

1850-100 Comment Letter No. 557

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Technical Director
Financial Accounting Standards Board
401 Merritt 7
P O Box 5116
Norwalk, CT 06856-5116
File Reference No. 1850-100

Dear Director:

Thank you for allowing us the opportunity to provide our comments on the FASB exposure draft for the proposed Accounting Standard Update Topic 840- Leases.

We are a NYSE listed national retailer with over 480 leased locations. We appreciate the importance of harmonizing US GAAP and IFRS. However due to the number of leases we currently hold, and are expected to enter into in the future, the proposed change in accounting method will have a significant impact on our financial statements. As such we have certain concerns.

As a retailer, our store occupancy (rent) charges are reported in our cost of goods sold and impacts gross profit margin. In order to retain comparability between reporting periods, and to not overstate gross profit margin, we would have to charge the amortization of the right-of-use asset to cost of goods sold in lieu of rent (lease payments). In other words the amortization arising from various long-term leases would have to be reported in the same line items in our financial statements as the operating lease payments are currently. In addition, the interest component of the lease payment would need to follow the amortization to the same line items on our financial statements. Charging interest on a right-of-use asset to non-operating interest expense would greatly obscure true interest incurred from financing which would need to be derived from the footnotes for clarity. Other than stating that interest expense arising from right-of-use assets should be presented, or disclosed, as a separate interest expense line item, the draft does not directly address the issue of charging interest of this nature elsewhere (i.e. operations), and as such we would appreciate if the guidance specifically addressed this issue.

In addition, we do not agree with capitalizing three year or less operating leases where the economic useful life may be significantly beyond the lease period. This applies especially to smaller items such as office equipment and other rapidly replaced devices. The complexity and costs of implementing such a sweeping accounting change in considering the minimal value it would yield for readers of financial statements is difficult to justify.

We will address our additional concerns in our responses to the questions posed by the board:

Question 1: Lessees

A) Do you agree that a lessee should recognize a right-of-use asset and a liability to make lease payments? Why or why not? If not, what alternative model would you propose and why?

Though we believe the current accounting is adequate, in the spirit of harmonizing US GAAP and IAS recognizing a right-of-use asset on significant long-term leases would be acceptable.

B) Do you agree that a lessee should recognize amortization of the right-of-use asset and interest on the liability to make lease payments? Why or why not? If not, what alternative model would you propose and why?

The amortization of such asset along with the interest component should logically occur. However, in order to maintain comparability with previously issued financial statements, the charges should be reported in the financial statements exactly where the current lease payments are being charged.

Question 3: Short-term leases

This exposure draft proposes that a lessee or a lessor may apply the following simplified requirements to short-term leases, defined in Appendix A as leases for which the maximum possible lease term, including options to renew or extend, is 12 months or less:

A) At the date of inception of a lease, a lessee that has a short-term lease may elect on a lease-by-lease basis to measure, both at initial measurement and subsequently, (i) the liability to make lease payments at the undiscounted amount of the lease payments and (ii) the right-of-use asset at the undiscounted amount of lease

payments plus initial direct costs. Such lessees would recognize lease payments in the income statement over the lease term (paragraph 64).

Do you agree that a lessee or a lessor should account for shortterm leases in this way? Why or why not? If not, what alternative approach would you propose and why?

While we believe the current accounting for such leases is adequate, should the boards ultimately conclude on requiring the recognition of a right-of-use asset, we believe all short term leases currently classified as operating leases should be be treated in this manner (undiscounted). The ability to evaluate each short-term lease on a lease by lease basis should extend to leases whose terms extend beyond 12 months (i.e. office copiers).

Question 4

- A) Do you agree that a lease is defined appropriately? Why or why not? If not, what alternative definition would you propose and why? B) Do you agree with the criteria in paragraphs B9 and B10 for distinguishing a lease from a contract that represents a purchase or sale? Why or why not? If not, what alternative criteria would you
- C) Do you think that the guidance in paragraphs B1-B4 for distinguishing leases from service contracts is sufficient? Why or why not? If not, what additional guidance do you think is necessary and why?

