Crowe Horwath LLP
Independent Member Crowe Horwath International

One Mid America Plaza, Suite 700
Post Office Box 3697
Oak Brook, Illinois 60522-3697
Tel 630.574.7878
Fax 630.574.1608
www.crowehorwath.com

September 13, 2013

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Via email to *director@fasb.org*

Re: File Reference No. 2013-270

Dear Technical Director:

We are pleased to comment on the Financial Accounting Standards Board's (FASB or Board) Proposed Accounting Standards Update, *Leases (Topic 842) a revision of the 2010 proposed FASB Accounting Standards Update, Leases (Topic 840)* (Exposure Draft).

We appreciate the efforts being made by the Board to determine the need for improvements to the existing lease accounting model for both lessees and lessors. The Board has indicated that many financial statement users have long criticized existing lease accounting rules because they do not require lessees to recognize assets and liabilities arising from operating leases. To address this longstanding criticism, the Board undertook this project to amend existing requirements, among other provisions, so that lessees would recognize most operating leases on their balance sheets. In addition, the current lease accounting model has been criticized for being too "rules based" by providing bright-lined tests for determining operating vs. capital lease classification. It has been argued that this rules based approach has allowed some entities the opportunity to structure lease arrangements that look a lot like long-term financings as operating leases. These arrangements, commonly referred to as "off-balance sheet financings", result in no recognition of a liability in an entity's financial statements.

The proposals contained in the Exposure Draft do accomplish the Board's objective of recognizing the assets and liabilities resulting from operating leases on the balance sheets of lessee entities, however, they introduce two types of leases, Type A and Type B, with different accounting results. Two different accounting models will continue to provide lessees with opportunities to structure leases to achieve a certain accounting result. Lessors will also be required to apply the same two model approach to the classification and accounting for leases. We believe that both lessees and lessors should apply a single model to the accounting for lease transactions. We do not think that the benefit derived from the application of a two model approach outweighs the economic and human capital costs that would be expended to apply the amendments being proposed.

Further, under the proposed guidance lessees will generally recognize a right-of-use asset and corresponding lease liability in their balance sheets for all leases other than those meeting the short-term policy election. The Board has not indicated whether this asset should be considered a tangible or intangible asset and the proposed guidance does not provide a framework for preparers, auditors, or users of the financial statements to evaluate the classification of this right-of-use asset as a tangible or

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intangible asset. This is of particular concern for regulated depository institutions, such as banks and savings institutions, which are generally limited in the amount of intangible assets that can be held without regulatory capital deductions. Beyond the impact to the banking industry; it is not uncommon for commercial entities and others to have debt covenant requirements based on tangible net worth.

We believe the Board should explicitly define the right-of-use asset as a tangible or intangible asset. This could be accomplished by addition to the Master Glossary or could be included within the lease accounting guidance. We believe this is important since this is a newly defined asset and absent a Board position on this matter, there likely will be inconsistency, at least initially, in the treatment of this asset in measurements by lenders, regulators and other financial statement users.

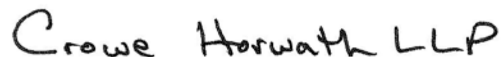
Although improvements have been made in the current proposal when compared to the 2010 Exposure Draft, we believe that the current proposal fails to provide a marked improvement over existing lease accounting rules. As discussed in more detail to our responses to individual questions, in some respects, we see the proposed changes introducing concepts that would add complexities in application that will present a significant burden for financial statement preparers without providing a corresponding benefit to financial statement stakeholders.

We strongly encourage the FASB to further consider the dissenting views provided by certain of its board members, input from the FASB's Investor Advisory Council (IAC), as well as responses from stakeholders on the proposal. Our understanding is that many financial statement users, including financial analysts, are comfortable with the existing lease accounting rules that have been in existence for many years. These users understand the information that is provided under existing rules and know how to interpret that information to provide useful decision-making information to interested stakeholders. While these users were encouraging the FASB to change and improve accounting for leases, our understanding is that many users do not believe the proposed guidance is an improvement over existing standards and therefore prefer existing standards to those being proposed. We believe it is very important to assess whether the proposed Exposure Draft achieves the original objectives.

Lastly, we have included several suggested alternatives that may be beneficial for nonpublic entities for the FASB and the Private Company Council to consider. We continue to believe there is high demand for these types of alternatives among private company financial reporting stakeholders.

Our comments to specific questions in the Exposure Draft are included in Attachment 1. Should you have any questions, please contact Scott G. Lehman at (630)574-1605 or scott.lehman@crowehorwath.com.

Sincerely,



Crowe Horwath LLP

ATTACHMENT 1

Question 1: Identifying a Lease - Do you agree with the definition of a lease and the proposed requirements in paragraphs 842-10-15-2 through 15-16 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.

We agree with the Board's decision to retain the concept that a lease can only result from a contract involving an asset that has been specifically identified.

