinguishing between leases and services becomes more critical under the new guidance.

11.1.11.1.2.1 Discount Rates

Entities will need to recognize ROU assets and lease obligations by using an appropriate discount rate at transition and on an ongoing basis. Compliance with this requirement may be difficult for entities with a significant number of leases since they will need to identify the appropriate incremental borrowing rate for each lease on the basis of factors associated with the underlying lease terms (e.g., lease tenor, asset type, residual value guarantees). That is, entities would not be permitted to use the same discount rate for all of their leases unless the leased assets and related terms are similar.

Additional considerations include:

- **Secured versus unsecured rate** — The definition of the incremental borrowing rate under ASC 842 requires lessees to obtain a collateralized or secured borrowing rate. Unsecured rates are likely to be higher and, therefore, to result in a lower lease liability. If a lessee does not borrow on a secured basis, it will most likely need to make adjustments to its unsecured borrowing rates to reflect a rate of a secured borrowing.

- **Parent versus subsidiary rate** — Sometimes it may be appropriate for a subsidiary to use an incremental borrowing rate other than its own. This will depend on the nature of the lease negotiations and the resulting terms and conditions (e.g., a consolidated group with a centralized treasury function that negotiates on behalf of all of its subsidiaries to benefit from its superior credit).

- **Leases denominated in a foreign currency** — When determining an incremental borrowing rate for a lease denominated in a foreign currency, entities should use assumptions that are consistent with a rate that the entities would obtain to borrow in the same currency in which the lease is denominated. The incremental borrowing rate should still reflect a collateralized rate in the relevant foreign environment.

- **Discount rate in transition** — Entities should determine the discount rate as of the effective date of ASC 842 when initially measuring lease liabilities (under the assumption that the entities continue to account for comparative periods under ASC 840). When selecting a discount rate, entities should elect, as an accounting policy consistently applied to all contracts, to use an interest rate that corresponds to either (1) the original lease term or (2) the remaining lease term.

- **Developing a method** — Life sciences entities should define a method for calculating the incremental borrowing rate that is auditable and supportable at transition and on an ongoing basis.
11.1.11.1.3 IT Systems

As a result of implementing the requirements of the new leasing standard, life sciences entities will most likely need to enhance their existing IT systems. The extent of the enhancements will be based on the size and complexity of an entity's lease portfolio and its existing leasing systems. As with any change to existing systems, an entity will need to consider the business ramifications (i.e., the potential impact on existing processes, systems, and controls) and the requirements of system users (e.g., the entity's legal, tax, financial planning and analysis, real estate, treasury, and financial reporting functions). Also, management may need to consider system changes that will enable the entity to estimate, before adoption of ASC 842, the new leasing standard's effect on key performance indicators and metrics, tax filings, debt covenants, or other filings. In addition, to the extent that an entity prepares IFRS statutory reports for foreign subsidiaries, its systems will need to distinguish between ASC 842 and IFRS 16 and will need to be equipped to handle the differences between the two standards.

11.1.11.1.4 Income Taxes

A lease's classification for accounting purposes does not affect its classification for tax purposes. A life sciences entity will therefore continue to be required to determine the tax classification of a lease under the applicable tax laws. While the classification may be similar for either purpose, the differences in tax and accounting principles and guidance often result in book/tax differences. Thus, once an entity implements the new leasing standard, it will need to establish a process to account for these differences. The requirement that entities reevaluate their leases under the new guidance also presents an opportunity for entities to reassess the tax treatment of such leases as well as their data collection and processes. Since the IRS considers a taxpayer's tax treatment of leases to be a method of accounting, any changes to existing methods may require IRS consent. Entities should also consider the potential state tax issues that may arise as a result of the new guidance, including how the classification of the ROU asset may affect the apportionment formula in the determination of state taxable income and how the significant increase in recorded lease assets could affect the determination of franchise tax payable.

11.1.11.1.5 Covenant Considerations

Given the requirement to bring most leases onto the balance sheet, many companies, including those in the life sciences industry, will reflect additional liabilities on their balance sheets after adopting the new leasing standard. An entity's determination of whether the increased leverage will negatively affect any key metrics or potentially cause debt covenant violations is a critical aspect of its planning for the new standard's implementation. This determination may depend, in part, on how various debt agreements define and limit indebtedness as well as on whether the debt agreements use “frozen GAAP” covenants (i.e., covenants based on the GAAP that applied at the time the debt was issued). ASC 842 requires presentation of operating lease liabilities outside traditional debt, which may provide relief. Regardless, we believe that it will be critical for all life sciences entities to determine the potential effects of the new leasing standard on debt covenants and begin discussions with lenders early if they believe that violations are likely to occur as a result of adopting ASC 842.

