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Mr. Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

Mr. Russell Golden
Chairman
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, Connecticut 06856-5116
USA

Dear Mr Hoogervorst and Mr. Golden:

Re: ED/2013/6 Exposure Draft – Leases

The Canadian Bankers Association[1] (the "CBA") appreciates the opportunity to comment on the International Accounting Standards Board's ("IASB") Exposure Draft ED/2013/6 Leases (the "ED").

The CBA commends the joint efforts of both the Financial Accounting Standards Board (the "FASB") and the IASB (together, the "Boards") to work together to develop a single converged standard. A consistent framework maximizes comparability of reported results between global banks that report under different accounting frameworks.

Our earlier concerns remain, that current operating leases will result in recognition of an asset and a related liability on the balance sheet even though the risks of ownership of those assets are not transferred to the lessee. This may be misleading to users as economically, substantially all of those risks remain with the lessor. While we are disappointed that our previous views on not recognizing a right-of-use ("ROU") asset and a lease liability for operating leases were not

[1] The Canadian Bankers Association works on behalf of 56 domestic banks, foreign bank subsidiaries and foreign bank branches operating in Canada and their 275,000 employees. The CBA advocates for effective public policies that contribute to a sound, successful banking system that benefits Canadians and Canada's economy. The Association also promotes financial literacy to help Canadians make informed financial decisions and works with banks and law enforcement to help protect customers against financial crime and promote fraud awareness. www.cba.ca.

incorporated in the revised ED, we understand that the Boards have given it due consideration and have made a conscious decision to proceed with the proposed model. Therefore, our comments are made under the assumption that the Boards are not willing to revisit the issue. We highlight the following key concerns to be addressed by the Boards before the final standard is issued:

Classification of ROU Asset on the Balance Sheet

The ROU asset in substance is not a tangible asset; however it represents the right to use a tangible asset. The ED highlights that if the ROU asset is not presented separately on the statement of financial position, it should be classified in the same category as the underlying asset. We agree with this view.

In addition, within Appendix D (Amendments to other IFRSs) the Boards propose a consequential amendment to IAS 38 *Intangible Assets* to exclude ROU asset from its scope which we support.

We strongly support an explicit clarification in the final standard that the ROU asset does not meet the definition of an intangible asset to remove any doubt and prevent unintended interpretations.

Recognition and Classification of Lease Expense

We agree that the different approaches used by lessees to recognize leases should properly reflect the economic benefits consumed in the underlying transactions. However, given the disparity of views on whether leases are considered financing transactions, we recommend that the Boards allow preparers to present lease expenses in a way that is appropriate for their given industry. From the perspective of the banking industry, recognizing interest expense from leases distorts the net interest margin from core banking activities which is a key performance metric considered by the users of the Bank's financial statements. Leases do not represent the core operations of the banking industry and we therefore recommend that the Boards allow preparers the flexibility to present expenses for Type A leases in the same way as Type B leases (as non-interest expense). We believe this would be the most appropriate income statement classification for the banking industry as it would not distort net interest margin, a key metric in the banking industry.

Lease Term

The determination of the lease term will have a significant impact on the measurement of the ROU asset that is recognized. The ED includes a revised definition for determining the lease term. Our concern is that the definition proposed in the ED could potentially lead to different interpretations of the application of “significant economic incentive” by the preparers and inconsistency in application could lead to a wide range of results. While the basis for conclusion has provided some context and rationale for changing the definition of a lease term from the current definition under IAS 17, we request the Boards further clarify whether the revised definition expands the original scope of the lease term.

Transition

We further request that the IASB ensure that the effective date of the standard be at least three years from the date of issue to allow sufficient time to assess, gather data and modify systems in order to accommodate the proposed changes.

Disclosures

We believe that the ED has proposed substantial additional disclosures. When assessing disclosures we believe that the cost of compilation, implementation and ongoing compliance should be considered relative to the possible benefit. In this context, we believe that the objective of providing users with relevant information can be met without mandating specific granular reconciliations and other quantitative data. We recommend that the Boards allow preparers a greater degree of judgment with respect to disclosures taking into consideration the significance of these leases to the entity and its operations.

Sincerely,

Attachment: Appendix A – Responses to the IASB ED Questions

Appendix A: Responses to the IASB ED Questions

Question 1: Identifying a lease
This revised Exposure Draft defines a lease as "a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration". An entity would determine whether a contract contains a lease by assessing whether:

a) **fulfillment of the contract depends on the use of an identified asset; and**
b) **the contract conveys the right to control the use of the identified asset for a period in exchange for consideration.**

A contract conveys the right to control the use of an asset if the customer has the ability to direct the use and receive the benefits from use of the identified asset.

