



CANADIAN FINANCE & LEASING ASSOCIATION  
ASSOCIATION CANADIENNE DE FINANCEMENT ET DE LOCATION

**BY Email:** [commentletters@iasb.org](mailto:commentletters@iasb.org)

December 15, 2010

International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

**Exposure Draft on Leases  
ED/2010/9**

Dear Sirs,

The Canadian Finance & Leasing Association ('CFLA' or 'Association') is pleased to respond to the Exposure Draft, ED/2010/9 Leases (the 'ED').

The CFLA represents the asset-based financing, equipment and vehicle leasing industry in Canada. CFLA members are the largest provider of debt financing in Canada, after traditional lenders such as banks and credit unions. As at December 31, 2009, the industry was financing C\$87.7 billion of assets, (approximately US\$86.9 billion as at the date of this letter) representing leases numbering in the millions. We estimate that between 20% and 25% of business capital assets are acquired through asset-backed financing and leasing in Canada each year.

The Association's more than 200 company members range from large multinationals to national and smaller regional domestic companies, crossing the financial services spectrum from manufacturers' finance companies and independent leasing companies, to banks, insurance companies, and suppliers to the industry. CFLA members provide financing and leasing to Canadian small, medium and large businesses as well as consumers.

As an Association, we assessed the ED proposals from the perspective of users of financial information as well as preparers of financial information. As users CFLA members are interested in both:

- the impact that the ED proposals will have on the quality and understandability of customer financial statements they use in adjudicating credit, and
- the potential impact that the ED proposals will have on the future design / acceptance / viability of leasing products.

As preparers, CFLA members are interested in finding a framework that appropriately reflects the economics and essence of the leasing model.

**General Comments**

CFLA recognizes the political sensitivity and the urgent need from a standard setter perspective to put these amendments to bed as quickly as possible. That being said, CFLA members also believe in the need to ultimately "get to the right answer"; one that is well thought out, internally consistent, and consistent with the economics of leasing activity.

As a user of financial information, CFLA members approach the exercise with a “debtor orientation”. They regularly use financial statements in making credit decisions with respect to their lessees and are keenly interested in a framework that provides consistent, quality, decision-useful information. Of most importance / relevance to members in reviewing a set of financial statements of a potential or existing lessee is the ability to assess the capacity of the lessee to meet the contractual cash flow requirements underlying the lease. Complex measurement requirements that introduce estimation risk would be considered to detract from the value of the information required from a credit adjudication perspective. Disclosure of key terms and optionality is necessary and sufficient in most cases for member purposes. If sufficiently fullsome, disclosure will provide information beyond contractual cash flows that other users might want for their purposes.

CFLA has several concerns with respect to the practicality of implementing some of the proposed guidance as it is currently presented relating to the Right of Use (“ROU”) model for lessee accounting. From an overall basis, it is CFLA’s view that the proposals will introduce a level of complexity and effort for all involved (lessees, lessors and other users of financial statements) without a commensurate increase in the quality of the information provided.

CFLA members recognize the challenge in developing a single model for lessor accounting given the broad range of activity that “leasing” encompasses. The Derecognition model, with some modification (as further discussed below) most faithfully represents the economic business model underlying most equipment and vehicle leasing activity (i.e. – financing).

Although CFLA does not yet have a solution, there may be some challenge in applying a one-size fits all model for lessees (beyond the initial recognition of the ROU asset and the Lease Obligation) given the range of lease products available and the specific reasons for entering into a lease arrangement.

**Overall, CFLA’s views are consistent with and expand upon Stephen Cooper’s Alternative View as set out in the ED.**

## **Specific Comments**

CFLA has identified the following key areas of concern with respect to the ED proposals.

