LVMH MOËT HENNESSY, LOUIS VUITTON

Dear Sirs,

We are pleased to comment on the Exposure Draft relating to lease accounting. This proposal concerns the LVMH Group, which operates a worldwide network of over 2,600 stores, in addition to concessions in airports and on cruise ships. Most of those locations are subject to lease and concession agreements falling within the scope of the project, in addition to the offices and warehouses that are also leased. Before going into the details of the questions, we take the opportunity to make general comments on the project.

- As preparers of IFRS compliant financial statements since 2004 which include numerous transactions accounted for according to IAS 17, we have never felt that this text was leading to an unfaithful representation of lease contracts. A difference should actually be made between a « poorly written standard » and a « poorly applied standard». The current distinction between operating and finance leases is far from irrelevant, though it can be misused and lead to abuses. Indeed, if an asset is specifically designed according to the lessee's needs, or if the lessee will benefit from the asset during most of its useful life, or if he will de facto pay the price of the asset, it is relevant to consider that the lessee has in substance purchased the asset, an analysis which is still valid in the proposal. But does the prevention of abuses constitute a sufficient basis for recognizing systematically a maximum liability, contingent upon future events, whose future changes will poorly depict the economic reality and complexity of the lease agreements in the financial statements? Would it not be preferable to improve the principles on which the current text relies and target a more faithful implementation of this standard?
- Regarding the Exposure Draft itself, we do not understand the rationale for presenting differently lease contracts and other contracts. An entity enters into many contracts, which generate future economic advantages upon realization of certain conditions. The fact that the entity is liable for paying the price is the counterpart to those future economic advantages.

This is generally the case of supply contracts. In such contracts, the supply may be contingent; it may depend on meteorological conditions for instance; but a reciprocal commitment of both parties to deliver economic resources does exist. Service agreements follow similar principles: they grant to the beneficiary a future right, and in exchange for this right the beneficiary has to settle his debt towards the service provider through the payment of the price. Such contracts are not capitalized in the balance sheet at contract inception, as assets and liabilities. Why would a specific treatment for lease contracts improve balance sheet presentation?

The same principle could be applied to employment contracts. Disposing from a qualified workforce undeniably represents an asset for the entity, but it is not capitalized in the balance sheet on the basis of discounted future salaries. Actually, no debt is booked for future employment period of employees, as the existence of such a debt depends on the occurrence of a contingent future situation, the presence of the employee and the effective accomplishment of work. Debts, or provisions towards employees are recorded in the balance sheet to account for future rights (for example: retirement benefits), but only up to the amount acquired to date. In our opinion, the lessee's debt towards the lessor has similar characteristics; it is closely related to the actual future utilization of the leased asset, the sole part which could be considered to give rise to a liability being its minimum and incompressible portion.

- Assuming that, from an accounting perspective, lease contracts should be differentiated from other contracts, it is important to note that a lease contract obliges two parties, the lessee and the lessor. Obviously, accounting standards targeting a worldwide implementation cannot take into account specificities deriving from local regulations. Still, the lessee's rights are undeniably limited by those of the lessor, this being particularly true with regards to the length of utilization of the leased asset. A liability whose valuation basis relies in the first place on the lessee's intent of utilization, lessor's rights to stop the contract being considered only in the second place should not be eligible for recognition. It may be justified from an accounting standpoint to recognize the lessee's debt towards the lessor, in cases where an incompressible length is specified in the lease contract (for its total duration or a shorter period), but how could such a liability be justified for the horizon beyond this minimum period?
- A liability should not be recognized if the underlying commitment is not certain, or at least probable; a liability cannot be based on a contingent commitment. Lessor's rights, as outlined above, make the probable length of utilisation of the leased asset uncertain. Furthermore, the lease liability has to be valued by inflating the minimum liability with elements whose future occurrence is not certain; contingent rents belong to those elements. Generally speaking, the existence of the debt is highly dependent on the occurrence of future events: the reality of the lease relationship in future periods.
- Differences between the initial valuation of the debt and its final amount will undoubtedly arise, especially due to errors in assessment of the most probable length of utilization; our understanding is that the correction of those errors will be reflected in the income statement, notably for the effect of leases whose duration ends up being shorter than the length retained initially, due to an anticipated interruption of the contract. How should such an income statement impact be justified economically?
- Finally, regarding the impact of the proposals on balance sheet and income statement presentation, the accounting treatment will be similar for leased assets and purchased assets, which will deprive investors from a meaningful information regarding the way the business is financed (in a capitalistic way or not). By making all leases look identical and hiding the complexity of lease arrangements, will the project truly meet its objective of enhancing comparability? This might end up producing comparability where there should be differentiation, and deprive users from an information whose predictive value would be diminished. LVMH is a very illustrative Group in this area, with a financial net debt as at December 31, 2009 amounting to Euros 2.9 million and a minimum lease commitment at the same date amounting to Euros 3.8 millions, probably less than the amount that would result from the Exposure Draft. We strongly believe that the addition of the two would not increase transparency and legibility on Group financing.

We remain available to answer any questions you may have.