Do you agree with the definition of a lease and the proposed requirements in paragraphs 6-19 for how an entity would determine whether a contract contains a lease? Why or why not? If not, how would you define a lease? Please supply specific fact patterns, if any, to which you think the proposed definition of a lease is difficult to apply or leads to a conclusion that does not reflect the economics of the transaction.

Yes, we generally agree with the definition of a lease in the ED as it is fairly consistent with the existing lease standard.

However, the current definition for short-term leases includes leases with a maximum possible term under the contract, including options to extend, of 12 months or less. While we are supportive of the Board's decision to provide relief for short-term leases, we would recommend that the definition for short-term leases should be extended to 24 months. We acknowledge the Board's concern that extending the scope exclusions to leases of 12 months or more may give rise to material assets and liabilities not being recognized on balance sheet. However, as most short-term leases have lease terms that in reality extends beyond 12 months, we believe this would ensure that the scope exclusion for short-term leases does indeed in practice provide the intended relief to preparers without compromising the project's intended objective of greater transparency of leasing activities.

Further, we believe that the definition should be further refined to scope out service contracts which do not transfer the ROU assets from one contracting party to the other. Under the ED, service contracts would generally be scoped out, however, it would result in clearer guidance if they are explicitly excluded in line with the current standard IAS 17 paragraph 3.

Question 2: Lessee Accounting
Do you agree that the recognition, measurement and presentation of expenses and cash flows arising from a lease should differ for different leases, depending on whether the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset? Why or why not? If not, what alternative approach would you propose and why?

Yes, we agree that the recognition, measurement and presentation of cash flows should differ for different leases depending on whether the lessee is expected to consume more than an insignificant portion of the economic benefits in the underlying asset. The different approaches used to recognize the leases should properly reflect the economic benefits consumed in the underlying transactions.

However, given the disparity of views on whether leases are considered financing transactions, we recommend that the Boards allow preparers to present lease expenses in a way that is appropriate for their given industry. From the perspective of the banking industry, recognizing interest expense from leases distorts the net interest margin from core banking activities which is a key performance metric considered by the users of the Bank's financial statements. Leases do not represent the core operations of the banking industry and we therefore recommend that the Boards allow preparers the flexibility to present expenses for Type A leases in the same way as Type B leases (as non-interest expense). We believe this would be the most appropriate income statement classification for the banking industry as it would not distort net interest margin, a key metric in the banking industry.

Question 3: Lessor Accounting
Do you agree that a lessor should apply a different accounting approach to different leases, depending on whether the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset? Why or why not? If not, what alternative approach would you propose and why?

Yes, we agree that a different accounting approach should be applied to different leases as it would better reflect the nature of the underlying transactions.

Question 4: Classification of leases
Do you agree that the principle on the lessee's expected consumption of the economic benefits embedded in the underlying asset should be applied using the requirements set out in paragraphs 28-34, which differ depending on whether the underlying asset is property? Why or why not? If not, what alternative approach would you propose and why?

Yes, we agree as this would better reflect the nature of the underlying transactions.

Question 5: Lease term
Do you agree with the proposals on lease term, including the reassessment of the lease term if there is a change in relevant factors? Why or why not? If not, how do you propose that a lessee and a lessor should determine the lease term and why?

Yes, we generally agree. Under the proposals, the lease term is the non-cancellable period of the lease including periods covered by an option to extend the lease if the lessee has significant economic incentive to exercise the option and periods covered by an option to terminate the lease if the lessee has a significant economic incentive not to exercise the option. However, IAS 17 currently defines a lease as the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option**.**

While the basis of conclusion has provided some context and rationale we request the Boards further clarify whether the revised definition expands the original scope of the lease term. Our concern is that the definition proposed in the ED could potentially lead to different interpretations and inconsistency in application could lead to a wide range of results.

Question 6: Variable lease payments
Do you agree with the proposals on the measurement of variable lease payments, including reassessment if there is a change in an index or a rate used to determine lease payments? Why or why not? If not, how do you propose that a lessee and a lessor should account for variable lease payments and why?

We generally agree with the proposals on the measurement of variable lease payments as performance-based variable lease payments have been excluded from the measurement of the lease liability and lease receivable. However, the requirement to reassess variable lease payments (dependent on an index or rate) and the resulting adjustment to assets and liabilities will require significant time and effort to compute where the impact may not be significant for the banking industry. The ED currently requires reassessment at the end of every reporting period which for certain entities would be on a quarterly basis. We recommend that reassessment be required only on an annual basis unless there is an indication that the impact of the changes in the index or rate is significant. This would address the Board's desire for accurate measurement of lease assets or liabilities while limiting reassessments to once per year when changes are unlikely to be significant.

Question 7: Transition
Paragraphs C2-C22 state that a lessee and a lessor would recognize and measure leases at the beginning of the earliest period presented using either a modified retrospective approach or a full retrospective approach. Do you agree with those proposals? Why or why not? If not, what transition requirements do you propose and why?

