



December 15, 2010
Financial Accounting Standards Board
401 Merritt 7
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Dear Board Members and Staff:

We appreciate the invitation to comment on the Proposed Accounting Standards Update regarding *File Reference No. 1850-100: Leases (Topic 840)*. Wawa is a privately owned retail convenience store chain operating over 570 stores in the mid-Atlantic region with total sales of over \$5 billion. Leases are an important financing tool for us as a significant number of our stores, or the land underlying our stores, are leased. We would like to offer the following comments to the questions included in the Proposed Accounting Standards Update:

Question 1: Lessees

(a) Do you agree that a lessee should recognize 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?

Answer 1a: We agree with the FASB's concept embodied in this proposed standard of the recognition of the rights and obligations conveyed by leases. We believe that the proposed accounting model improves the reporting of lease agreements to more closely resemble their economic substance, and puts financial statement recognition of entities that lease assets in a more comparable situation with those that choose to purchase their assets. The proposed treatment will sweep away years of rigid form over substance accounting for leases and reduce the impact of differing lease accounting treatments driving business decisions. We understand that this proposed standard will have a significant impact on many company's debt covenants and will require adjustment of the covenants to negate the impact of the accounting change on each company's true performance.

(b) Do you agree that a lessee should recognize amortization 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?

Answer 1b: We agree that the right-of-use asset should be amortized and that the liability should be expensed utilizing the effective interest method. These expense recognition methods closely mirror the expense recognition that would typically be used if the assets were purchased and financed, placing entities on more comparable reporting basis regardless of their choice of financing their productive assets. Although the proposed model will result in differing expense recognition for leased versus purchased land (the former amortized, the latter a non-depreciated asset), this difference in accounting is not easily remedied since there is no asset to sell at the end of the lease for the lessee.

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?

(c) Do you agree that there should be no separate approach for lessors with leveraged leases, as is currently provided for under US GAAP (paragraph BC15)? If not, why not? What approach should be applied to those leases and why?

Answer 2: Arrangements in which we are a lessor are a very insignificant portion of our business. Therefore, we will focus our responses to the questions concerning lessee accounting and generally not address the lessor questions in this document.

Question 3: Short-term leases

This exposure draft proposes that a lessee or a lessor may apply the following simplified requirements to short-term leases, defined in Appendix A as leases for which the maximum possible lease term, including options to renew or extend, is 12 months or less:

(a) At the date of inception of a lease, a lessee that has a short-term lease may elect on a lease-by-lease basis to measure, both at initial measurement and subsequently, (i) the liability to make lease payments at the undiscounted amount of the lease payments and (ii) the right-of-use asset at the undiscounted amount of lease payments plus initial direct costs. Such lessees would recognize lease payments in the income statement over the lease term (paragraph 64).

(b) At the date of inception of a lease, a lessor that has a short-term lease may elect on a lease-by-lease basis not to recognize assets and liabilities arising from a short-term lease in the statement of financial position, nor derecognize any portion of the underlying asset. Such lessors would continue to recognize the underlying asset in accordance with other Topics and would recognize lease payments in the income statement over the lease term (paragraph 65).

(See also paragraphs BC41–BC46.)

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?

Answer 3: We believe that the proposed treatment for short-term leases is generally reasonable. However, we believe that the proposed standard should include a provision that the guidance need not be applied to immaterial items. Most companies have immaterial leases for items such as fax machines and copiers. Companies should not be required to expend scarce resources on detailed lease analysis for minor leases that are not significant individually or in the aggregate if the results will be clearly immaterial to the company's results and therefore not impact the perception of the readers of financial statements.

We also believe that the Board should specifically address how month-to-month leases should be accounted for under the proposed model. Since such leases generally may be cancelled by either party upon very short notice, they differ significantly from leases with fixed terms and specified optional extensions that are frequently exercisable at the sole discretion of the lessee.

Definition of a lease

This exposure draft proposes to define a lease 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 (Appendix A, paragraphs B1–B4 and BC29–BC32). This exposure draft also proposes guidance on distinguishing between a lease and a contract that represents a purchase or sale (paragraphs 8, B9, B10 and BC59–BC62) and on distinguishing a lease from a service contract (paragraphs B1–B4 and BC29–BC32).

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?

Answer 4a: We believe that the proposed definition of a lease is appropriate.

(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?

Answer 4b: We believe that the proposed criterion for distinguishing a lease from a contract that represents a purchase or sale is appropriate. We believe that transfer of ownership or bargain purchase options are appropriate criteria and are consistent with the substance of such transactions.

(c) 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?

Answer 4c: We believe that the proposed criterion for distinguishing a lease from a service contract is appropriate as they require the identification of specific assets in the agreement and control of the assets by the lease. Both of these criteria are essential for sufficient substantive specific identification and control of assets to record them as assets and liabilities on the lessee's financial statements.