11.1.12 FASB's Response to the COVID-19 Pandemic

On April 8, 2020, the FASB met to discuss its ongoing efforts to monitor and respond to the impact of COVID-19 on the preparation of financial statements under U.S. GAAP, including the related accounting and financial reporting implications. Specifically, the Board discussed proposals to delay the effective dates of certain recently issued standards, including ASC 842, for certain entities. The Board later finalized this proposed deferral for certain entities on June 3, 2020, by issuing ASU 2020-05. (See Chapter 16 of Deloitte's Leasing Roadmap for more information.) Further, the FASB discussed and
provided feedback on technical inquiries received from stakeholders regarding certain accounting topics affected by COVID-19, including staff guidance on how to account for rent concessions provided as a result of the pandemic.

On April 10, 2020, the FASB issued a staff Q&A (the “Staff Q&A”) to provide guidance on its remarks at the April 8 Board meeting about accounting for rent concessions resulting from the COVID-19 pandemic. Specifically, the Staff Q&A affirms the discussion at the April 8 meeting by allowing entities to forgo performing the lease-by-lease legal analysis to determine whether contractual provisions in an existing lease agreement provide enforceable rights and obligations related to lease concessions, as long as the concessions are related to COVID-19 and the changes to the lease do not result in a substantial increase in the rights of the lessor or the obligations of the lessee. In addition, the Staff Q&A affirms that entities may make an election to account for eligible concessions, regardless of their form, either by (1) applying the modification framework for these concessions in accordance with ASC 840 or ASC 842 as applicable or (2) accounting for the concessions as if they were made under the enforceable rights included in the original agreement and are thus outside of the modification framework.

See Deloitte’s Financial Reporting Alert, “Financial Reporting Considerations Related to COVID-19 and an Economic Downturn,” for more information on applying the FASB’s relief related to qualifying concessions as well as interpretive responses to frequently asked questions.

### 11.2 Amendments to the New Leasing Standard

The FASB has been working with stakeholders throughout the implementation of ASC 842 to clarify the guidance in the new leasing standard and identify aspects of that guidance that could pose challenges for entities. In response to stakeholders’ comments and in a manner consistent with its ongoing Codification improvements project, the Board has issued additional ASUs to clarify the guidance in ASC 842, correct unintended application of the standard, or provide certain relief to entities. To make stakeholders more aware of its amendments to ASC 842, the Board decided to incorporate those amendments into ASUs developed outside of its project on Codification improvements in general.

ASUs issued to date that amend certain aspects of ASC 842 are broadly applicable to the life sciences industry and include the following:

- **ASU 2018-10 on improvements to ASC 842** — In July 2018, the FASB issued ASU 2018-10, which makes 16 narrow-scope amendments (i.e., minor changes and clarifications) to certain aspects of ASC 842.

- **ASU 2018-11 on targeted improvements to ASC 842** — In July 2018, the FASB issued ASU 2018-11 to provide entities with relief from the costs of implementing certain aspects of the new leasing standard. Specifically, under the amendments in ASU 2018-11:
  - Entities may elect not to recast the comparative periods presented when transitioning to ASC 842.
  - Lessors may elect not to separate lease and nonlease components when certain conditions are met.

- **ASU 2019-01 on Codification improvements to ASC 842** — In March 2019, the FASB issued ASU 2019-01 to amend certain guidance in ASC 842 in response to feedback from stakeholders. The ASU includes:
  - Guidance on determining the fair value of the underlying asset for lessors other than manufacturers or dealers that aligns with certain legacy guidance in ASC 840.
  - A clarifying amendment that exempts lessees and lessors from providing certain interim disclosures in the fiscal year in which they adopt the new leasing standard.
For further discussion of ASU 2018-10 and ASU 2018-11, see Deloitte’s August 7, 2018, Heads Up.

ASU 2020-02, which amends an SEC paragraph in ASC 842-10, is discussed below.

For a complete list of ASUs issued to amend and clarify the guidance in ASC 842, see Section 17.3.1 of Deloitte’s Leasing Roadmap.

11.2.1 Leases (Topic 842): Update to SEC Section on Effective Date (ASU 2020-02)

At the July 20, 2017, EITF meeting, the SEC staff announced that it would not object when certain PBEs elect to use the non-PBE effective dates solely to adopt the FASB’s new standards on revenue and leasing. The staff announcement clarifies that the ability to use non-PBE effective dates to adopt the new revenue and leasing standards is limited to the subset of PBEs “that otherwise would not meet the definition of a public business entity except for a requirement to include or the inclusion of its financial statements or financial information in another entity’s filings with the SEC” (referred to herein as “specified PBEs”).

