



CENTER FOR CAPITAL MARKETS

C O M P E T I T I V E N E S S

TOM QUAADMAN
VICE PRESIDENT

1615 H STREET, NW
WASHINGTON, DC 20062-2000
(202) 463-5540
tquaadman@uschamber.com

December 15, 2010

Ms. Leslie Seidman
Acting Chairman
Financial Accounting Standards Board
301 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-05116

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London EC 4M 6XH
United Kingdom

**Re: File Reference: No. 1850-100, Exposure Draft: *Leases*;
Exposure Draft, *Leases*, ED/2010/9**

Dear Acting Chairman Seidman and Sir David:

The U.S. Chamber of Commerce (the “Chamber”) is the world’s largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness (“CCMC”) to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy.

The CCMC is committed to promoting effective and transparent financial reporting that enables capital markets to operate efficiently. Leases are crucial to the domestic and global economy, and so the CCMC welcomes the opportunity to comment on the Financial Accounting Standards Board (“FASB”) and International Accounting Standards Board (“IASB”) Exposure Draft, *Proposed Accounting*

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 2

Standards Update on Leases (“lease accounting proposal”), to revise lease accounting standards.

In 2009, the CCMC commented on the FASB discussion paper- ***Leases: Preliminary Views*** (“discussion paper”).¹ At the time, the CCMC raised serious issues and concerns regarding the proposals to revise lease accounting standards. While the CCMC appreciates the work of the FASB and IASB members and staffs in improving the lease accounting proposals, the three main concerns of the CCMC still remain:

- **The timing is wrong and a compressed period of consideration will not allow for appropriate input and dialogue;**
- **The lease accounting proposal does not consider all of the aspects of lease transactions and is therefore unsound; and**
- **The lease accounting proposal increases, rather than reduces complexity in financial reporting.**

Additionally, the CCMC also believes that the lease accounting proposal:

- **Fails to accurately reflect business models and instead will act as a driver of economic activity; and**
- **Fails to provide a cost-benefit analysis to justify the implementation of the current lease accounting proposal.**

Unless these concerns are addressed in a substantive manner, the CCMC believes that the implementation of the lease accounting proposals will obfuscate financial reporting, distort and depress economic activity, and harm investor interests. Such unintended consequences, as the global economy recovers from the Financial

¹ See July 17, 2009 letter from CCMC Chairman Richard Murray to Russell Golden commenting on the discussion paper. This letter raised serious issues with the lease proposal as presented at that time and those points will be raised during the course of this comment letter.

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 3

Crisis, will hamper economic growth and job creation. Therefore, we respectfully request that the FASB and IASB extend the June, 2011 deadline for final consideration and make the changes necessary to allow accounting standards to be reflective of the underlying economics of lease transactions.

Our specific concerns and principles are discussed in greater detail below.

I. Discussion on Concerns

This letter is the fourth time in past year and a half that the CCMC has written individually or collectively to FASB, IASB, or governmental leaders on lease accounting.² The reason for this level of activity is because of the importance of lease transactions in a 21st century global economy.

Leases are an essential element for many different segments of the global economy. In the United States alone it has been estimated that lease transactions now exceed one trillion dollars. Obviously, transactions of such a nature must be accurately reported so that all stakeholders can understand the scope of activity involved. Therefore, the development and implementation of lease accounting reforms should be conducted carefully to insure accurate financial reporting and avoid dislocations of economic activity. Unintended consequences of this sort will harm investors and businesses, while placing additional stress upon a fragile economic recovery. Even though, the lease accounting proposal represents an improvement over the discussion paper, in our opinion, the appropriate balance has still not been struck to justify moving forward.

Leases are used by businesses, because they allow for the use of equipment or real estate, with payments over time, giving businesses the flexibility needed for a more efficient deployment of capital. Such deployment of capital may be used to fuel

² See CCMC letter of July 17, 2009 commenting on the FASB discussion paper- *Leases: Preliminary Views*; joint trade association letter to the G-20 Leaders on October 22, 2010 requesting the G-20 delay time deadlines on lease accounting proposals; and December 8, 2010 joint trade association letter to FASB and IASB commenting on the current lease proposals.

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 4

business expansion and job creation, thereby benefiting investors over the long-term.³ As such, the lease accounting proposal would impact almost every public company and business model. Substantially changing the accounting for this essential economic activity has widespread implications for property owners, public and private companies, investors, and lenders alike and could have a broad impact on the capital markets. Unfortunately, the lease accounting proposal, as currently drafted, could promote market instability for lessors and lessees, harm the financial services sectors that provide support for these transactions and adversely impact investors who provide the capital to companies that use leases.

a. Timing Concerns

Essentially, the subject is too vast to be soundly completed with the time and resources that the FASB and IASB have been able to devote to it, as a number of other complex convergence projects are moving forward on a similar timeline and pace.