**1. The definition of Lease Term to be used in deriving Minimum Lease Payments should remain consistent with the current IAS 17 definition. Optional periods should not be included unless there is an incentive for the lessee to exercise.**

- CFLA does not believe that market-based extension / renewal terms represent an unconditional obligation of the lessee and therefore do not meet the definition of a liability or contingent liability in IAS 37. Whether or not a lessee will exercise its rights under the renewal / extension option is solely within its discretion.
- Where renewal / extension is “obvious”, it is acknowledged that the extended term should be factored into the measurement of lease assets / liabilities for both lessees and lessors. The “more likely than not” threshold is too low. CFLA would suggest “reasonably certain” consistent with existing IAS 17 language. Qualitative considerations should be considered in assessing whether the lessee will be incented to exercise the renewal / extension option (i.e. -where equipment is specialized / strategic and hard to replace (NATURE OF ASSET), where pricing of the renewal / extension period rentals is favourable (BARGAIN RENEWAL), or where lessee will find it virtually impossible to meet the return conditions set out in the lease (TERMS OF LEASE)), in which case the renewal / extension term should be factored into the total lease term.
- Added estimation / measurement uncertainty introduced by the “longest term more likely than not to occur” will make the amounts recorded less clear / easy to understand for users. More emphasis will be required to understand lessee assumptions / scenarios considered or lessor assumptions with respect to what the lessee might do. Lessors will not have sufficient

information to reliably estimate lessee actions and therefore it is unlikely that lessee and lessor assumptions will align for any individual lease. CFLA does not believe that this will increase decision usefulness of information provided for users.

- Requiring the inclusion of potential extension / renewal terms which may not ultimately be exercised will result in an overstatement of the assets and liabilities associated with leases for lessees and an overstatement of the lease asset for lessors.
- Exercise of renewal / extension options in most cases will be based on business conditions that exist near the end of the lease term which cannot be reliably estimated at lease inception.
- Disclosure with respect to the existence and terms of renewal / extension options would provide users with sufficient information.

**2. Contingent Rentals should not be included in deriving Minimum Lease Payments unless they relate to an index or rate (consistent with current IAS 17 requirements) or represent “disguised minimum lease payments”.**

- Contingent rentals based on usage or other performance metrics are ultimately dependent on actions to be taken by the lessee and are not enforceable by the lessor until such actions are taken.
- Contingent rentals for equipment and vehicle equipment leases typically involve variable rents based on an index / rate (CPI, interest rate) or excess usage (intended to compensate for depletion of residual value). Contingent amounts beyond the base index / rate are typically not factored into the upfront pricing of the lease.
- The proposals should include qualitative considerations to include base rentals that have been “disguised” as contingent rent (“anti-avoidance measure”) using management’s best estimate rather than a probability weighted scenario analysis.
- Projecting contingent rentals beyond “disguised amounts” using a probability weighted scenario analysis will add considerable uncertainty / estimation risk. CFLA does not believe that it will add sufficiently reliable information for users of financial information to warrant the additional effort. It is unlikely that lessee and lessor assumptions will be aligned. It also is unlikely that the lessor will have sufficient information available to reliably estimate contingent rentals based on usage / performance.
- Variable lease payments should be based on the level of the index or the rate at the inception date rather than requiring lessees / lessors to estimate potential future economic conditions as the quality of those future estimates is unlikely to be reliable and the added effort would not produce greater decision-useful information for users.
- The impact of contingent rent or variable rental features could readily be conveyed through note disclosures, including information relating to the terms of the contingency / variability and actual in-period adjustments required in each of the last 3 years (for example).

**3. The requirement to continually reassess and re-measure assets and liabilities associated with leasing each period should be removed.**

- Continuous reassessment of lease term and lease payments will require significant effort, and therefore administrative cost burden, particularly for lessees and lessors with large lease portfolios. Proposals in the ED to only quantify when change is expected to be significant will not sufficiently simplify the exercise.

- The lease term determined at inception should not be changed unless a renewal / extension term not previously included is committed to.
- Contingent rentals beyond the base “disguised amounts” described above should be recorded when incurred. The impact of these additional payments can be best understood through separate disclosure and / or presentation.
- Reassessing the impact that current excess rentals might have on future periods introduces the potential for volatility from period to period based on assumptions / estimation. It is unclear that this will provide added value to users of the financial statements.
- Continuous reassessment also introduces the potential for “fine-tuning” assumptions from period to period to achieve a desired income result which would seem contrary to the intended objectives of the ED.