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?

We challenge the need to differentiate leases between the two categories as proposed in the Exposure Draft defined as Type A and Type B leases. We believe that an approach with only one category, Type A leases, would both better serve financial statement users and enhance the comparability of lease obligations amongst lessees.

The lessee model for Type B leases solves one perceived issue – the "frontloading" of expenses that results from the application of the proposed Type A lease model (and current U.S. GAAP for capital leases). However, in addressing this problem, the problems created by Type B leases far outweigh any benefits derived as discussed further below.

- Type B leases result in the amortization of the right-of-use asset on a decelerated basis. The decelerated amortization of an asset is rarely permissible under existing U.S. GAAP. The model for Type B leases is therefore conceptually inconsistent with existing U.S. GAAP and would mandate an unusual amortization method for the right-of-use asset.

- The two-model approach would require lessees to perform additional analysis to classify and bifurcate all of its lease contracts, and the Type B model is unfamiliar to most financial statement preparers and users. Whereas the model for Type A leases is similar to existing U.S. GAAP for capital leases. As a result, the Type A model can more easily be analogized to the existing capital lease model (or to an asset purchase/financing model). In addition, software and other systems currently exist that would assist financial statement preparers with the necessary amortization schedules with little modification. The Type B model, on the other hand, has no similar model. Financial statement users will incur more costs to understand the new model and systems will likely need to be modified to enable financial statement preparers to amortize the right-of-use asset on a decelerated basis.

- Finally, a two-model approach for lease contracts may create opportunities for entities to structure lease agreements to achieve a certain accounting result which has long been a criticism of the existing lease accounting model. Although both Type A and Type B models require the entity to recognize the underlying assets and liabilities inherent in a lease contract, the separation of lease contracts based on whether the lessee is expected to consume more than an insignificant portion of the economic benefits of the leased asset inherently creates an opportunity for entities to structure lease contracts to achieve a desired accounting result. For example, the Exposure Draft would require an entity to classify a lease of property as a Type B lease unless the lease term is for the major part of the remaining economic life of the underlying asset. An entity with a 10 year lease of an older office building might argue that the age of the building indicates that it has a relatively short remaining economic useful life, when in fact it is longer, and therefore the lease contract meets the exception criteria of paragraph 842-10-25-7 and should be classified as a Type A lease. The entity may be motivated to make this argument because Type A lease costs are classified as amortization

and interest costs in the income statement. Therefore, Type A lease classification may cause the entity to pass a debt covenant based on EBITDA. Similarly, an entity that is leasing a machine with a debt covenant based on net income may wish to minimize the frontloading impact of a Type A lease, and may therefore may assert the total economic life is greater than it actually is in order to achieve Type B classification.

We strongly recommend the Board consider a model for lessees where all lease contracts are accounted for under the Type A model described in the Exposure Draft. Alternatively, if the Board were to continue to support the Type B model for lessees, we urge the Board to provide an option where a nonpublic entity would be permitted to adopt an accounting policy to treat all lease contracts as a Type A lease. Requiring a nonpublic entity to apply a two model approach to determine lease classification places and undue burden on an entity's financial reporting resources, without providing an incremental benefit to financial statement users.

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?

The Board initially began deliberating the merits of the existing lease accounting model because of criticism that the application of the existing model did not result in financial statements that adequately reflected a lessee's long-term cash obligations relating to leases classified as operating. Although not subject to the same criticism as the lessee accounting model, the Board is proposing wholesale changes to the existing lease accounting model for lessors that are symmetrical with the changes being proposed for lessees. We do not believe that a lessor should apply different accounting approaches to different leases. Consistent with our comments made regarding lease classification for lessees, as well as our comment letter on the 2010 ED, we propose that lessors be required to apply a single lessor lease accounting model, Type A. In our response to the 2010 ED, we proposed that lessors apply the "derecognition approach" for all leases other than land and sale leaseback transactions. This approach is most consistent with the Type A approach where income on the lease is recognized using the interest method over the term of the lease.

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 842-10-25-5 through 25-8, which differ depending on whether the underlying asset is property? Why or why not? If not, what alternative approach would you propose and why?

If the Board concludes to maintain the two lease model concept, we agree that the proscribed criteria is needed in order to determine appropriate classification between Type A and Type B. Though, we do not believe that the application of the "principles based" requirements set out in paragraphs 842-10-25-5 through 25-8 though will result in less structuring of lease classification than the existing "rules based" requirements. We foresee opportunities for such structuring in the interpretation of such phrases as "insignificant part, major part, and substantially all." We encourage the Board to provide more classification of leases implementation examples than what is currently presented in the Exposure Draft. Given the "principles based" nature of the proposed amendments, it is critical for such implementation guidance to be robust and include examples that preparers would likely encounter in practice.

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?