While the staff announcement is written in the context of specified PBEs, the principal beneficiaries of the relief will be SEC filers that include financial statements or financial information prepared by specified PBEs in their own filings. SEC Regulation S-X rules under which such filings may be prepared could include:

• Rule 3-05, “Financial Statements of Businesses Acquired or to Be Acquired.”
• Rule 3-09, “Separate Financial Statements of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons.”
• Rule 3-14, “Special Instructions for Financial Statements of Real Estate Operations Acquired or to Be Acquired;”
• Rule 4-08(g), “Summarized Financial Information of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons.”

Under the new leasing standard, there is one adoption date for PBEs and another (later) adoption date for non-PBEs. The ASC master glossary defines a PBE, in part, as a business entity that is “required by the [SEC] to file or furnish financial statements, or [that] 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)” (emphasis added). The definition further states that “[a]n 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.”

Before the staff’s announcement, certain nonpublic companies applying the PBE definition in the adoption-date criteria would have been required to use the public-company adoption dates for the new revenue and leasing standards. While the SEC staff announcement provides considerable and welcome relief to registrants preparing to adopt the new leasing standard, it is purposely narrow in scope and should not be applied by analogy to the adoption-date assessment for any other standards besides the revenue and leasing standards. The SEC staff announcement does not preclude specified PBEs from adopting the provisions of the new revenue and leasing standards on the adoption date applicable to all other PBEs if a specified PBE wishes to use the PBE adoption date.
In November 2019, the FASB issued ASU 2019-10, which, among other things, amends the effective dates of ASC 842 for non-PBEs to fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. At the 2019 AICPA Conference on Current SEC and PCAOB Developments, the SEC staff announced that it would not object if specified PBEs adopt ASC 842 by using ASU 2019-10’s timelines that apply to non-PBEs. ASU 2020-02, issued in February 2020, codifies this position by adding a note to ASC 842-10-S65-1.

11.3 Ongoing FASB Activity

In September 2020, the FASB held two public roundtables to discuss challenges with implementing ASC 842. These roundtables are part of the FASB's broader effort to solicit feedback from stakeholders on difficulties with applying or interpreting the new leasing guidance. Present at the roundtables were all FASB board members, members of industry groups, preparers (from both public and private companies), users, and representatives from accounting firms (both large firms and private-company auditors). Representatives from the SEC and PCAOB staffs also observed the meeting.

Roundtable participants discussed the following five topics identified by the FASB staff through its outreach efforts:

- Topic 1 — Lessee Application of Rate Implicit in the Lease.
- Topic 2 — Lessee Application of Incremental Borrowing Rate.
- Topic 3 — Embedded Leases.
- Topic 4 — Lease Modifications.
- Topic 5 — Lessee Allocation of Fixed and Variable Payments.

For a more detailed summary of the roundtable discussions and information about next steps, see Deloitte’s September 28, 2020, Heads Up.

11.4 SEC Comment Letter Themes Related to Leases

As a result of SEC registrants’ adoption in 2019 of the new leasing standard, the focus of the SEC staff's comments on leasing transactions is shifting from registrants' accounting under the legacy leasing guidance (codified in ASC 840) to their application of the new leasing standard. While the number of comment letters related to the adoption of ASC 842 has increased over the past year, we have not yet seen a significant number of comment letters related to leasing transactions under ASC 842, and we believe that the SEC staff is still in the early stages of its review process. Although it is currently unclear what trends may result from staff comments on the application of ASC 842, life sciences companies may want to consider comments issued recently on the following lease accounting and disclosure topics:

- How ASC 842 is being applied in certain arrangements.
- The discount rate used to calculate the amount of the lease liability and corresponding ROU asset.
- The nature and treatment of variable lease payments that depend (or do not depend) on an index or rate.
- Required ASC 840 disclosures in prior periods when the registrant has elected not to recast its comparative periods in the period of adoption when transitioning to ASC 842.

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4 In June 2020, the FASB issued ASU 2020-05, which further amends the effective dates of ASC 842. See Section 11.1.11 for more information.
Given the low, albeit increasing, volume of SEC staff comments related to ASC 842 that have been issued thus far, registrants should continue monitoring staff comments to identify any new comments or trends related to the new leasing standard that may emerge in the future. For more information about SEC comment letter themes that are relevant to life sciences companies, see Deloitte's SEC Comment Letter Roadmap. In addition, see Deloitte’s January 7, 2020, Heads Up, which outlines the ASC 842 disclosure requirements, elaborates on some of those requirements, and provides examples of related SEC comments issued to registrants.
Appendix B — Titles of Standards and Other Literature

**AICPA Literature**

**Accounting and Valuation Guides**
- Assets Acquired to Be Used in Research and Development Activities
- Valuation of Privately-Held-Company Equity Securities Issued as Compensation