**4. The criteria used to determine when the Derecognition model versus the Performance Obligation model applies should be more closely linked to the lessor’s business model.**

- Most equipment and vehicle lessors would describe their business model as that of financing. The arrangements typically involve a single lessee for the life of the contract with the asset disposed of at the end of term (either to the lessee or to the market). The asset is typically acquired for that single purpose and is not redeployed. The pricing of the contract is set to achieve a desired rate of return on the lessor’s investment in the leased asset, through the combination of payments from the lessee and expected cashflows from the final disposition of the asset if not transferred to the lessee.
- There may be some equipment and vehicle lessors that undertake leasing activity in the context of an asset management model (i.e. – where asset may be refurbished and redeployed to another lessee or potentially a secondary dealer market).
- Most real estate leases would likely not fit the Derecognition model as the asset is actively managed by the lessor and is often leased in parts (separate floors) and to multiple lessees over time.
- The criteria set out in the ED with respect to the applicability of the Derecognition vs Performance Obligation model is too explicit and would in fact result in many equipment and vehicle lessors being classified as asset managers. Perhaps the qualitative criteria provided should focus not on what happens during the term of the lease but whether or not the asset is redeployed at the end of the initial arrangement.
- Disclosure requirements could be added requiring lessors to describe the nature of their business and the model that best suits their business (along with supporting rationale) thereby ensuring that the financial statements reflect the business in a way that is most meaningful to its users.

**5. The Derecognition model should provide for accretion of the residual asset during the lease term. This is consistent with the view that leases accounted for under the Derecognition model are viewed as a financing activity**

- Lessors assess the overall economics of a lease transaction based on the cash flows to be received from the lessee as well as the final disposition of the asset.

**6. The Transition provisions should provide reporting entities with the choice of full retrospective application or the more simplified transition provisions outlined in the ED**

- CFLA continues to struggle with the lessee income recognition pattern proposed by the ED as it does not appear to match the pattern of benefits consumed over the term of the lease. Straight line recognition of rental expense (rather than interest expense and amortization expense) is in most cases the most meaningful representation of the cost of leasing activity from a lessee’s perspective.

- The income statement recognition pattern proposed will result in a front end loading of expense for the lessee and income for the lessor compared to current lease accounting due to the combination of effective interest method recognition on the lease obligation / finance receivable respectively and the straight line amortization of the ROU asset for the lessee versus prior straight line rental recognition. To the extent that this recognition pattern is retained the Transition provisions need to be amended to enable companies to avoid the “skew” that would be introduced by forcing all leases to commence the proposed recognition pattern at the same point in time. Typically a leasing portfolio includes leases at varying stages of their lifecycle therefore the front end loading impact is expected to naturally “smooth” over time. Recasting all leases based on remaining payments at the transition date will skew the results.

**7. The election not to recognize assets or liabilities arising from a short term lease should be applied to both lessees and lessors.**

- CFLA agrees with the definition of short term leases set out in the ED.
- CFLA also agrees that there should be simplified requirements for short term leases as the effort required to track and record short term leases would significantly outweigh the benefits provided.
- There should be symmetry between the treatment of short term leases by lessees and lessors.
- In CFLA’s view, the recording of lease payments in profit and loss over the lease term accompanied by disclosure with respect to the contractual commitments relating to leasing activity, similar to the disclosure requirements required today under IAS 17 would provide sufficient information for user purposes.

**8. There does not appear to be any study on the cost of implementing the proposals in the ED. CFLA members believe it to be substantial.**

As noted in the Conceptual Framework, “cost is a pervasive constraint on the information that can be provided by general purpose financial reporting. Reporting such information imposes costs and those costs should be justified by the benefits of reporting that information”. CFLA members are not aware of any study on the cost of implementing the proposals in the ED but they believe it to be substantial as described in the Appendix attached to this letter

If asked, CFLA would be willing to attempt to quantify the cost for leases with an equipment cost of less than C\$100,000. This would cover the bulk of leases by number in Canada.

The Association’s detailed responses to the questions in the ED are included in the Appendix attached to this letter.

If there are any questions arising from these comments or a further discussion would be helpful, please do not hesitate to contact the undersigned at [david.powell@cfla-acfl.ca](mailto:david.powell@cfla-acfl.ca).

Yours very truly,



David Powell  
President & Chief Executive Officer

**Question 1: Lessees**

- a) *Do you agree that a lessee should recognise 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?*
- b) *Do you agree that a lessee should recognise amortisation 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?*

CFLA members understand the desire for a lessee accounting model that eliminates the current distinction between operating and finance leases with respect to balance sheet presentation, and more particularly the recognition of a right-of-use asset and a liability to make lease payments with respect to all leases.

