

FASB Improves Discount Rate Guidance for Lessees That Are Not Public Business Entities

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The Financial Accounting Standards Board (FASB) recently issued Accounting Standards Update (ASU) 2021-09 that revises the application of discount rate guidance for lessees that are not public business entities.

Background and Overview

ASU 2021-09 provides for lessees that are not public business entities to use a practical expedient that allows them to make an accounting policy election to use a risk-free rate as the discount rate for all leases. The FASB received feedback that some private companies were reluctant to use the risk-free rate election for all leases because a risk-free rate, such as a U.S. Treasury rate, is low compared to their expected average incremental borrowing rate and, using the risk-free rate, could increase an entity's lease liabilities and right-of-use assets. The following are the significant aspects of the accounting update:

- ASU 2021-09 allows a non-public entity to use the risk-free rate as its discount rate by class of underlying asset when accounting for leases under ASC Topic 842. Entities that make this election are required to disclose the class of underlying assets to which the risk-free rate was applied.
- ASU 2021-09 also requires that if the rate implicit in the lease for any individual lease is readily determinable, it must be used instead of the risk-free rate or an incremental borrowing rate.

Effective Dates

ASC 842 is effective for private companies and certain not-for-profit entities for annual periods beginning after December 15, 2021, and interim periods in annual periods beginning after December 15, 2022.

Entities that have not yet adopted ASC 842 as of November 11, 2021 are required to adopt ASU 2021-09 when they adopt ASC 842.

For entities that have adopted ASC 842 as of November 11, 2021, ASU 2021-09 is effective for fiscal years beginning after December 15, 2021, and interim periods in annual periods beginning after December 15, 2022. Early adoption is permitted.

For a complete version of ASU 2021-09, click [here](#).

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