



financial executives
international

COMMITTEE ON PRIVATE COMPANY STANDARDS

December 15, 2010

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P. O. Box 5116
Norwalk, CT 06856-5116
Sent by email to director@fasb.org

File Reference No. 1850-100

Dear Technical Director:

The Committee on Private Company Standards (CPC-S) of Financial Executives International (FEI) wishes to express its views on the Financial Accounting Standards Board's (FASB's) Exposure Draft of a Proposed Accounting Standards Update, Leases, (Topic 840) (the proposed Update).

FEI is the leading advocate for the views of corporate financial management in the United States. It is a professional association of more than 15,000 CFOs, treasurers, controllers and other senior financial managers. CPC-S is a technical committee of FEI which formulates private company positions for FEI in line with the views of the membership. This letter represents the views of CPC-S and not necessarily the views of FEI.

General Comments

First, we believe that changes to the lease model are needed and the proposed update is a significant improvement in the presentation of relevant financial information to users. As users of financial statements in the consideration of the creditworthiness of our customers, a more complete picture of the liabilities that have been incurred and will claim future cash resources is a significant improvement. There will be costs incurred in implementing the new standards and maintaining the processes in the future that may not be insignificant. However, in general, the benefits of the information and the ability of companies to rationalize the processes and make them routine will make the investment worthwhile.

We believe the information will be relevant to users of private company financial statements. We also believe that the changes to lease accounting will be viewed differently by public and private company statement users. Even though there are key user differences that need to be considered, we believe that the proposed Update is an improvement to existing GAAP and will provide relevant information to both groups.

That being said, we believe there are certain aspects of the proposed update that could be improved. We have concerns that certain requirements add additional costs that will be complex and significant and will not result in additional useful information to the user. Some requirements may even reduce useful information and reduce the update's ability to provide a clear picture of assets and claims on those assets.

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We will discuss those items in more detail below, but specifically the requirement to separate non-optional services from base lease payments is an area where we think improvements could be made while reducing costs overall.

Also, as usual, we are keenly focused on the needs of private company users and appreciate the ability to comment on needs from the private company perspective. Thank you for making that a priority in the process.

Presented below are responses to the questions asked in the proposed 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?**
- (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?**

Yes, we agree with the right of use model. We believe there is a liability created by all leasing arrangements and it should be stated on the financial statements. We believe the offset to this liability should be an asset which can be fairly described as a right of use asset representing the value of the entity's ability to use the property, whether that is inventory, PP&E or an intangible.

We believe that some private companies will have to rely on their accountants to help make the calculations required under the proposed standard as their books and records may be transaction based. However, while the need for discounting calculations will increase, the existing capital lease standards require these calculations and the change will not be completely new.

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?**

We agree with the performance obligation approach and the derecognition approach as they are presented in the proposed update. We also agree that no separate approach for leveraged leases is needed. The simplification of leasing rules will improve the understandability to users and is accomplished by eliminating special purpose rules.

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?

We appreciate the consideration of a simplified approach for short term leases and the conceptual premise of the proposed standard. The previous rules based standards were abused to an extent that violated their original intent. While we believe the consideration given is an improvement that will provide relief on small leases, we believe additional simplification could be accomplished without harming the overall improvements made by the proposed standard. We would like to suggest that short term leases be exempted from the capitalization and liability process entirely and be expensed directly. This exclusion would only apply to leases with a term of less than a year. We recognize that exclusions can lead to abuse but believe that excluding leases that are truly short term in nature was not the abuse of the past. The abuse in the past was partly due to using a short lease term not counting renewal periods that were more likely than not to be exercised in the total lease term for purposes of capital vs. operating determination. We agree that abuse should be prevented by closing loopholes and exclusions whenever possible; however, exclusions that do not detract from providing material relevant information can still be accomplished. We believe the exclusion of short term leases will significantly reduce the ongoing costs for smaller private companies without sacrificing the relevant information in the financial statements. Some smaller private companies rely on short term leases to a greater extent than do large companies with greater access to capital.

If an exclusion is not granted, we believe the proposed expedient is helpful in reducing the burden of complying with the standard. We also agree that lessors should be granted the same practical expedient as lessees when accounting for short term leases.

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).

We agree with the definition of a lease versus a sale. We would like some clarification on leases that were previously capital leases that will no longer be leases due to a title transfer at the end of the lease. Under existing rules, the capital lease standards provided guidance on how to calculate the liability and asset. If these assets are excluded from the scope of the proposed lease standard, we are not sure where in the ASC guidance will exist for the same calculations as existed in the past.

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?

(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?

(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?

We agree that leases are well defined but we have concerns that the substitution exclusion can and will lead to excessive abuse if not clarified in some way. In B2 and B3, the substitution principle allows for the exemption of significant leases of property. While we understand that there are situations where substitution may indicate that the right of use asset is not an asset but the purchase of a service, there are significant leases that allow for substitution and should be more appropriately accounted for as leases.