**Audit and Accounting Guide**
- Revenue Recognition

**Clarified Statements on Auditing Standards**
- AU-C Section 501, “Audit Evidence — Specific Considerations for Selected Items”
- AU-C Section 620, “Using the Work of an Auditor’s Specialist”

**Issues Papers**
- Identification and Discussion of Certain Financial Accounting and Reporting Issues Concerning LIFO Inventories
- 86-2, Accounting for Options

**Other**
- AICPA Technical Q&A Section 2260.03, “Other Assets; Legal Expenses Incurred to Defend Patent Infringement Suit”

**FASB Literature**

**ASC Topics**
- ASC 105, *Generally Accepted Accounting Principles*
- ASC 205, *Presentation of Financial Statements*
- ASC 210, *Balance Sheet*
- ASC 220, *Income Statement — Reporting Comprehensive Income*
- ASC 230, *Statement of Cash Flows*
- ASC 235, *Notes to Financial Statements*
- ASC 250, *Accounting Changes and Error Corrections*
ASC 260, *Earnings per Share*
ASC 270, *Interim Reporting*
ASC 275, *Risks and Uncertainties*
ASC 280, *Segment Reporting*
ASC 310, *Receivables*
ASC 320, *Investments — Debt and Equity Securities*
ASC 321, *Investments — Equity Securities*
ASC 323, *Investments — Equity Method and Joint Ventures*
ASC 326, *Financial Instruments — Credit Losses*
ASC 330, *Inventory*
ASC 340, *Other Assets and Deferred Costs*
ASC 350, *Intangibles — Goodwill and Other*
ASC 360, *Property, Plant, and Equipment*
ASC 405, *Liabilities*
ASC 410, *Asset Retirement and Environmental Obligations*
ASC 420, *Exit or Disposal Cost Obligations*
ASC 450, *Contingencies*
ASC 460, *Guarantees*
ASC 470, *Debt*
ASC 480, *Distinguishing Liabilities From Equity*
ASC 505, *Equity*
ASC 605, *Revenue Recognition*
ASC 606, *Revenue From Contracts With Customers*
ASC 610, *Other Income*
ASC 705, *Cost of Sales and Services*
ASC 710, *Compensation — General*
ASC 715, *Compensation — Retirement Benefits*
ASC 718, *Compensation — Stock Compensation*
ASC 720, *Other Expenses*
ASC 730, *Research and Development*
ASC 740, *Income Taxes*
ASC 805, *Business Combinations*
ASC 808, *Collaborative Arrangements*
Appendix B — Titles of Standards and Other Literature

ASC 810, Consolidation
ASC 815, Derivatives and Hedging
ASC 820, Fair Value Measurement
ASC 825, Financial Instruments
ASC 830, Foreign Currency Matters
ASC 835, Interest
ASC 840, Leases
ASC 842, Leases
ASC 845, Nonmonetary Transactions
ASC 848, Reference Rate Reform
ASC 855, Subsequent Events
ASC 860, Transfers and Servicing
ASC 905, Agriculture
ASC 915, Development Stage Entities
ASC 930, Extractive Activities — Mining
ASC 942, Financial Services — Depository and Lending
ASC 944, Financial Services — Insurance
ASC 946, Financial Services — Investment Companies
ASC 948, Financial Services — Mortgage Banking
ASC 954, Health Care Entities
ASC 958, Not-for-Profit Entities
ASC 960, Plan Accounting — Defined Benefit Pension Plans
ASC 985, Software