That being said, there are challenges in trying to define a single model for subsequent lessee accounting as not all leasing contracts are the equivalent of a financed purchase of an asset. Where the terms of the lease are such that the lessee is expected to utilize substantially all of the expected economic benefits of the leased asset, it is acknowledged that leasing is essentially equivalent to a financed purchase and that an income pattern equivalent to a financed purchase (i.e. – straight line amortization expense and effective interest expense on liability) makes most sense.

In all other cases, however, an expense pattern should be considered that reflects the lessee's consumption of the right of use benefits conveyed by the lease (i.e. – straight line in most situations) over time as rental expense is more meaningful for a user of financial statements. Artificially allocating the cost of leasing activity between amortization expense and interest expense does not provide decision-useful information.

**Question 2: Lessors**

- a) *Do you agree that a lessor should apply (i) the performance obligation approach if the lessor retains exposure to significant risks or benefits associated with the underlying asset during or after the expected lease term, and (ii) the derecognition approach otherwise? Why or why not? If not, what alternative approach would you propose and why?*
- b) *Do you agree with the boards' proposals for the recognition of assets, liabilities, income and expenses for the performance obligation and derecognition approaches to lessor accounting? Why or why not? If not, what alternative model would you propose and why?*

The Association acknowledges the difficulty in developing a model that can be applied to all leasing transactions and support the need for more than one model to address lessor accounting. CFLA believes that the criteria used to determine whether the performance obligation versus the derecognition model applies should be more closely linked to the lessor's business model for the following reasons:

- Most equipment and vehicle lessors would describe their business model as that of financing and as such, the arrangements typically involve a single lessee for the life of the contract with the asset disposed of at the end of term (either to the lessee or to the market). The asset is typically acquired for that single purpose and is not redeployed. The pricing of the contract is set to achieve a desired rate of return on the lessor's investment in the leased asset, through the combination of payments from the lessee and expected cash flows from the final disposition of the asset if not transferred to the lessee.
- There may be some equipment and vehicle lessors that undertake leasing activity in the context of an asset management model (i.e. – where asset may be refurbished and redeployed to another lessee or potentially a secondary dealer market).

- Most real estate leases would likely not fit the Derecognition model as the asset is actively managed by the lessor and is often leased in parts (separate floors) and to multiple lessees over time.
- The criteria set out in the ED with respect to the applicability of the Derecognition versus Performance Obligation model is too explicit and would in fact result in many equipment and vehicle lessors being classified as asset managers. Perhaps the qualitative criteria provided should focus not on what happens during the term of the lease but whether or not the asset is redeployed at the end of the initial arrangement.
- Disclosure requirements could be added requiring lessors to describe the nature of their business and the model that best suits their business (along with supporting rationale) thereby ensuring that the financial statements reflect the business in a way that is most meaningful to its users.

Furthermore, the lessor model should allow for the accretion of the residual asset during the lease term to better reflect the economics of the lease transaction. This is consistent with the view that leases accounted for under the Derecognition model are viewed as a financing activity. Lessors assess the overall economics of a lease transaction based on the periodic cash flows to be received from the lessee during the term of the lease, as well as from the final disposition of the asset.

Since most equipment and vehicle lessors would likely conclude that the Derecognition model best reflects the nature of their business model, CFLA has not provided specific comments on the application of the Performance Obligation model.

**Question 3: Short-term leases**

*Do you agree that a lessee or a lessor should account for short-term leases as described in the ED? Why or why not? If not, what alternative approach would you propose and why?*

CFLA agrees with the definition of short term leases set out in the ED.

There should be simplified requirements for short term leases as the effort required to track and record short term leases would significantly outweigh the benefits provided.

Also, there should be symmetry between the treatment of short term leases by lessees and lessors.

In CFLA's view, the recording of lease payments in profit and loss over the lease term accompanied by disclosure with respect to the contractual commitments relating to leasing activity, similar to the disclosure requirements required today under IAS 17 would provide sufficient information for user purposes.