Yours sincerely,

Jean-Jacques Guiony

CFO

Olivier Pérouse

Accounting Director

Note: We have not responded to questions addressed specifically to lessors, as we have no significant involvements as lessors.

THE ACCOUNTING MODEL

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?

Securing the future use of an asset represents an economic value that could be recognized as an accounting asset, provided that the nature of this asset is carefully analyzed. A lease contract conveys components that go further the securitization of the use of the asset over a certain period of time. In our experience of such contracts, a significant part of those components is not earned yet at contract inception and will be earned over contract's life, as both parties fulfil their respective obligations (including payment of rents by the lessee, and maintenance of asset in optimal conditions by the lessor). Such a relationship, though based on a multi-year agreement defining the use of the underlying property, cannot be encompassed only in terms of rights and obligations, but is closer to a business relationship, in which both parties have an interest in developing the profitability of the underlying asset. This is notably the case of concessions in department stores, or in airports.

Business relationships are managed in accordance with economic environment, under contractual constraints. While contractual constraints are well-known at contract inception, future economic environment can only be anticipated. Various circumstances will likely arise over the course of the lease, resulting in a real lease history (in terms of duration / amount of rents) different from the one that had been initially anticipated. We question whether or not financial statements are the place where anticipations of the future should be reflected. We believe that only existing elements existing should be reflected in the financial statements. Others may be explained.

Recording elements pertaining to the occurrence of future events in the balance sheet might create undesirable and meaningless balance sheet volatility.

(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?

We agree that, having segregated the right-of-use from other components of the lease contract, the right-of-use asset should be amortized and that an interest on the liability should be recognized.

Question 3: Short-term leases

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

We see no objection with the treatment proposed by the Board for short-term leases.

DEFINITION OF A LEASE

Question 4

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

We agree with the definition of a lease but we would have expected the Board to define the "right-of-use" as well, which is the cornerstone of the new standard, so that it can be linked with practice and market reality.

As an example, how would the Board differentiate the "right-of-use" from key moneys (customary for real estate leases) or any other sort of entrance fees paid to obtain lease contracts? Those in our perspective are closer to the concept of "right-of-use" than the one proposed by the Board to the extent that, if the lease was transferred to another party, the amount obtained from the transferee would be closer to the entrance fees paid initially (and already recognized as an intangible asset in the balance sheet) than to the discounted value of future lease payments which the Board proposes to use to determine value of the right-of-use.

(b) 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?

We agree with those criteria.

SCOPE

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?

We agree with the scope exclusions.

Question 6: Contracts that contain service components and lease components

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?

We are very reserved about the "by default" approach proposing to apply lease accounting even to contracts including service components. We take the opportunity to raise serious doubts regarding the resulting asset on the balance sheet, which in part would include capitalization of the value of future services. We believe that this anomaly points out to the fact that the right-of-use is poorly defined and all resulting proposals may be biased.

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?

We have difficulties understanding the rationale of the Board: why should the right-of-use be accounted for while the right-to-purchase should not? On one side it is argued that rights the entity has over assets should be recognized, while on the other side purchase options - which represent true economic rights earned at contract inception - should not be accounted for. Are lease payments the appropriate measurement basis for the right-of-use, since retaining this measurement basis results in not recognizing purchase options?

MEASUREMENT

As a preliminary, we wish to raise concerns about the Board's assertion – not supported in the basis for conclusions – that the cost of the right-of-use asset corresponds to the discounted value of future lease payments, considered itself a reasonable approximation of fair value. We believe this assertion is not reflective of the complexity of a lease contract, as lease payments in our view remunerate the lessor for many more elements than just the fact of entitling the lessee to use the asset in the future.

As an illustration, in the area of real estate, when an active market for the transfer of leases exists, the amounts paid (key moneys) do not correspond to discounted future lease payments. However, such markets do not exist in all cases, and a valuation principle applicable to all leases must be retained. In defining this principle, it is necessary to distinguish the portion of lease payments remunerating the right-of-use from the portion remunerating the actual use of the asset, which involves a certain level of assumptions.

For that purpose, we believe economics of the transaction would be more faithfully translated in the financial statements if the cost of the right-of-use was commensurate with the level of commitment entered into by lessee and lessor. Hence, limited possibilities to exit prior to the end of the contract (or at dissuasive costs), elevated fixed payments, renewal options..., could be indicative of a higher value placed by both lessee and lessor on the right-of-use since they committed to such conditions.

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?

We strongly disagree with this. We believe that the purpose of financial statements is to provide a fair representation of assets and liabilities as they exist as of closing date, not of future assets and liabilities. Assumptions regarding future events are made for accounting purposes only to the extent that they are necessary to support the value of existing assets / liabilities, but in no case to assess the value of future assets or liabilities. Assessing the value of future assets belongs to planning processes, not to accounting.