ASUs
ASU 2010-27, Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers — a consensus of the FASB Emerging Issues Task Force
ASU 2011-06, Other Expenses (Topic 720): Fees Paid to the Federal Government by Health Insurers — a consensus of the FASB Emerging Issues Task Force
ASU 2014-02, Intangibles — Goodwill and Other (Topic 350): Accounting for Goodwill — a consensus of the Private Company Council
ASU 2014-09, Revenue From Contracts With Customers (Topic 606)
ASU 2014-10, Development Stage Entities (Topic 915): Elimination of Certain Financial Reporting Requirements, Including an Amendment to Variable Interest Entities Guidance in Topic 810, Consolidation
ASU 2014-15, Presentation of Financial Statements — Going Concern (Subtopic 205-40): Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern
ASU 2014-16, Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid
Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity — a consensus of the
FASB Emerging Issues Task Force
ASU 2015-14, Revenue From Contracts With Customers (Topic 606): Deferral of the Effective Date
ASU 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period
Adjustments
ASU 2016-01, Financial Instruments — Overall (Subtopic 825-10): Recognition and Measurement of Financial
Assets and Financial Liabilities
ASU 2016-02, Leases (Topic 842)
ASU 2016-08, Revenue From Contracts With Customers (Topic 606): Principal Versus Agent Considerations
(Reporting Revenue Gross Versus Net)
ASU 2016-09, Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based
Payment Accounting
ASU 2016-10, Revenue From Contracts With Customers (Topic 606): Identifying Performance Obligations and
Licensing
ASU 2016-11, Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC
Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements
at the March 3, 2016 EITF Meeting
ASU 2016-12, Revenue From Contracts With Customers (Topic 606): Narrow-Scope Improvements and
Practical Expedients
ASU 2016-13, Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial
Instruments
Payments — a consensus of the FASB Emerging Issues Task Force
ASU 2016-16, Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory
ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business
ASU 2017-04, Intangibles — Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment
ASU 2017-05, Other Income — Gains and Losses From the Derecognition of Nonfinancial Assets (Subtopic
610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial
Assets
ASU 2017-11, Earnings per Share (Topic 260); Distinguishing Liabilities From Equity (Topic 480); Derivatives
and Hedging (Topic 815): (Part I) Accounting for Certain Financial Instruments With Down Round Features,
(Part II) Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain
Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests With a Scope Exception
Appendix B — Titles of Standards and Other Literature

ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities

ASU 2017-13, Revenue Recognition (Topic 605), Revenue From Contracts With Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017 EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments (SEC Update)

ASU 2017-14, Income Statement — Reporting Comprehensive Income (Topic 220), Revenue Recognition (Topic 605), and Revenue From Contracts With Customers (Topic 606) (SEC Update)

ASU 2018-01, Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842

ASU 2018-07, Compensation — Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting

ASU 2018-08, Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made

ASU 2018-10, Codification Improvements to Topic 842, Leases

ASU 2018-11, Leases (Topic 842): Targeted Improvements


ASU 2018-17, Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities

ASU 2018-18, Collaborative Arrangements (Topic 808): Clarifying the Interaction Between Topic 808 and Topic 606

ASU 2018-20, Leases (Topic 842): Narrow-Scope Improvements for Lessors

ASU 2019-01, Leases (Topic 842): Codification Improvements

ASU 2019-04, Codification Improvements to Topic 326, Financial Instruments — Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments

ASU 2019-05, Financial Instruments — Credit Losses (Topic 326): Targeted Transition Relief

ASU 2019-08, Compensation — Stock Compensation (Topic 718) and Revenue From Contracts With Customers (Topic 606): Codification Improvements — Share-Based Consideration Payable to a Customer

ASU 2019-10, Financial Instruments — Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates

ASU 2019-11, Codification Improvements to Topic 326, Financial Instruments — Credit Losses

ASU 2019-12, Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes
ASU 2020-01, Investments — Equity Securities (Topic 321), Investments — Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815): Clarifying the Interactions Between Topic 321, Topic 323, and Topic 815 — a consensus of the FASB Emerging Issues Task Force

ASU 2020-02, Financial Instruments — Credit Losses (Topic 326) and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 119 and Update to SEC Section on Effective Date Related to Accounting Standards Update No. 2016-02, Leases (Topic 842)

ASU 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting

ASU 2020-05, Revenue From Contracts With Customers (Topic 606) and Leases (Topic 842): Effective Dates for Certain Entities

ASU 2020-06, Debt — Debt With Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging — Contracts in Entity's Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity's Own Equity

ASU 2021-01, Reference Rate Reform

**Concepts Statements**

No. 5, Recognition and Measurement in Financial Statements of Business Enterprises

No. 6, Elements of Financial Statements

No. 8, Conceptual Framework for Financial Reporting — Chapter 8, Notes to Financial Statements

**Proposed ASUs**

No. 2015-340, Government Assistance (Topic 832): Disclosures by Business Entities About Government Assistance

No. 2017-210, Inventory (Topic 330): Disclosure Framework — Changes to the Disclosure Requirements for Inventory

No. 2017-280, Consolidation (Topic 812): Reorganization


No. 2019-790, Derivatives and Hedging (Topic 815): Codification Improvements to Hedge Accounting

**Other**


FASB Staff Revenue Recognition Implementation Q&As

**IFRS Literature**

IFRS 2, Share-Based Payment

IFRS 3, Business Combinations

IFRS 5, Non-Current Assets Held for Sale and Discontinued Operations

IFRS 9, Financial Instruments

IFRS 10, Consolidated Financial Statements
IFRS 11, Joint Arrangements
IFRS 12, Disclosure of Interests in Other Entities
IFRS 15, Revenue From Contracts With Customers
IFRS 16, Leases
IAS 1, Presentation of Financial Statements
IAS 7, Statement of Cash Flows
IAS 10, Events After the Reporting Period
IAS 12, Income Taxes
IAS 17, Leases
IAS 20, Accounting for Government Grants and Disclosure of Government Assistance
IAS 27, Separate Financial Statements
IAS 32, Financial Instruments: Presentation
IAS 37, Provisions, Contingent Liabilities and Contingent Assets
IAS 38, Intangible Assets
IAS 40, Investment Property