Since accounting changes can impact lending and other investment decisions, the CCMC believes that the rush to complete the lease accounting proposal is not prudent because of the possible far ranging unintended consequences. Those consequences are discussed in more depth in the next section. However, the recent debate regarding the fair value assessment of assets in inactive markets illustrates the adverse impact of unintended consequences upon businesses and financial reporting policy.

For that reason, the Chamber and 25 other trade associations wrote to the G-20 Finance Ministers requesting the removal of the June, 2011 deadline to insure that the lease accounting project be completed in a thoughtful and deliberative manner.⁴ The G-20 leaders at the Seoul Summit acknowledged the need to push back deadlines

³ See the July 21, 2010 edition of the *Wall Street Journal*, *Northrop Is Flying East*. Northrop Grumman purchased, rather than leased a new headquarters building because of concerns to lease accounting changes that could lead to reduced buying capacity. The transaction was estimated at between \$78.4-\$105 million dollars. Such a decision has an opportunity impact and ramifications over the resources available to operate a business.

⁴ Joint trade association letter to the G-20 Leaders on October 22, 2010 requesting the G-20 delay time deadlines on lease accounting proposals.

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 5

for the accounting convergence projects.⁵ While this is a welcome development, the CCMC believes that it is more important to take the time to get the lease accounting provisions done right, rather than rush to completion for the sake of change.

b. Failure to consider all of the aspects of lease transactions

Companies borrow and raise capital to expand, create jobs, and operate. Since the standard will impact the ability of businesses to borrow and raise capital, it is all the more important to ensure that any new lease accounting proposal is designed and implemented appropriately. The issues and unintended consequences that have not been fully explored and vetted include the following:

- The potential breach of loan covenants and contractual arrangements and loss of cost reimbursement for rent in contractual arrangements that are based on current U.S. Generally Accepted Accounting Principles (“USGAAP”) as well as overall changes to credit underwriting requirements;
- Complicated recognition and presentation requirements that mask true economic activity and do not reflect the value of a contract;
- Adverse impact to capital of banks, during the ongoing financial crisis, due to both lessee and lessor accounting changes;
- Adverse impact on the ability of businesses to borrow, the cost of leases, and capital formation;

⁵ The G-20 Seoul Summit communiqué, in paragraph 38, moved the previous stated deadline from June, 2011 to the end of 2011:

We re-emphasized the importance we place on achieving a single set of improved high quality global accounting standards and called on the International Accounting Standards Board and the Financial Accounting Standards Board to complete their convergence project by the end of 2011. We also encouraged the International Accounting Standards Board to further improve the involvement of stakeholders, including outreach to, and membership of, emerging market economies, in the process of setting the global standards, within the framework of independent accounting standard setting process.

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 6

- Adverse impact on equipment and real property valuations, with consequential impact on lenders, especially the already fragile banking sector;
- Front ended lessee cost patterns that do not reflect true economic activity;
- Differing recognition of assets and liabilities creating mismatches that do not reflect the value of a contract for lessors;
- Rules that are not symmetrical between lessor and lessee;
- Inequitable treatment of executory costs for lessors and lessees;
- Requirements to forecast and record future events and contingencies that are unique to leases and not aligned with existing overarching GAAP requirements;
- Requirements for a lessor performance obligation model that would result in the doubling counting of assets, plus the recognition of a lease liability that would never be subject to settlement through future cash or future asset transfers;
- Unknown implementation costs, including the need for costly implementation of new accounting systems, as well as ongoing compliance costs; and
- Changes in behavioral actions that will depress commercial real estate values, as well as a defacto prohibition of accepted business activities including permissible allowable cost reimbursements permitted under contractual obligations and government regulations.

If these issues are not addressed, adverse consequences may be felt by nearly every business that lease equipment or commercial real estate, those that provide equipment or real estate through lease vehicles and those that finance lease

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 8

interim and annual financial reporting period (sometimes monthly), the lease accounting proposal vastly increases accounting complexity.

In developing an effective lease accounting standard, CCMC believes that the following basic principles must be followed:

- 1) New lease accounting standards must reflect economic activity, not drive it;
- 2) New lease accounting standards must permit the financial statements to represent the true effect of lease transactions;
- 3) New lease accounting standards should not raise the cost of capital or unnecessarily create adverse impacts upon financial statements;
- 4) FASB and IASB should insure that the benefits outweigh the costs;
- 5) New lease accounting standards must take into account non-accounting issues, such as contractual obligations, to truly represent lease transactions;
- 6) To insure accuracy, lease accounting standards should be consistent between the lessor and lessee; and
- 7) Standard setters should transparently identify the investor interests and needs they seek to address.

Application of these principles will achieve the goal of a new lease accounting standard that is less complex, accurately reflects economic activity and will avoid the adverse unintended consequences that can flow from a flawed revision.