As a result, we raise serious doubts regarding the possibility, on this valuation basis, to meet the criteria necessary for good quality financial statements:

- relevance / predictive value of financial statements: the value of assets / liabilities which do not exist yet (and which may never exist) is likely to fluctuate significantly, creating undesirable and meaningless volatility in the financial statements;
- faithful representation: in our Group, assumptions made in planning processes cover a one-year period
 in a great level of detail (similar to that required for accounting), and an additional 4-year period in a level
 of detail which we consider would not be sufficient for accounting purposes, thus values are likely to be
 less accurate than what is required for accounting data, all the more since they will be built solely for
 accounting purposes;
- verifiability: valuation will heavily rely on assumptions made internally, not on external data, which will be difficult to validate;
- comparability: according to the model proposed, the valuation will reflect in the first place the entities' anticipations about the leases, and, in the second place, the extent to which those anticipations are mitigated by contractual constraints. Thus, for entities subject to similar contractual constraints due to specific lease regulations, amounts recorded would differ mostly because of different anticipations about leases. In order to achieve comparability, contractual constraints should be considered in the first place, and entity-specific anticipations extrapolating on those constraints should not be taken into account.

Regarding the absence of reassessment of the discount rate subsequently to initial recognition:

- if the probable lease term integrates one or several renewal periods, the discount rate would be disconnected from the actual level of interest rates at renewal date, though the amount of the new rent would likely integrate the current level of interest rates;
- the right-of-use will be subject to impairment testing according to IAS 36. Discount rates used to perform impairment tests are updated at each closing according to current conditions. If the discount rate used for impairment testing exceeds the initial discount rate, it will generate an impairment, which in fact results from the fact that the discount rate used to assess the right-of-use is not updated.

Those inconsistencies should be addressed by the Board.

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?

We strongly disagree with this proposal because, again, including contingent payments in the valuation would not be representative of assets and liabilities as they exist as of closing date.

Contingent rents are not due until the basis for determination of the rents is achieved. By agreeing on contingent rents, the lessee and the lessor enter into a business relationship. In such cases, the lessor takes risks on his remuneration. Such agreements are common for retail space operated in commercial galleries or "shops-in-the-shops" (in department stores), as well as for airport concessions.

Anticipating contingent rents in the valuation of the right-of-use asset would be in contradiction with the substance of this particular relationship, which is a sort of partnership, involving among others the undertaking of regular actions aimed at promoting & developing the commercial area as a whole, for the benefits ot both lessor and lessees. The variability of rents is an indication that, on lessors' side, rents are a type of turnover, while on lessee side, they represent period costs rather than amortization of assets earned from the beginning.

We are also reserved about the practical feasibility and reliability of the estimates, on which amounts charged to the P&L are based. In addition to the fact that such projections are made in much less detail than what is required for accounting, variables to be assessed may even be beyond control of the lessee (number of passengers for airports), and formulas may combine several variables. Recording a straight-line amortization expense on the basis of such estimates would significantly distort annual profitability. This would also erase the difference between an entity that benefits from flexibility thanks to variable rents and another one that pays fixed rents. It would make comparable what should not be.

Lastly, we note that the accounting treatment for differences between estimated and actual contingent rents needs clarification: the Board states that any difference relating to **past** and current period should be charged to profit & loss. Does it mean that, though rents are due and have been cashed out at the end of each accounting period, the Board implicitly acknowledges that –in case amount paid is higher than estimated- a portion of those amounts may be deferred, resulting in an asset which would likely not meet asset recognition criteria set by the Conceptual Framework?

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?

This question is not relevant. Asking this question indicates that the valuation basis of the right-of-use is inappropriate, and entails a level of uncertainty which is inacceptable for accounting purposes, since it is necessary, not only to exercise judgement at first recognition, but also in the follow-up on such assets / liabilities.

PRESENTATION

Question 12: Statement of financial position

(a) 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?

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, 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?

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?

We disagree that liabilities and assets should systematically be distinguished from other assets and liabilities, because this is in contradiction with the concept of materiality put forward in IFRS. Multiplying the number of lines appearing on the face of the balance sheet might be counter-productive and dilute important information among less important information. We believe that entities should be entrusted here in determining whether or not it is relevant to present a separate line. Information could be requested in the notes.

Regarding the statement of comprehensive income, requesting such a presentation would contradict the possibility to present income statement either by function or by nature, clearly showing a trend towards a presentation by nature, even if it is not considered relevant by management. We believe that, if the income statement is presented by function, the information should be disclosed in the notes.

Regarding the statement of cash flows, again, we believe entities should exercise their judgement in determining the relevance of a separate line.

DISCLOSURE

Question 15

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?

We agree with this proposal.

TRANSITION

Question 16

(a) The exposure draft proposes that lessees and lessors should recognise 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?

We agree with this proposal.

(b) Do you think full retrospective application of lease accounting requirements should be permitted? Why or why not?

We do not think that full retrospective application should be permitted as it would be not be reliable.

BENEFITS AND COSTS

Question 17

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?

We disagree with the Board's assessment of the costs and benefits. As explained, we are very reserved about the benefits of this new treatment, and consider that they are largely outweighed by the costs of implementation and monitoring. Those involve an adaptation of information systems at the smallest level of the organization, as this treatment will impact day-to-day accounting entries in every subsidiary. Introducing so much complexity in areas which are inherently difficult to monitor closely due to the number and diversity of transactions is a potential source of errors that should not be neglected in the assessment of costs and benefits.