IRC
Section 78, “Gross Up for Deemed Paid Foreign Tax Credit”
Section 163(j), “Interest; Limitation on Business Interest”
Section 382, “Limitation on Net Operating Loss Carryforwards and Certain Built-In Losses Following Ownership Change”
Section 409A “Inclusion in Gross Income of Deferred Compensation Under Nonqualified Deferred Compensation Plans”
Section 422, “Incentive Stock Options”
Section 423, “Employee Stock Purchase Plans”

PCAOB Literature

SEC Literature
CF Disclosure Guidance
Topic 9, “Coronavirus (COVID-19)”
Topic 11, “Special Purpose Acquisition Companies”
Final Rules
No. 34-88365, *Accelerated Filer and Larger Accelerated Filer Definitions*

No. 33-10786, *Amendments to Financial Disclosures About Acquired and Disposed Business*

No. 33-10890, *Management’s Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information*

FRM
Topic 1, “Registrant’s Financial Statements”
Topic 2, “Other Financial Statements Required”
Topic 3, “Pro Forma Financial Information”
Topic 5, “Smaller Reporting Companies”
Topic 7, “Related Party Matters”
Topic 10, “Emerging Growth Companies”

Interpretive Release
33-10403, *Updates to Commission Guidance Regarding Accounting for Sales of Vaccines and Bioterror Countermeasures to the Federal Government for Placement Into the Pediatric Vaccine Stockpile or the Strategic National Stockpile*

Regulation S-K
Item 103, “Business; Legal Proceedings”
Item 201, “Market Price of and Dividends on the Registrant’s Common Equity and Related Stockholder Matters”
Item 301, “Selected Financial Data”
Item 302, “Supplementary Financial Information”
Item 303, “Management’s Discussion and Analysis of Financial Condition and Results of Operations”
Item 305, “Quantitative and Qualitative Disclosures About Market Risk”
Item 402, “Executive Compensation”
Item 404, “Transactions With Related Persons, Promoters and Certain Control Persons”
Item 407, “Corporate Governance”
Item 503, “Prospectus Summary”
Item 601, “Exhibits”

Regulation S-X
Rule 1-02(w), “Definitions of Terms Used in Regulation S-X (17 CFR part 210); Significant Subsidiary”
Article 2, “Qualifications and Reports of Accountants”
Rule 3-01, “Consolidated Balance Sheet”
Rule 3-02, “Consolidated Statements of Comprehensive Income and Cash Flows”

Rule 3-05, “Financial Statements of Businesses Acquired or to Be Acquired”

Rule 3-09, “Separate Financial Statements of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons”

Rule 3-10, “Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered”

Rule 3-14, “Special Instructions for Financial Statements of Real Estate Operations Acquired or to Be Acquired”

Rule 3-16, “Financial Statements of Affiliates Whose Securities Collateralize an Issue Registered or Being Registered”

Rule 4-08(g), “General Notes to Financial Statements; Summarized Financial Information of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons”

Rule 4-08(n), “General Notes to Financial Statements; Accounting Policies for Certain Derivative Instruments”

5-02, “Commercial and Industrial Companies; Balance Sheets”

5-03, “Commercial and Industrial Companies; Statements of Comprehensive Income”

Article 8, “Financial Statements of Smaller Reporting Companies”

Rule 10-01(b), “Interim Financial Statements; Other Instructions as to Content”

Article 11, “Pro Forma Financial Information”

Rule 11-01 “Presentation Requirements”

**SAB Topics**

No. 1.M, “Financial Statements; Materiality”

No. 5.A, “Miscellaneous Accounting; Expenses of Offering”

No. 5.Y, “Miscellaneous Accounting; Accounting and Disclosures Relating to Loss Contingencies”

No. 11.A, “Miscellaneous Disclosure; Operating-Differential Subsidies”

No. 13, “Revenue Recognition”

No. 14.B, “Share-Based Payment; Transition From Nonpublic to Public Entity Status”

No. 14.D, “Share-Based Payments; Certain Assumptions Used in Valuation Methods”

**SEC Securities Act of 1933 General Rules and Regulations**

Rule 144, “Persons Deemed Not to be Engaged in a Distribution and Therefore Not Underwriters — General Guidance”
TRG Agenda Papers

TRG Agenda Paper 6, Customer Options for Additional Goods and Services and Nonrefundable Upfront Fees