We agree with the proposed amendments to the definition of lease term and believe them to be an improvement from the amendments introduced in the 2010 Exposure Draft (ED) which proposed that the lease term would be based on 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. In our comment letter on the 2010 ED, we suggested the introduction of the term “significant” in relation the ability to cancel or extend a lease. We believe the current proposal to include the concept of a “significant economic incentive” threshold is more operational than the concept proposed in the 2010 ED. The inclusion of the “more likely than not” threshold without the term “significant” would have likely resulted in more reassessments, resulting in increased financial costs, that likely would have outweighed any benefits derived from a lower threshold. Though, we do encourage the Board to provide robust implementation guidance that includes “real-life” scenarios, that financial statement preparers are likely to encounter in practice, which detail how to apply the concept of “significant economic incentive” in determining the term of a lease.

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?

Existing capital lease guidance provides that leases with variable payments do not require an adjustment to the lease liability when payments tied to an index or rate change; rather changes in rates and indices are reflected in payments as they occur resulting in a favorable or unfavorable impact to lease expense. The application of the amendments proposed potentially result in positive or negative changes to the lease liability but, because the offset is charged to expense, it does not provide corresponding recognition to the right-of-use asset. This results in an asymmetric view of the lease arrangement.

The revaluation of the liability for each change in the variable payment as required by the Exposure Draft may likely cause an undue level of administrative costs on financial statement preparers who have multiple lease arrangements that are subject to indexes that likely change multiple times throughout the year. If the Board decides to retain the proposed requirement to reassess the lease when there is a change in the index or rate, we believe it would be helpful for the Board to clarify whether all changes (which would include even minimal changes in a rate or index) are required for the reassessment.

Question 7: Transition - Subparagraphs 842-10-65-1(b) through (h) and (k) through (y) 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 the Boards should consider? If yes, what are they and why?

We agree with the Board’s decision to allow for a modified retrospective approach or a full retrospective approach at the option of the lessee or lessor. Though, we also believe that entities should be allowed to recognize the cumulative effect of initially adopting the proposed amendments as an adjustment to the opening balance of retained earnings in the year of initial adoption (that is, comparative years would not be restated). We also suggest that entities provide additional disclosures regarding the impact of the initial application of the amendments on each financial statement line item. If the Board does not believe that such an option would be appropriate for public entities, we believe our suggested options should be allowed for nonpublic entities.

Question 8: Disclosure - Paragraphs 842-10-50-1, 842-20-50-1 through 50-10, and 842-30-50-1 through 50-13 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?

Overall, the proposed disclosures appear appropriate and necessary to provide financial statement users with the information necessary to understand how the reporting entity's leases were accounted for and reported in the financial statements. We do, however, have several suggestions for the Board to consider.

The proposed requirement to present a reconciliation of the opening and closing balances of the Type A and Type B lease liability stipulated in paragraph 842-20-50-4 is optional for nonpublic lessees and we agree with this option since such disclosures would present an . We also suggest that the Board consider providing disclosure relief for nonpublic lessors. As proposed, paragraphs 842-30-50-7 and 842-30-50-8 would require lessors to present a rollforward of opening and closing balances of the lease receivable and residual asset, respectively. We recommend that the disclosure requirements contained in these paragraphs also be optional for nonpublic entities regarding disclosure requirements.

In addition, paragraph 842-20-50-9 proposes that a lessee shall disclose a maturity analysis of commitments for nonlease components related to a lease, showing the undiscounted cash flows on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years. We are not certain why the Board is proposing this disclosure as such disclosure is not required when nonlease components are entered into independent of a lease. For example, when a lessee enters into a service agreement on a leased machine with a 3rd party as opposed to the lessor, the lessee is not required to provide such a disclosure.

Question 9: Nonpublic Entities (FASB Only) - 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:

1. **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.**
2. **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 requirements without unduly sacrificing information necessary for users of their financial statements? If not, what changes do you propose and why?

We commend the Board's decision to provide relief to help reduce the cost and effort to implement the proposed amendments for nonpublic entities. We agree that for many nonpublic entities, especially those with no comparable borrowings, the cost and effort to attempt to identify an appropriate incremental borrowing rate would outweigh any benefit from obtaining such a rate.

Our responses to Questions 2 and 8 above also include comments on other potential relief for nonpublic entities.

Question 10: (FASB Only) - 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?

The Exposure Draft indicates that related party leases should be assessed based on the legally enforceable terms of the lease and should not require special considerations of the related party relationships. However, we believe that it may be more difficult to objectively determine lease terms in some situations for related parties especially when considering the number of optional renewal periods. We believe it would be of great benefit to financial statement preparers if the FASB incorporated implementation guidance that addresses related party transactions in the final standard.

Question 11: (FASB Only) - 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?

We do not believe that it is necessary to require additional disclosures beyond those required by Topic 850 with respect to related party leasing arrangements.