We are in agreement with the definitions and guidance related to questions 4a, 4b and 4c. However, we believe there could be more clarity on what constitutes sufficient transfer of risks with regards to the underlying asset, and some additional guidance on what would define or constitute a "trivial amount of risk."

Question 5: Scope exclusions

propose and why?

This exposure draft proposes that a lessee or a lessor should apply the proposed guidance to all leases, including leases of right-of-use assets in a sublease, except leases of intangible assets, leases of biological assets and leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources (paragraphs 5 and BC33–BC46).

Do you agree with the proposed scope of the proposed guidance? Why or why not? If not, what alternative scope would you propose and why?

We agree with the exclusions with the exception of subleases which we have addressed in response to Question 12.

Question 8: Lease term

Do you agree that a lessee or a lessor should determine the lease term as the longest possible term that is more likely than not to occur taking into account the effect of any options to extend or terminate the lease? Why or why not? If not, how do you propose that a lessee or a lessor should determine the lease term and why?

We respectfully disagree with the board regarding the lease term. We believe only the known, legally binding, lease term should be the basis for the term. Moreover, it would be difficult to estimate with accuracy and certainty events extending out 20 years. In addition, this can become problematic with regards to the amortization of leasehold improvements as currently they are recognized over the shorter of their useful lives or the duration of the lease. We believe the boards need to provide some additional guidance on the issue of the amortization period, to determine if it will be required to be extended over the estimated renewal periods (if less or equal to the useful life), and if it would possibly result in a bifurcation of treatment in that the liability could extend for a greater period than the amortization of leasehold improvements.

Question 9: Lease payments

Do you agree that contingent rentals and expected payments under term option penalties and residual value guarantees that are specified in the lease should be included in the measurement of assets and liabilities arising from a lease using an expected outcome technique? Why or why not? If not, how do you propose that a lessee or a lessor should account for contingent rentals and expected payments under term option penalties and residual value guarantees and why?

Do you agree that lessors should only include contingent rentals and expected payments under term option penalties and residual value guarantees in the measurement of the right to receive lease payments if they can be reliably measured? Why or why not? We believe strongly that contingent rent should not be included in the present value calculation. The contingency is typically triggered by success (or failure) to achieve goals within a specific period. Provided that such contingencies are annual, we strongly believe that such costs are period costs and should be accounted for accordingly. If contingent rent must be included, then a reasonable estimate of expected payments (based on known and historical/trended data) should be used as a basis rather than a probability-weighted average based calculation.

Question 10: Ongoing reassessments

Do you agree that lessees and lessors should remeasure assets and liabilities arising under a lease when changes in facts or circumstances indicate that there is a significant change in the liability to make lease payments or in the right to receive lease payments arising from changes in the lease term or contingent payments (including expected payments under term option penalties and residual value guarantees) since the previous reporting period? Why or why not? If not, what other basis would you propose for reassessment and why?

Ongoing reassessments should not be routinely required but rather should occur only in the event of a triggering event, analogous to impairment of an asset "where impairment indicators exist." Should there be an actual material change ("indicator"), then a reassessment should be required. In that light, perhaps the literature could provide certain specific criteria that would outline various triggering events.

Question 11

Do you agree with the criteria for classification as a sale and leaseback transaction? Why or why not? If not, what alternative criteria would you propose and why?

We agree with the criteria for sale and leaseback transactions as it provides consistency between the current treatment of a sale-leaseback transaction and the proposed treatment for the recognition of a right-of-use asset.

Question 12: Statement of financial position

A) Do you agree that a lessee should present liabilities to make lease payments separately from other financial liabilities and should present right-of-use assets as if they were tangible assets within

property, plant and equipment, but separately from assets that the lessee does not lease (paragraphs 25 and BC143-BC145)? Why or why not? If not, do you think that a lessee should disclose this information in the notes instead? What alternative presentation do you propose and why?

