GREEN GROUP ENERGY COLLABORATIVE (GREENCO)

Ms. Leslie Seidman
Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

February 8, 2012

Dear Ms. Seidman:

GREENCO is a collaboration of all the major participants in implementing energy efficiency projects in New York's hospitals: the hospitals themselves, ESCOs and equipment vendors, financial institutions, utilities, multiple branches of government, legal and accounting experts and environmental advocacy groups. In an arrangement that is unique and potentially very powerful, these groups have come together to address a problem that all see and want to solve: achieving energy and cost savings, reducing negative environmental impact, and improving employee and patient health through capital investments in energy efficiency.

In collaboration with the Healthcare Association of New York State (HANYS) and its member organizations, GREENCO would like to express its concerns about the potential unintended consequences of the proposed changes to FASB 13 described in the Re-Exposure Draft.

In the Leases Exposure Draft (ED), the accounting boards¹ defined a lease as a contract in which the right to use a specified asset is conveyed, for a period of time, in exchange for consideration.² As of December 23, 2011, the accounting boards have tentatively decided the following in relation to applying that definition:

- 1. An entity would determine whether a contract contains a lease on the basis of the substance of the contract, by assessing whether:
 - a. The fulfillment of the contract depends on the use of a specified asset; and
 - b. The contract conveys the right to control the use of a specified asset for a period of time.
- 2. A contract would convey that right to control the use if the customer has the ability to direct the use, and receive the benefit from use, of a specified asset throughout the lease term.

¹ The "accounting boards" include the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB).

² IASB/FASB 21 March 2011 available at http://bit.ly/zha5nH.

- A "specified asset" refers to an asset that is explicitly or implicitly identifiable.
- 4. A physically distinct portion of a larger asset of which a customer has exclusive use is a specified asset.

A strict reading of the ED may suggest that the equipment component of any service contract will be treated as an operating lease. While this treatment may make sense in many circumstances, we believe it would have unintended and potentially perverse consequences if applied woodenly to performance-based energy-efficiency service agreements (ESAs).

ESAs allow customers to implement energy-efficiency improvement projects without an upfront capital investment. The mechanics of an ESA work like so: an energy-efficiency service provider (ESA Provider) receives a license from a hospital customer to implement a broad range of measures designed to increase energy efficiency and reduce operating expenses. During the term of the agreement, the ESA Provider takes title to and owns all project-related equipment, and has the ability at its option to add or change the equipment installed, provides ongoing maintenance and maintains access and control to the efficiency improvements. In exchange for these services, the hospital customer makes periodic service payments based on the project's actual performance and associated reductions in utility costs and operating expenses.³ If no reductions in utility costs and operations are realized, the hospital customer pays nothing.

Unlike leases, ESA transactions are "executory contracts," which require both parties to perform. Hospitals that pursue energy-efficiency investments through an ESA would effectively be forced to place an operating expense in the form of future utility bills on their balance sheets. 5

The purpose of the FASB is to improve the reliability and usefulness of financial reporting practices by promoting consistency and accuracy across all types of industries and financial markets. Treating the equipment-component of an ESA as a lease would not advance these objectives, but would penalize hospitals for investing in energy-efficiency by effectively forcing them to put future utility payments on balance sheet.

Unintended Consequences

Hospitals account for more than nine percent of the energy used in the U.S. commercial-buildings sector and eight percent of greenhouse-gas (GHG) emissions in the United States. Hospitals in New York spend an estimated \$700 million annually on energy costs. A 20 percent reduction in energy costs at hospitals in New York would yield annual savings of roughly \$125 million.

³ The ESA payments include an output-based services charge, which is set on a price per unit of energy savings.

⁴ ESA transactions do not include unreasonable termination penalties or similar elements commonly considered indicative of "disguised leases."

⁵ This would arguably diminish the usefulness of financial reports by forcing entities to recognize liabilities and expenses for services that are yet to be provided.

As explained in comments previously submitted in response to the first ED,⁶ hospitals have limited access to debt financing and many hospitals will have no other sources of capital for needed equipment without the ability to execute a transaction that is not likely to affect their ability to finance their core mission of delivering quality patient care.

By eliminating legitimate uses of off-balance sheet financing used by hospitals converting an otherwise operating expense as a capital expense, FASB will further constrain access to capital for hospitals and accelerate the erosion of capital already taking place in our economy. Furthermore, the accounting standard proposed in the ED would potentially vitiate efforts by policy-makers to promote energy-efficiency, which is a critical component of many federal, state and local governments' strategies for achieving energy cost-savings and emissions reductions in the near to mid future.

GREENCO applauds the accounting boards for pursuing greater transparency, consistency and efficiency in financial-reporting practices. For this reason, we would urge the accounting boards to consider the potential unintended consequences likely to result from the ED carefully.

Thank you for your consideration of these comments.

Sincerely,

C. William Schroth Executive Director

⁶ See Comment Letter No. 171, December 7, 2010.