Scope

Question 5: Scope exclusions

This exposure draft proposes that a lessee or a lessor should apply the proposed guidance to all leases, including leases of right-of-use assets in a sublease, except leases of intangible assets, leases of biological assets and leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources (paragraphs 5 and BC33–BC46).

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

Answer 5: We believe that the scope of the proposed exclusions are appropriate as they are sufficiently broad to encompass most assets that entities are likely to lease and exclude specific situations where other guidance is more relevant.

Question 6: Contracts that contain service components and lease components

This exposure draft proposes that lessees and lessors should apply the guidance in proposed Accounting Standards Update, Revenue Recognition (Topic 605): Revenue from Contracts with Customers, to a distinct service component of a contract that contains service components and lease components (paragraphs 6, B5–B8 and BC47–BC54). 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 guidance in the exposure draft on 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?

Answer 6a: We believe that the proposed treatment of contracts with both lease and service components is generally appropriate. However, for arrangements where the lease portion cannot be reasonably segregated from the combined contract, there should be an evaluation of the significance of the lease portion of the contract to the service portion. In those instances where the lease portion of the contract is not estimated to be a significant portion of the overall agreement, then the combined contract should not be required to follow the proposed lease accounting treatment.

Question 7: Purchase options

This exposure draft proposes that a lease contract should be considered terminated when an option to purchase the underlying asset is exercised. Thus, a contract would be accounted for as a purchase (by the lessee) and a sale (by the lessor) when the purchase option is exercised (paragraphs 8, BC63 and BC64). 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?

Answer 7: We agree with the proposed treatment that purchase options should be accounted for when the purchase option is exercised. Since the exercise of a purchase option changes the nature of the lessee's legal position with respect to the leased asset from that of user to owner, the accounting by the lessee should change accordingly and concurrently with the lessee's legal relationship with respect to the leased asset.

Measurement

This exposure draft proposes that a lessee or a lessor should measure assets and liabilities arising from a lease on a basis that:

- (a) assumes 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 (paragraphs 13, 34, 51, B16–B20 and BC114–BC120).
- (b) includes in the lease payments contingent rentals and expected payments under term option penalties and residual value guarantees specified by the lease by using an expected outcome technique (paragraphs 14, 35, 36, 52, 53, B21 and BC121–BC131). Lessors should only include those contingent rentals and expected payments under term option penalties and residual value guarantees that can be reliably measured.
- (c) is updated 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 (paragraphs 17, 39, 56 and BC132–BC135).

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?

Answer 8: We believe that the lease term should include the sum of the following periods:

- **The contractually fixed lease term**
- **Any exercised option term**
- **Any option term for which exercise is judged to be probable at lease inception.**

We believe that it is inappropriate to include additional option periods, even if it is estimated that it is more likely than not that they would be exercised based on subjective entity specific criteria, as we do not believe that the “more likely than not” threshold is a sufficiently high threshold to determine, at lease inception, that a liability exists as required by the existing definition of a liability (see our response to Question 9 below for further details on this rationale). We also believe that the proposed calculation for lease term is an overly cumbersome process for estimating how long a business will most likely lease an asset.

The determination of lease term as provided by the proposed standard would be an effective method for estimating a reasonable term of a lease for disclosure purposes as this information is useful for financial statement readers. However, we believe that the option periods to be included in the evaluation of a lease term disclosure should only include those periods where the option to extend is exclusively at the discretion of the lessee. When an option to extend includes provisions requiring mutual agreement or are otherwise outside of the exclusive control of the lessee, they cannot be considered more likely than not since the lessee has little or no control over the lessor’s decision process.

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 reliably measured? Why or why not?

Answer 9: Only a fraction of our leases include contingent rent provisions, so the proposed guidance on contingent rentals is not expected to have a significant impact on our effort to adopt this proposed standard. However, we disagree with the proposed treatment of contingent rentals. We believe the proposed approach violates the fundamental definition of a liability as stated in Concepts 6 (as currently codified in the Accounting Standards Codification in 450-10-05 (Q&A 01)). Paragraph 36 of FASB Concepts Statement No. 6, *Elements of Financial Statements*, describes a liability as follows:

A liability has three essential characteristics: (a) it embodies a present duty or responsibility to one or more other entities that entails settlement by probable future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand, (b) the duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice, and (c) the transaction or other event obligating the entity has already happened.

Contingent rent is the result of both a past event (signing the lease with contingent rental provisions), and future events (the basis for the contingent rent, such as reaching a certain level of sales). We believe that the proposed treatment of contingent rent violates characteristic (c) of the above mentioned guidance as the treatment would have financial statement preparers record liabilities for future events that may not occur. We believe that contingent rentals should only be

included to the extent that amount and timing of the contingent rentals are probable and reasonably estimable.