**Question 4: Definition of a lease**

- Do you agree that a lease is defined appropriately? Why or why not? If not, what alternative definition would you propose and why?*
- 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 propose and why?*
- 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?*

CFLA agrees that a lease is defined as a contract in which the right to use a specified asset or assets is conveyed, for a period of time, in exchange for consideration.

There is no need to exclude in-substance purchases from the scope of the leasing standard. If the purchase option is reasonably certain of being exercised then it should ultimately be factored into the determination of lease payments, and therefore included in the recorded ROU asset and lease obligation by the lessee. The end result would seem to be consistent with a financed purchase. From a lessor perspective, inclusion of a reasonably certain purchase option in the lease payments would result in full derecognition of the leased asset and recognition of a financing receivable equivalent to the fair value of the leased asset. Again, this would seem consistent with a financed sale. As such, CFLA does not see the need to introduce a further level of complexity in assessing in-scope versus out of scope contracts.

CFLA supports the guidance in paragraphs B1 – B4 for distinguishing leases from services contracts. This guidance is generally consistent with current Canadian lease accounting framework and the current requirements in IFRIC 4.

**Question 5: Scope exclusions**

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

CFLA agrees with the proposed scope of the ED. We note that the exclusion of leases of intangible assets is consistent with current Canadian lease accounting framework (prior to transition to IAS 17).

**Question 6: Contracts that contain service components and lease components**

*If the service component in a contract that contains service components and lease components is not distinct:*

- a) *the FASB proposes the lessee and lessor should apply the lease accounting requirements to the combined contract.*
- b) *the IASB proposes that:*
  - i *a lessee should apply the lease accounting requirements to the combined contract.*
  - ii *a lessor that applies the performance obligation approach should apply the lease accounting requirements to the combined contract.*
  - iii *a lessor that applies the derecognition approach should account for the lease component in accordance with the lease requirements, and the service component in accordance with the proposals in Revenue from Contracts with Customers.*

*Do you agree with either approach to accounting for leases that contain service and lease components? Why or why not? If not, how would you account for contracts that contain both service and lease components and why?*

CFLA agrees that guidance for revenue recognition should be applied to a distinct service component of a contract that contains a service component and lease component. If the service component contained in a contract is not distinct, then the lease accounting requirements should be applied to the combined contract by both lessees and lessors. There should be symmetry in the lessee and lessor treatment of service components in a lease contract.

**Question 7: Purchase options**

*Do you agree that a lessee or a lessor should account for purchase options only when they are exercised? Why or why not? If not, how do you think that a lessee or a lessor should account for purchase options and why?*

CFLA disagrees that a lessee or a lessor should account for purchase options only when they are exercised. Purchase options should be included in the determination of lease payments when exercise is reasonably certain to occur. This is consistent with the response to question 8 below for extension and renewal options. CFLA believes that there should be consistent accounting treatment between purchase options and extension options included in a lease contract.

**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?*

CFLA does not agree that a lessee or lessor should determine that lease term as the longest possible term that is more likely than not to occur. It is proposed that the definition of lease term should remain consistent with the current IAS 17 definition. Optional periods should not be included unless there is an incentive for the lessee to exercise.

- Market-based extension / renewal terms do not represent an unconditional obligation of the lessee and therefore do not meet the definition of a liability or contingent liability in IAS 37. Whether or not a lessee will exercise its rights under the renewal / extension option is solely within its discretion.
- Where renewal / extension is “obvious”, it is acknowledged that the extended term should be factored into the measurement of lease assets / liabilities for both lessees and lessors. The “more likely than not” threshold” is too low. CFLA suggests “reasonably certain” consistent with existing IAS 17 language. Qualitative considerations should be considered in assessing whether the lessee will be incented to exercise the renewal / extension option (i.e. -where equipment is specialized / strategic and hard to replace (NATURE OF ASSET), where pricing of the renewal / extension period rentals is favourable (BARGAIN RENEWAL), or where lessee will find it virtually impossible to meet the return conditions set out in the lease (TERMS OF LEASE)), in which case the renewal / extension term should be factored into the total lease term
- Added estimation / measurement uncertainty introduced by the “longest term more likely than not to occur” will make the amounts recorded less clear / easy to understand for users. More emphasis will be required to understand lessee assumptions / scenarios considered or lessor assumptions with respect to what the lessee might do. It is also expected that lessors will not have sufficient information to reliably estimate lessee actions and therefore it is unlikely that lessee and lessor assumptions will align for any individual lease. CFLA does not believe that this will increase decision usefulness of information provided for users.
- Requiring the inclusion of potential extension / renewal terms which may not ultimately be exercised will result in an overstatement of the assets and liabilities associated with leases for lessees and an overstatement of the lease asset for lessors.
- Exercise of renewal / extension options in most cases will be based on business conditions that exist near the end of the lease term which cannot be reliably estimated at lease inception.
- Disclosure with respect to the existence and terms of renewal / extension options would provide users with sufficient information.