II. Potential Solutions

The CCMC believes that the principles enumerated above will help to guide the FASB and IASB to the appropriate standards that will benefit all with a stake in accurate financial reporting. We applaud FASB for holding roundtables and soliciting

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 9

additional input. Based upon these principles, the CCMC recommends that the following are addressed to resolve the concerns raised earlier.

- **Business Model-** the business model is the driver of success of a company and the prime driver for the intent of an investor to furnish a company with capital. Providers, users or financiers of leases have made leases an integral part of their business model. Accordingly, for these companies and their investors, it is important that the business model be a key component in the creation of lease accounting standards.
- **Estimates-** FASB and IASB should drop requirements to estimate contingent revenues and lease extensions in the initial measurement of leases. Leases should be measured only referencing the fixed minimum periods. To go beyond that begins to take into account contingencies and other payments or terms that may not come to fruition and obscures the initial obligation of a lease. Appropriate disclosure, where needed will provide investors with information that is of relevance, while not obfuscating the financial obligations and performance of a company.
- **Leveraged Leases-** additional input is needed regarding leveraged leases. 35 years ago, SFAS 13 was issued because leveraged leases are unique vehicles and are critical to the financing of many types of capital assets. Given their importance to certain sectors of the economy, we recommend the Boards engage in targeted field testing and research for this particular type of structure before the final conclusions on the accounting for leveraged leases are determined.
- **Short Term Leases-** the CCMC does not believe that short term leases, those with maximum rental terms (including renewal options) of one year or less, require balance sheet recognition. Lessees should have the same elections for short-term leases as those provided to lessors. As a result, lessees should have the option to simply recognize such leases on a straight-line basis over the term, similar to the manner in which operating leases are recognized today. This better matches cash flows, avoids the significant effort and costs

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 10

associated with accounting for and measuring such short-term assets and liabilities and represents a practical way of handling this class of lease transactions.

These suggestions are not an exhaustive list of possible proposals, but are illustrative of several of the major revisions that should occur in order to allow the lease accounting proposal to move forward.

III. Need for a Cost-Benefit Analysis and Field Testing

CIFiR also recommended a cost-benefit analysis in the development of new standards and such analysis is commonly required in the development of regulations. As included in the principles above, CCMC urges that the FASB and IASB to insure that the benefits outweigh the costs of any lease accounting proposal. While a cost-benefit analysis demonstrating the need for a proposal should be a practice for all accounting projects, the economic consequences for lease accounting demand it.

The FASB and IASB discuss various outreach activities in paragraphs BC200 through BC205 of the lease accounting proposal. However, this discussion does not represent a robust cost-benefit analysis. In addition, the discussion does not seem to appreciate that current disclosures required by the FASB, IASB, and SEC provide users with information on, for example, operating leases and cash flows that is not costly to assess or adjust. Moreover, it does not appear that the FASB and IASB have conducted any field testing to meaningfully assess the costs of implementing the lease accounting proposal and consider such costs in conjunction with the purported benefits being advanced by users.

Further, as we have previously stated,⁶ FASB and IASB cannot and should not consider the costs and benefits of individual proposals in a vacuum. Companies are facing a tidal wave of new accounting and disclosure-related requirements, each of which will carry increased costs. There is a finite limit on the total amount of additional costs attributable to new accounting and disclosure obligations that

⁶ See August 11, 2010 letter from U.S. Chamber of Commerce to the FASB on *Proposed Accounting Standards Update, "Disclosure of Certain Loss Contingencies"* (File Reference No. 1840-100).

Ms. Leslie Seidman
Sir David Tweedie
December 15, 2010
Page 11

businesses can absorb without harming the economic recovery. The FASB and IASB should consider this overall burden on companies, which investors will ultimately bear, in making cost-benefit determinations. Such a cost-benefit analysis should be developed as the lease accounting proposal is developed and implemented.

Accordingly, the CCMC recommends that the FASB and IASB provide a robust cost-benefit analysis of any lease accounting proposal, and such an analysis should include field testing, as well as a post-implementation review.

Conclusion

Again, the CCMC appreciates the work done by the staffs of the FASB and IASB in developing the lease accounting proposal and believes that it represents an improvement over the discussion paper. However, as explained above, we have serious concerns regarding the direction of this project and the substance of the proposal itself. The proposal fails to consider business models and all of the aspects of lease transactions, lacks a cost-benefit analysis and ultimately, will increase complexity in financial reporting and will act as a driver of economic activity.

Furthermore, because of the current schedule and desire to meet an arbitrary deadline, the CCMC is concerned that the accelerated due process effort on the part of the standard-setters will unnecessarily and adversely impact the quality of the lease accounting proposal. We believe that the task of correctly completing the lease accounting project outweighs the need of simply completing it with a standard that may ultimately be flawed.

Thank you for your consideration and the CCMC stands ready to assist in these efforts.

Sincerely,

Tom Quadman