

ACC06

Accounting for Leases and Portfolio Decisions of Active Corporate Bond Funds

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Abstract

This study examines the impact of the new lease standard, ASC 842, on the portfolio decisions of active corporate bond funds. ASC 842 requires firms to recognize operating leases on the balance sheet and disclose additional information to support this recognition. Using monthly portfolio holdings, I find that shortly after its implementation, active corporate bond funds reduce holdings of bonds issued by firms with significant exposure to operating lease recognition. Further analyses show the effect is more pronounced for non-sophisticated funds, high-yield funds, issuers with more overestimated imputed interest rate (underestimated as-capitalized operating leases) and more complex leasing activities questioned by regulators. These findings suggest that active corporate bond funds fail to fully adjust for off-balance-sheet operating leases and underestimate credit risks of de facto riskier holdings under the legacy lease accounting standard. This study is the first to highlight the impact of accounting reporting changes on the portfolio decisions of active corporate bond funds and provides evidence to FASB during its post-implementation review of the ASC 842.

Conference Track

Accounting