**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 measured reliably? Why or why not?*

Contingent rentals should not be included in the measurement of assets and liabilities arising from a lease, unless they relate to an index or rate or represent disguised minimum lease payments for the following reasons:

- Contingent rentals based on usage or other performance metrics are ultimately dependent on actions to be taken by the lessee and are not enforceable by the lessor until such actions are taken.
- Contingent rentals for equipment and vehicle equipment leases typically involve variable rents based on an index / rate (CPI, interest rate) or excess usage (intended to compensate for depletion of residual value). Contingent amounts beyond the base index / rate are typically not factored into the upfront pricing of the lease.
- The ED proposals should include qualitative considerations to include base rentals that have been “disguised” as contingent rent (“anti-avoidance measure”) using management’s best estimate rather than a probability weighted scenario analysis.
- Projecting contingent rentals beyond “disguised amounts” using a probability weighted scenario analysis will add considerable measurement uncertainty / estimation risk. CFLA does not believe that it will add sufficiently reliable information for users of financial information to warrant the additional effort. It is unlikely that lessee and lessor assumptions will be aligned. It also is unlikely that the lessor will have sufficient information available to reliably estimate contingent rentals based on usage / performance.
- Variable lease payments should be based on the level of the index or the rate at the inception date rather than requiring lessees / lessors to estimate potential future economic conditions as the quality of those future estimates is unlikely to be reliable and the added effort would not produce greater decision-useful information for users.
- The impact of contingent rent or variable rental features could readily be conveyed through note disclosures, including information relating to the terms of the contingency / variability and actual in-period adjustments required in each of the last 3 years (for example).

**Question 10: Reassessment**

*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?*

CFLA does not agree that lessees and lessors should remeasure assets and liabilities arising under a lease at each reporting period for the following reasons:

- The continuous reassessment of lease term and lease payments will require significant effort, particularly for lessees and lessors with large lease portfolios. The ED proposals to only quantify when change is expected to be significant will not sufficiently simplify the exercise.
- The lease term determined at inception should not be changed unless a renewal / extension term not previously included is committed to.
- Contingent rentals beyond the base “disguised amounts” described in question 9 above should be recorded when incurred. The impact of these additional payments can be best understood through separate disclosure in the financial statements.
- Reassessing the impact that current excess rentals might have on future periods introduces the potential for volatility from period to period based on assumptions / estimation. This will not provide added value to users of the financial statements.
- Continuous reassessment also introduces the potential for “fine-tuning” assumptions from period to period to achieve a desired income result which would seem contrary to the intended objectives of the ED.

Reassessment should occur only if there have been contractual changes in the terms of the lease.

**Question 11: Sale and leaseback**

*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?*

Sale and leaseback transactions are not commonly utilized by CFLA members. As such, the Association does not have any specific comments on this question.

**Question 12: Statement of financial position**

- 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 or investment property as appropriate, 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?*
- Do you agree that a lessor applying the performance obligation approach should present underlying assets, rights to receive lease payments and lease liabilities gross in the statement of financial position, totaling to a net lease asset or lease liability (paragraphs 42, BC148 and BC149)? Why or why not? If not, do you think that a lessor should disclose this information in the notes instead? What alternative presentation do you propose and why?*
- Do you agree that a lessor applying the derecognition approach should present rights to receive lease payments separately from other financial assets and should present residual assets separately within property, plant and equipment (paragraphs 60, BC154 and BC155)? Why or why not? Do you think that a lessor should disclose this information in the notes instead? What alternative presentation do you propose and why?*
- 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?*

CFLA agrees that a lessee should present liabilities to make lease payments separately from other financial liabilities in the statement of financial position. The Association agrees that a lessee should

present right-of-use assets as if they were tangible assets within property, plant and equipment or investment property as appropriate in the statement of financial position. A lessee should separately present owned and leased assets either in the statement of financial position or in the notes to the financial statements.