We agree that both the assets and liabilities arising from the right-of-use assets should be presented separately in the statement of financial position. However we also believe that leases for like items and similar characteristics should be aggregated and reported as separate right-of-use asset items depending on materiality.

D) Do you agree that lessors should distinguish assets and liabilities that arise under a sublease in the statement of financial position (paragraphs 43, 60, BC150 and BC156)? Why or why not? If not, do you think that an intermediate lessor should disclose this information in the notes instead?

We agree with reporting assets and liabilities arising from subleases separately, but only if material. We also would appreciate some clarity on the treatment of subleases where risk is transferred substantially from an existing lessee to a counter-party (sub lessee). We are concerned that this may lead to a recognition of the asset and liability on the financial statements of both the sublessor and sublessee and therefore be double counted.

Question 13: Income statement

Do you think that lessees and lessors should present lease income and lease expense separately from other income and expense in the income statement (paragraphs 26, 44, 61, 62, BC146, BC151, BC152, BC157 and BC158)? Why or why not? If not, do you think that

We strongly disagree that lease expense should be presented separately in the income statement. It is imperative that the items be charged to the very same line items on the income statement that such activity is currently charged to. This would not only maintain comparability but proper expense aggregation and representation.

Question 14: Statement of cash flows

Do you think that cash flows arising from leases should be presented in the statement of cash flows separately from other

cash flows (paragraphs 27, 45, 63, BC147, BC153 and BC159)? Why or why not? If not, do you think that a lessee or a lessor should disclose this information in the notes instead? Why or why not?

We believe that as a lessee the treatment for such activity in the statement of cash flows should be consistent with current treatment for capital lease obligations within the financing section, although be reported on a separate line. Concurrently, the investments of which should be disclosed in supplemental disclosures of non-cash investing activities.

Question 15

Do you agree that lessees and lessors should disclose quantitative and qualitative information that:

- (a) identifies and explains the amounts recognized in the financial statements arising from leases; and
- (b) describes how leases may affect the amount, timing and uncertainty of the entity's future cash flows?

We agree with the disclosure requirements as currently outlined in the exposure draft.

Question 16

A) This exposure draft proposes that lessees and lessors should recognize and measure all outstanding leases as of the date of initial application using a simplified retrospective approach (paragraphs 88–96 and BC186–BC199). Are these proposals appropriate? Why or why not? If not, what transitional requirements do you propose and why?

We agree with the simplified retrospective approach.

B) Do you think full retrospective application of lease accounting requirements should be permitted? Why or why not?

We believe for the sake of full industry comparability (between like companies) that only one method should be required, and that the full retrospective application should not be permitted.

C) Are there any additional transitional issues the boards need to consider? If yes, which ones and why?

We believe that some additional clarity should be provided regarding the treatment and disclosure of the deferred rent balances related to the right-of-use leases during transition.

Question 17

Paragraphs BC200–BC205 set out the boards' assessment of the costs and benefits of the proposed requirements. Do you agree with the boards' assessment that the benefits of the proposals would outweigh the costs? Why or why not?

In considering the potential expenses and commitment of resources that would arise from this change in lease accounting, and the benefits it may yield, we do not believe the potential benefits would outweigh the sizable costs and effort. For instance this will require additional software for lease tracking beyond what we currently use, as well as the implementation of an enhanced fixed asset system to accommodate the large influx of new assets and depreciation calculations. In considering this along with the additional manpower needed to maintain and implement such systems, we strongly believe these additional costs to implement the new accounting will add little share holder value.

Other comments

Question 18

Do you have any other comments on the proposals?

Regarding rent credits and landlord construction allowances, there needs to be clarity on the treatment for these items upon transition and for ongoing activity throughout the life of the lease.

Please clarify the calculation of the incremental borrowing rate in terms of application during reassessment and impairment, as well as the initial calculation of the incremental rate. We would like to know if a different rate would be permissible to use should circumstances change during reassessment or any other revaluation.

Thank you again for allowing us the opportunity to share our views on the exposure draft.

Very truly yours,

Michael Archbold

EVP & Chief Financial Officer