P.A. Pieterse van Wijck
Van der Helstlaan 67
1412 HJ Naarden
The Netherlands

dalw@xs4all.nl

December 14, 2010

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

ED 2010 9 Leases

Sir,

Conceptually a lease is simply one of the many ways by which an entity can make benefits (both positive and negative) embodied in a resource, flow to the entity. In other words, leasing is simply one of the many ways by which an entity may acquire assets. Whether these benefits are tangible (a good) or intangible (a service), limited in time or not, or any other distinction with respect to nature of the benefits or characteristics of the transaction, is completely irrelevant. The overriding recognition principle is, that benefits that can be made to flow by an entity to that entity, constitute an asset and should be presented in the statement of financial position. Obviously the corresponding obligation should be presented in the statement of financial position as well.

The price of any acquisition of benefits embodied in a resource includes rewards (considerations) for all cost categories incurred by the resource provider. There is no (conceptual) reason to present these rewards as separate cost elements in the financial statements of the acquiring entity, unless these rewards relate to benefits, which are separately identified in the acquisition contract.

Acquisition of benefits embodied in a resource by an entity inevitably leads to de-recognition of that resource by the resource provider.

The above reasoning leads to the following answers on the questions.

Q1.

a. Yes, because it abandons the erroneous distinction between operating and financial lease. On the other hand, introducing a standard on lease is unnecessary. The Board might instead consider preparing a general standard on recognizing and measuring assets, rather than issuing standards which focus on the nature of the asset or the method of acquisition.

b. No.

As a result of the Board's approach, the caption "interest expense" in an entity's financial statements is in actual fact a mixture of cost of cash provided (interest in its "purest" form, i.e. a cash outflow to the cash provider), cost incurred for not paying on delivery as agreed between parties and cost assumed to be incurred for not paying on delivery, calculated at an imaginary rate. Especially in this latter case "interest expense" cannot be considered to reflect economic reality. The Board might consider to eliminate from the various standards this and similar assumptions, which lead to recognizing and measuring assets and liabilities at values that do not reflect economic reality.

Q2

No for both a. and b. See my reasoning above.

Q3

Yes, but not because it is conceptually right, but because it is practical.

Q4

A definition of a lease is not necessary. Nevertheless, I do have the following comments:

With reference to the current definition of an asset, it is inconsistent that the definition of a lease as well as §§ B1 thru B4 refer to (an) asset(s). It would be more appropriate to replace "asset" by "resource".

The criterion "more than an insignificant amount of ..." introduced § B4a is flawed and impractical. It is flawed, because, given the definition of an asset, the criterion should simply be that a benefit can be made to flow to the lessee. §B4b describes just one of the many means of this flow and is thus an unnecessary paragraph. §B4c, first part of the criterion is the same as §B4a and is thus a useless criterion.

In § 8a a definition of a purchase is provided. Again with reference to the definition one would have expected that this definition would have included wording about ability to make the benefits embodied in a resource flow to the entity. Instead the inconsistent and impracticable notion of "...all but a trivial amount of the risks and benefits" is used.

This inconsistent application of the definition of an asset, leads to a major flaw in the approach of the Board with respect to recognizing a lease. A lease transfers the right of use of a resource to another entity resulting in:

- the receiving entity (lessee) enjoying some (but not all) of the benefits of that resource for a period of time and
- the transferring entity not being able to enjoy these benefits anymore during that period.

Compared to the moment prior to entering into the (lease) contract the value of the resource (which is the sum of the benefits included in it) has decreased, whereby that (decrease in) value has been replaced by a contractual right to receive a consideration. Logically, the benefits that have been transferred need to be de-recognized; it is inconceivable that a transfer of benefits to a lessee does not lead to de-recognizing these benefits by the lessor! In other words, the performance obligation model is fundamentally wrong and the de-recognition model is the only right one. De-recognition is

in fact a continuum, whereby on the one end the value of benefits embodied in a resource transferred tends to nil, and whereby on the other end this value tends to the full original (prior to the lease transaction) value. In the latter end of the continuum it is for instance the contractual time limit in the flow of the benefits that causes the value of de-recognition being different from a sale of all benefits embodied in the resource (constituting the asset for the lessor) by the lessor entity and a purchase by the lessee entity.

The Board considers "significant risks and benefits" as the criterion to determine applicability of the performance obligation approach or the de-recognition approach. What the Board in fact tries to accomplish is to determine a range on the continuum, whereby anything outside this range should be reported by means of the performance obligation approach. The undesirable result of this approach is that both lessor and lessee will present the same benefit in their financial statements, albeit under different descriptions. Another problem of the approach is, that is it unknown what "significant" is and that consequently interpretation of this criterion will be subjective, leading to diverging application in practice.

Finally, in § B9 a definition (or description) of sale or purchase (acquisition) is given. To my knowledge, this is the first time in IFRS that a definition of these key elements of economic activity is provided. One would have expected that such description would have been presented as one of the fundaments of the Conceptual Framework. Unfortunately, in this description as well the Board mixes up asset and benefits embodied in a resource. An entity does not have control over an asset; it has control over the benefits (both negative and positive) embodied in a resource and therefore these benefits are called an asset.

Q5

The scope exclusions are a direct consequence of the failure to recognize that not a standard on lease is required, but rather a general standard on recognizing and measuring assets.

Q6

The distinction between lease (method of acquiring benefits) components and service (nature of benefits) components is conceptually both wrong and unnecessary.

Q7

Purchase options are relevant only to the extent that these contribute to the assessment of the probability that benefits will indeed flow to the entity and thus need be recognized and measured.

Q8

Yes, provide that "lease" is substituted by "the term over which the benefits will flow to the entity".

Q9 and Q10

Yes, in the sense that the (re-)measurement guidance provided should be applied for all types of transactions whereby benefits in a resource are acquired, not only for "lease" transactions.

Q11

No, because the distinction is unnecessary.

Q12

a. Assets should be presented by nature; the method of acquisition should not lead to a distinction in classification. Liabilities other than incurred in exchange for cash provided are not "financing liabilities" and accordingly should not be presented as such.
b. The performance obligation approach is in my opinion wrong, as explained above.
c. A financial asset is a right to receive cash in return for cash provided. The right to receive payments in exchange for the transfer of benefits embodied in a resource to another entity is not a financial asset and consequently is to be presented separately from financial assets.
d. No. Assets and liabilities should primarily be classified by nature, not by method of acquisition or disposition.

Q13.

No. Income and expense should primarily be classified by nature, not by method of use or exchange.

Q14.

No. Cash flows should primarily be presented by nature of the asset or liability that created the cash flow.

Q15.

Generally the objectives of disclosures are:

a. To describe the basis (contractual, statutory or constructive obligation) for recognizing the asset or liability
b. To describe the method of measuring the asset or liability
c. To explain the amount at which the asset or liability is measured

No need exist to separately address future cash flows, because principally financial statements present the outcome of the conversion and exchange process any entity is engaged in, not future possible outcomes.

I have no answers with respect to Q16 thru Q18.

Please note that the above views are my personal views, not the views of any of the organizations I am related to.

Sincerely Yours,

P. A. Pieterse van Wijck