Are there any additional transition issues that the boards should consider? If yes, what are they and why?

Yes, we agree. The ED requires retrospective restatement but provides transition reliefs under the modified retrospective approach. The computation of balances at the beginning of the earliest comparative period presented as opposed to the lease commencement date is less onerous for preparers while ensuring sufficient information for the users of financial statements.

We support the decision by the Boards to provide transition relief under the modified retrospective approach. However, consistent with the Board's decision to provide relief provided for IFRS 10 *Consolidated Financial Statements*, we recommend that similar relief should be provided for leases and that entities should not be required to recognize lease liabilities and ROU assets for leases previously classified as operating leases, if the term has ended before the end of the period in which the new standard has been applied. This will provide more useful information to users of the financial statements of banks as we do not view leasing as a financing transaction.

We further request that the IASB ensure that the effective date of the standard be at least three years from the date of issue to allow sufficient time to assess, gather data and modify systems in order to accommodate the proposed changes.

Question 8: Disclosure
Paragraphs 58-67 and 98-109 set out the disclosure requirements for a lessee and a lessor. Those proposals include maturity analyses of undiscounted lease payments; reconciliations of amounts recognized in the statement of financial position; and narrative disclosures about leases (including information about variable lease payments and

options). Do you agree with those proposals? Why or why not? If not, what changes do you propose and why?

We believe that the proposed disclosures, such as the quantitative reconciliation of opening and closing balances of ROU assets, lease liability, lease receivable and the residual asset are significantly more extensive than the current requirements to disclose the maturing analyses of undiscounted lease payments for operating leases. When assessing disclosures we believe that the cost of compilation, implementation and ongoing compliance should be considered relative to the possible benefit. We believe that the objective of providing users with relevant information can be met without mandating specific granular reconciliations and other quantitative data. We recommend that the Boards allow preparers a greater degree of judgment with respect to disclosures taking into consideration the significance of these leases to the entity.

Question 9 (FASB-only): Nonpublic entities
To strive for a reasonable balance between the costs and benefits of information, the FASB decided to provide the following specified reliefs for nonpublic entities:

a) **To permit a nonpublic entity to make an accounting policy election to use a risk-free discount rate to measure the lease liability. If an entity elects to use a risk-free discount rate, that fact should be disclosed.**
b) **To exempt a nonpublic entity from the requirement to provide a reconciliation of the opening and closing balance of the lease liability.**

Will these specified reliefs for nonpublic entities help reduce the cost of implementing the new lease accounting replacements without unduly sacrificing information necessary for users of their financial statements? If not, what changes do you propose and why?

No comment on this question.

Question 10 (FASB-only): Related party leases
Do you agree that it is not necessary to provide different recognition and measurement requirements for related party leases (for example, to require the lease to be accounted for based on the economic substance of the lease rather than the legally enforceable terms and conditions?) If not, what different recognition and measurement requirements do you propose and why?

No, we disagree. Under the FASB proposals, all leases should be accounted for by lessees and lessors that are related parties, based on legally enforceable terms and conditions of the lease. However, in our view and consistent with existing US GAAP, entities should be required to account for leases with related parties on the basis of their economic substance which is consistent with the requirements for all leases. This would better reflect the terms and conditions of the underlying transactions and ensure that the treatment is consistent with the IASB proposals.

Question 11 (FASB-only): Related party leases
Do you agree that it is not necessary to provide additional disclosures (beyond those required by Topic 850) for related party leases? If not, what additional disclosure requirements would you propose and why?

Yes, we agree. No additional disclosures are required as current requirements are in line with disclosure requirements for other related party transactions.

Question 12 (IASB-only): Consequential amendments to IAS 40
The IASB is proposing amendments to other IFRSs as a result of the proposals in this revised Exposure Draft, including amendments to IAS 40 *Investment Property*. The amendments to IAS 40 propose that a right-of-use asset arising from a lease of property would be within the scope of IAS 40 if the leased property meets the definition of investment property. This would represent a change from the current scope of IAS 40, which permits, but does not require, property held under an operating lease to be accounted for as investment property using the fair value model in IAS 40 if it meets the definition of investment property.

Do you agree that a right-of-use asset should be within the scope of IAS 40 if the leased property meets the definition of investment property? If not, what alternative would you propose and why?

No, we believe that the current scope of IAS 40 *Investment Property* should be maintained. Currently, the standard permits but does not require property held under an operating lease to be accounted for as investment property using the fair value model if it meets the definition of investment property. The use of a fair value model for a ROU asset is extremely complex and will require significant judgement and resources to maintain such assessments on an ongoing basis. As such, preparers should have the flexibility to use the model that best reflects their economic substance.