As noted in the response to Question 2 above, it is expected that most equipment and vehicle equipment lessors will conclude that the Derecognition model best reflects their business model. As such CFLA has not provided specific comments on presentation proposals relating to the Performance Obligation approach.

As noted in the response to Question 2 above, CFLA believes that the Derecognition approach should provide for the accretion of the residual asset during the lease term. This is consistent with the view that a lease accounted for under the Derecognition model is viewed as a financing activity. As such, the unguaranteed residual asset is more akin to a financial asset than a tangible property, plant and equipment asset. The unguaranteed residual asset component of a lease should be presented separately from the lease payment component either on the face of the statement of financial position or in the notes to the financial statements.

The Association has no specific comments on component question (d).

**Question 13: Statement of comprehensive income**

*Do you think that lessees and lessors should present lease income and lease expense separately from other income and expense in profit or loss (paragraphs 26, 44, 61, 62, BC146, BC151, BC152, BC157 and BC158)? Why or why not? If not, do you think that a lessee should disclose that information in the notes instead? Why or why not?*

CFLA agrees that lessees and lessors should present the impact of leasing activity separately in the income statement. Separate presentation provides more useful information to users of financial statements.

**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?*

CFLA agrees that cash flows arising from leasing activity should be presented separately from other cash flows on the face of the statement of cash flows.

**Question 15: Disclosure**

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

- a) *identifies and explains the amounts recognised 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 (paragraphs 70–86 and BC168–BC183)? Why or why not? If not, how would you amend the objectives and why?*

CFLA agrees with the quantitative and qualitative information disclosures outlined in the ED. These disclosures will enable users of financial statements to better understand the nature of the entity's leases and the entity's exposures to risks and uncertainties from its leasing activities.

**Question 16: Transition**

- a) *The 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?*
- b) *Do you think full retrospective application of lease accounting requirements should be permitted? Why or why not?*
- c) *Are there any additional transitional issues the boards need to consider? If yes, which ones and why?*

The transitional provisions should provide entities with a choice between full retrospective application or the simplified retrospective approach as outlined in the ED.

The income statement recognition pattern proposed will result in a front end loading of expense for the lessee and income for the lessor compared to current lease accounting due to the combination of effective interest method recognition on the lease obligation / finance receivable respectively and the straight line amortization of the ROU asset for the lessee versus prior straight line rental recognition. To the extent that this recognition pattern is retained, the transitional provisions should be amended to enable entities to avoid the “skew” that would be introduced by forcing all leases to commence the proposed recognition pattern at the same point in time. Typically, a leasing portfolio includes leases at varying stages of their lifecycle therefore the front end loading impact is expected to naturally “smooth” over time. Recasting all leases based on remaining payments at the transition date will skew the results.

**Question 17: Benefits and costs**

*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 the absence of changes to the ED proposals, CFLA cannot agree that the benefits would outweigh the costs. The requirements related to lease term, contingent rentals and renewal options introduce significant estimation risk and measurement uncertainty to the recognition of leases in financial statements, all at significant cost to a preparer in terms of compiling the information and to users in terms of understanding and analyzing the information.

These proposals detract from the value of financial information from a credit adjudication perspective. As users of financial statements, CFLA members would prefer disclosure related to the amount, timing and uncertainty of cash flows rather than amounts recognized in the financial statements based on significant estimates and judgments. This would make financial information more useful for decision-making and would ultimately increase comparability across financial statements.

**Question 18: Other comments**

*Do you have any other comments on the proposals?*

As noted in the Conceptual Framework, “cost is a pervasive constraint on the information that can be provided by general purpose financial reporting. Reporting such information imposes costs and those costs should be justified by the benefits of reporting that information”. There does not appear to be any study on the cost of implementing the proposals in the ED. CFLA believes that cost to be substantial as described further above.

If asked, CFLA would be willing to attempt to quantify the cost for leases with an equipment cost of less than \$100,000. This would cover the bulk of leases by number in Canada.