TRG Agenda Paper 11, October 2014 Meeting — Summary of Issues Discussed and Next Steps

TRG Agenda Paper 41, Measuring Progress When Multiple Goods or Services Are Included in a Single Performance Obligation

TRG Agenda Paper 44, July 2015 Meeting — Summary of Issues Discussed and Next Steps

TRG Agenda Paper 54, Considering Class of Customer When Evaluating Whether a Customer Option Gives Rise to a Material Right

TRG Agenda Paper 55, April 2016 Meeting — Summary of Issues Discussed and Next Steps

Superseded Literature

AICPA Statement of Position

96-1, Environmental Remediation Liabilities

EITF Issues

Issue 00-21, “Revenue Arrangements With Multiple Deliverables”

Issue 01-8, “Determining Whether an Arrangement Contains a Lease”

Issue 01-9, “Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor’s Products)”

Issue 01-10, “Accounting for the Impact of the Terrorist Attacks of September 11, 2001”

Issue 02-16, “Accounting by a Customer (Including a Reseller) for Certain Consideration Received From a Vendor”

Issue 08-6, “Equity Method Investment Accounting Considerations”

Issue 09-2, “Research and Development Assets Acquired in an Asset Acquisition”

Issue 09-4, “Seller Accounting for Contingent Consideration”

FASB Interpretations

No. 14, Reasonable Estimation of the Amount of a Loss — an interpretation of FASB Statement No. 5

No. 48, Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109

FASB Statements

No. 5, Accounting for Contingencies

No. 52, Foreign Currency Translation

No. 95, Statement of Cash Flows

No. 114, Accounting by Creditors for Impairment of a Loan — an amendment of FASB Statements No. 5 and 15

No. 123(R), Share-Based Payment
No. 133, *Accounting for Derivative Instruments and Hedging Activities*