As the Board is likely striving to include increased information about future cash flows useful for financial statement readers' evaluation, we agree that estimated future contingent rentals may be a significant cash flow for some businesses (and the use of contingent rental provisions may in fact increase in prominence if not appropriately addressed within this ED). We therefore believe that footnote disclosure of the estimated contingent rental payments determined in accordance with the proposed standard in a manner similar with current tabular disclosure requirements for future operating lease payments would be the appropriate method for providing this information to financial statement users without inappropriately impacting the amount of assets and liabilities recorded.

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?

Answer 10: We believe that the proposed guidance on reassessments is reasonable and provides a balance of preparation effort versus reader benefit. However, it may be more useful for the standard to include guidance for triggers that would require financial statement preparers to reassess leases. We are glad to see that annual reassessments are not required. To require an annual reassessment of all leases would be unreasonably burdensome on financial statement preparers while providing little or no additional useful information to financial statement users. However, failing to reassess leases when substantive changes occur would render the recorded financial information concerning those leases less representative of the underlying lease contracts and therefore detract from, rather than enhance, the usefulness of the information to the readers of the financial statements.

Sale and leaseback

This exposure draft proposes that a transaction should be treated as a sale and leaseback transaction only if the transfer meets the conditions for a sale of the underlying asset and proposes to use the same criteria for a sale as those used to distinguish between purchases or sales and leases. If the contract represents a sale of the underlying asset, the leaseback also would meet the definition of a lease, rather than a repurchase of the underlying asset by the lessee (paragraphs 66–67, B31 and BC160–BC167).

Question 11

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?

Answer 11: We believe that the proposed guidance on sale and leaseback transactions is appropriate as it results in accounting for sale and leaseback transactions essentially in accordance with the substance of the transactions.

Presentation

This exposure draft proposes that lessees and lessors should present the assets, liabilities, income (or revenue), expenses and cash flows arising from leases separately from other assets, liabilities, income, expenses and cash flows (paragraphs 25–27, 42–45, 60–63 and BC142–BC159).

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, 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?

Answer 12(a): We believe that the presentation of lease assets and liabilities should be based on the materiality of the leases to the lessee's balance sheet. If leases are material to a lessee's balance sheet, then the right-of-use assets should be disclosed as the proposed guidance states. However, we believe the liability should be recorded as debt and not reported as a separate line in the balance sheet as it is simply another form of long or short term financing. If leases that are immaterial to a lessee's balance sheet, they should be permitted to be combined with other captions in the lessee's balance sheet with footnote disclosure of the recorded lease assets and liabilities.

(b) 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, totalling 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?

(c) 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?

(d) 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?

As noted earlier, we are generally refraining from addressing questions concerning lessors

Question 13: Income statement

Do you think that lessees and lessors should present lease income and lease expense separately from other income and expense in the income statement (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?

Answer 13: We believe that the lease expense (and sublease income) should not be broken out separately in the income statement. Since one of the goals of the FASB is to make financial statements more comparable across companies, requiring companies that lease assets to report financial information differently from companies that purchase assets and finance them is inconsistent with this goal.

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?

Answer 14: We believe that the cash flow treatment should follow that of the balance sheet and be based on the materiality of leases in accordance with our response to Question 12(a) above. Additionally, we believe that only the principal portion of the cash payments made by lessees should be classified as financing cash flows, and the interest portion of such payments classified as operating cash flows. This treatment would be consistent with the treatment of principal and interest payment for other financing activities. Since one of the stated goals of this guidance is to provide more useful and consistent information to financial statement users, changing the nature of one particular type of financing activity in the statement of cash flows would be inconsistent with this goal.

From a lessor's perspective, we want to ensure that the FASB clearly specify where the cash inflows and outflows are to be reported in the statement of cash flows.

Disclosure

Question 15

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

- (a) identifies and explains the amounts recognized 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?

Answer 15: We believe that the quantitative and qualitative disclosures listed should be required only when leases, and such disclosure information, are material to the lessees' or lessors' financial statements.

Transition

Question 16

(a) This 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?

Answer 16: We believe that the transition guidance is a fair balance of accuracy and effort. We also believe that both early adoption and a full retrospective approach should be permitted.

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?

Answer 17: We believe that the board's assessment of the costs and benefits of the proposed requirements is generally a fair assessment. As a retailer with significant leases, we agree with the concerns raised by financial statement preparers and also understand the usefulness of the information to financial statement users. We caution that sufficient time for adoption needs to be included to allow all entities, especially those with significant leases across multiple systems and

countries, to develop and implement sufficient lease reporting systems to support the reporting requirement of the proposed guidance.

Other comments

Question 18

Do you have any other comments on the proposals?

Answer 18: We believe that the proposed standard must specifically address the treatment of lease-related costs such as common area maintenance and real estate taxes.

Non-public entities

Question 19

Should any of the proposed guidance be different for non-public entities (private companies and not-for-profit organizations)? If so, which requirement(s) and why?

Answer 19: As a non-public entity, we believe that the guidance should apply to both public and non-public entities.

Thank you again for the opportunity to offer our comments on this exposure draft. We would be pleased to discuss our comments or answer any questions you may have.

Sincerely,

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