



The voice of banking
& financial services

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London
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15 December 2010

Dear Sir David,

Exposure Draft ED/2010/9: Leases

This is the British Bankers' Association's response to the above exposure draft, we welcome the opportunity to comment. We share the view that the existing IAS 17 model based on the differentiation of leases into operating and financing categories has its shortcomings and therefore support the decision to develop a stronger standard which better meets the needs of users.

The Exposure Draft identifies three principal failings in the existing standard: i) the bright lines definition impeding comparability and exacerbating complexity, ii) a paucity of information about rights and obligations that meet the definition of assets and liabilities in the Conceptual Framework and iii) a failure to provide decision-useful information to users. We do not believe that the proposed standard addresses these shortcomings sufficiently for it to be regarded as an improvement and therefore urge the Board to conduct further work before proceeding.

For example, in seeking to remove the bright line between finance and operating leases, the proposed approach for lessees replaces one bright line with another between service contracts and leases. The choice of accounting treatment based on the proposed criteria is complex and we would therefore suggest the Board develop a definition of a lease which is both robust and operational. On the lessor side, the proposed approach relies on a complex division between four categories of transaction.

In terms of the consistency of the proposed model with the Conceptual Framework, we share the view expressed in AV 7 that the proposed standard fails to deal appropriately with payments for optional lease periods and contingent rentals which depend on the use of an asset (a concern expressed in our 17 July 2009 response to the Discussion Paper). The decision to require a lessee with a lease which has an initial term of X but an option to extend the lease by Y to estimate the most likely term, fails to reflect the fact that the lessee has no obligation to make payments beyond the initial term. In addition to introducing complexity and a significant degree of management judgement, this approach also creates an inconsistency as it will require a lessee to recognise possible liabilities for lease payments which are likely but not certain whilst not requiring the recognition of liabilities for unavoidable commitments to acquire services. An alternative approach might be to require the provision of enhanced disclosures.

Of the two models proposed on the lessor side, we see more merit in the application of the 'derecognition' model rather than the performance obligation approach as this is more aligned to lessee accounting. In addition, our view is that the performance obligation approach is conceptually flawed and results in effectively double-counting assets. This is particularly concerning for financial institutions as it will in effect result in a double capital charge. We would add that for preparers,

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continuous reassessment could be overly burdensome, especially where continual assessment is required around the lease term and the impact of contingent rentals.

The third point on which this project has been justified is to meet the needs of users. However, we remain to be convinced that the Board has identified what information users want from financial statements and whether the proposed standard will deliver this. We therefore suggest the Board to engage fully with the user community via further field work and outreach activities to ensure that the final standard meets users' needs. If nothing else, it is only after the benefits of the proposals can be clearly identified that a proper assessment can be made of whether or not the significant costs associated with the implementation of the proposals – including ancillary costs associated with loan covenants which may be impacted, tax legislation which may need to be changed (and if not aligned, the possibility of running two different models) – justify the benefits.

In conclusion, we urge the Board to give full and proper consideration to these concerns which we believe to be widely held before proceeding. We concede that this may not be compatible with the June 2011 completion date but we place greater emphasis on the development of a strong standard than the replacement of IAS 17.

Yours sincerely

A handwritten signature in black ink that reads "Paul Chisnall". The signature is written in a cursive, flowing style.

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