No. 141, *Business Combinations*

No. 141(R), *Business Combinations*

No. 160, *Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51*
Appendix C — Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>AETR</td>
<td>annual effective tax rate</td>
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<td>AFS</td>
<td>available for sale</td>
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<td>AICPA</td>
<td>American Institute of Certified Public Accountants</td>
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<td>AMT</td>
<td>alternative minimum tax</td>
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<td>API</td>
<td>active pharmaceutical ingredient</td>
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<td>APIC</td>
<td>additional paid-in capital</td>
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<td>ASC</td>
<td>FASB Accounting Standards Codification</td>
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<td>ASR</td>
<td>accelerated share repurchase</td>
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<td>ASU</td>
<td>FASB Accounting Standards Update</td>
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<td>BCF</td>
<td>beneficial conversion feature</td>
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<td>BEAT</td>
<td>base erosion anti-abuse tax</td>
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<td>BEMTA</td>
<td>base erosion minimum tax amount</td>
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<td>BPD</td>
<td>branded prescription drug</td>
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<td>CAM</td>
<td>critical audit matter</td>
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<td>CCF</td>
<td>cash conversion feature</td>
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<td>CECL</td>
<td>current expected credit loss</td>
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<td>CFC</td>
<td>controlled foreign corporation</td>
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<td>CFR</td>
<td>Code of Federal Regulations</td>
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<td>CMO</td>
<td>contract manufacturing organization</td>
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<td>CODM</td>
<td>chief operating decision maker</td>
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<td>CRO</td>
<td>contract research organization</td>
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<td>DTA</td>
<td>deferred tax asset</td>
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<td>DTL</td>
<td>deferred tax liability</td>
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<td>EBITDA</td>
<td>earnings before interest, taxes, depreciation, and amortization</td>
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<td>ED</td>
<td>exposure draft</td>
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<td>EDGAR</td>
<td>SEC electronic data gathering, analysis, and retrieval system</td>
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<td>EGC</td>
<td>emerging growth company</td>
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<td>EITF</td>
<td>Emerging Issues Task Force</td>
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<td>EPS</td>
<td>earnings per share</td>
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<td>ESPP</td>
<td>employee stock purchase plan</td>
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<td>European Union</td>
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<td>EUR</td>
<td>euros</td>
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<td>FASB</td>
<td>Financial Accounting Standards Board</td>
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<td>FDA</td>
<td>Food and Drug Administration</td>
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<td>FDII</td>
<td>foreign derived intangible income</td>
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<td>FIFO</td>
<td>first in, first out</td>
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<td>FIN</td>
<td>FASB Interpretation</td>
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<td>FOB</td>
<td>free on board</td>
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<td>FRM</td>
<td>SEC Division of Corporation Finance Financial Reporting Manual</td>
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<td>FVTOCI</td>
<td>fair value through other comprehensive income</td>
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<td>GAAP</td>
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<td>GILTI</td>
<td>global intangible low-taxed income</td>
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<td>GPO</td>
<td>group purchasing organization</td>
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<td>HFI</td>
<td>held for investment</td>
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<td>HFS</td>
<td>held for sale</td>
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<td>IAS</td>
<td>International Accounting Standard</td>
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<td>IASB</td>
<td>International Accounting Standards Board</td>
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<td>IBNR</td>
<td>incurred but not reported</td>
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<td>Abbreviation</td>
<td>Description</td>
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<td>IFRS</td>
<td>International Financial Reporting Standard</td>
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<td>IIR</td>
<td>investigator-initiated research</td>
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<td>IP</td>
<td>intellectual property</td>
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<td>IPO</td>
<td>initial public offering</td>
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<td>IPR&amp;D</td>
<td>in-process research and development</td>
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<td>IRC</td>
<td>Internal Revenue Code</td>
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<td>IRS</td>
<td>Internal Revenue Service</td>
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<td>ISO</td>
<td>incentive stock option</td>
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<td>IT</td>
<td>information technology</td>
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<td>LCD</td>
<td>liquid-crystal display</td>
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<td>LIBOR</td>
<td>London Interbank Offered Rate</td>
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<tr>
<td>LIFO</td>
<td>last in, first out</td>
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<td>M&amp;A</td>
<td>merger and acquisition</td>
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<td>MD&amp;A</td>
<td>Management’s Discussion &amp; Analysis</td>
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<td>MSL</td>
<td>medical science liaison</td>
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<td>NFP</td>
<td>not-for-profit entity</td>
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<td>NOL</td>
<td>net operating loss</td>
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<td>NQSO</td>
<td>nonqualified stock option</td>
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<td>NSO</td>
<td>nonstatutory option</td>
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<td>OCA</td>
<td>SEC’s Office of the Chief Accountant</td>
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<td>OCI</td>
<td>other comprehensive income</td>
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<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>OEM</td>
<td>original equipment manufacturer</td>
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<tr>
<td>PBE</td>
<td>public business entity</td>
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<tr>
<td>PCAOB</td>
<td>Public Company Accounting Oversight Board</td>
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<tr>
<td>PCC</td>
<td>Private Company Council</td>
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<tr>
<td>PP&amp;E</td>
<td>property, plant, and equipment</td>
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<td>PRV</td>
<td>priority review voucher</td>
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<td>PTRS</td>
<td>probability of technical and regulatory success</td>
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<tr>
<td>Q&amp;A</td>
<td>question and answer</td>
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<td>QIP</td>
<td>qualified improvement property</td>
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<tr>
<td>R&amp;D</td>
<td>research and development</td>
</tr>
<tr>
<td>R&amp;E</td>
<td>research and experimentation</td>
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<tr>
<td>REMS</td>
<td>risk evaluation and mitigation strategy</td>
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<td>ROU</td>
<td>right of use</td>
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<td>SaaS</td>
<td>software as a service</td>
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<td>SAB</td>
<td>Staff Accounting Bulletin</td>
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<td>SEC</td>
<td>Securities and Exchange Commission</td>
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<td>SME</td>
<td>small to medium-sized entity</td>
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<td>SPAC</td>
<td>special-purpose acquisition company</td>
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<td>SPPI</td>
<td>solely payments of principal and interest</td>
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<td>SRC</td>
<td>smaller reporting entity</td>
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<td>Standard &amp; Poor’s 500 Index</td>
</tr>
<tr>
<td>TD</td>
<td>Treasury Decision</td>
</tr>
<tr>
<td>TRG</td>
<td>transition resource group</td>
</tr>
<tr>
<td>USD</td>
<td>U.S. dollars</td>
</tr>
<tr>
<td>UTB</td>
<td>unrecognized tax benefit</td>
</tr>
<tr>
<td>VIE</td>
<td>variable interest entity</td>
</tr>
<tr>
<td>VWAP</td>
<td>volume-weighted average daily market price</td>
</tr>
</tbody>
</table>
The following is a list of short references for the Acts mentioned in this Guide:

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Act</th>
</tr>
</thead>
<tbody>
<tr>
<td>CARES Act</td>
<td>Coronavirus Aid, Relief, and Economic Security Act</td>
</tr>
<tr>
<td>FAST Act</td>
<td>Fixing America's Surface Transportation Act</td>
</tr>
<tr>
<td>JOBS Act</td>
<td>Jumpstart Our Business Startups Act</td>
</tr>
<tr>
<td>Securities Act</td>
<td>Securities Act of 1933</td>
</tr>
<tr>
<td>2017 Act</td>
<td>Tax Cuts and Jobs Act of 2017</td>
</tr>
</tbody>
</table>