Under existing standards, copiers may be capital leases if they fail the life and percent of value test. However, many copier leases include a substitution clause that allows the lessor the ability to substitute a different machine under certain circumstances. We are concerned that some of these leases previously treated as capital leases will be excluded from the scope of the new standard which would detract from the Board's goal of providing information relevant to future cash flows (we assume that is one of the purposes of this standard and we agree it is a worthy objective).

If the substitution issue is not addressed, we expect lessors to exploit this principle to manipulate accounting treatment with lease terms as happened under existing rules.

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?

We agree with the proposed guidance, but only as a practical way to get lease improvements accomplished. We do not see theoretical differences in some intangible leases and leases of tangible property.

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?

We understand the conceptual separation between leases and services. However, when taken too literally, the separation of any service from a predominately leasing contract will create additional work that will outweigh the benefits provided by the separation. If a property lease includes water, is it really important to separate the water component of the lease? Does that separation more accurately reflect the future claim on cash flows? Could a tenant purchase water from another source and should that matter?

We believe that a small expedient would lead to less work and would not detract from the overall benefit of the proposed standard. We believe that the change may even improve the standard in some ways. The expedient we propose is that all mandatory 'services' be included in the liability and right of use asset calculations. If a service is optional, we believe the service should be excluded from the liability calculation. For instance, if a copier requires a lessee to pay for monthly maintenance (the copier cannot be substituted), that maintenance would be included in the lease liability calculation. If an asset were leased and the maintenance were optional, the optional maintenance service would be expensed as incurred.

This expedient will be important in many asset and real estate leases. Many real estate leases include common area maintenance. This maintenance is not optional, but is often (but not always) separately stated in the lease. The common area maintenance is not a separate contract, but part of the same contract with all other terms for collection and eviction attached to the payment of the maintenance. In some leases, maintenance is not stated separately but could be estimated. The work required to make the estimates and separate that amount from the base rent payment will add to the burden and complexity of the proposed standard. It will add to the implementation costs and to the ongoing burden of compliance. While it may add some level of technical purity, we do not believe the added costs will add benefits commensurate with the added costs.

We believe that many smaller private companies rely on leases with these service components and simplifying the accounting treatment will benefit them and help keep the costs of implementation and ongoing operations lower while preserving the relevant information provided by the proposed standard.

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?

We believe that purchase options should be included in the asset and liability calculation if it is more likely than not that the option will be exercised. While we agree with the premise that a lease would stop and a purchase would occur with the exercise of a purchase option, we believe the most relevant measure to users is presentation of the substance and ultimate resolution of the contract. If the contract is intended

to result in the ownership transfer and management believes that it will exercise the option to own the asset, the entire contract should be treated as a purchase at inception.

We had significant discussions about whether a purchase option should be included in the calculation. If the option is not a requirement, why should it be included at all? It is more of a possible liability rather than a legal liability. We believe that users or private companies are more keenly focused on more certain liabilities and probability weighted liabilities are not as relevant to those users. The inclusion of purchase options that are MLTN was a way to recognize that there are times when a purchase option is almost certain. In those cases, we believe it is more appropriate to include the purchase option in the liability and asset calculation because it is relevant. Our compromise in thought was that the MLTN threshold helped to filter relevant items from less relevant items which were either 'not likely to occur' or true probability weighted scenarios.

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?

Yes, we agree that the lessee or lessor should determine the lease term as the longest possible term that is more likely than not to occur and that they should take into account any options to extend or terminate the lease. We also believe that the lessee or lessor should consider the purchase options when calculating the lease term. If a lease has a 5-year term and a purchase option is available beginning in year 2, we believe that the term of 2 years should be considered if it is more likely than not that the purchase option would be exercised. This relates to our suggestion to include purchase options in the lease calculations. However, if there is a 95% chance a purchase option would be exercised in year 2, why would a 2-year term not be a reasonable lease term even if the lease term only called for a 5 year term?

We agree that the longest possible term that is more likely than not (MLTN) to occur is a reasonable approach to determining the lease term. The MLTN standard also seems like a reasonable measure for contingent rentals. Why all the probability methods? We do not believe that different probability methods make the estimates more accurate; we believe different estimation methods make the process more complicated and less internally consistent. We believe the MLTN method is easier to apply in practice and using it as a measure for contingent rentals would not detract from the benefits of the proposed standard.

We suggest a single estimation method. We suggest the MLTN method be used to determine the lease term, the contingent rentals and any other estimates in the proposed standard. Simplicity helps understandability.

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?

We agree. Contingent rentals are often a significant part of the rental cost. If contingent rentals are not included, we believe it would open a door for abuse by adding remote contingencies in order to exclude the payments from the liability calculation. We do not believe remote contingencies should ever be a factor in financial statement recognition or disclosures and therefore we agree – reasonable contingencies should affect the liability and asset calculations.

We recognize that this may be initially difficult to institutionalize, but we also believe that for lessors and lessees, contingent rentals are estimated during lease negotiations. The estimates will not be correct; they will be estimates. We believe as long as the audit profession adheres to the practice of allowing some reasonable changes in estimates and does not require changes for every possible change in estimates on an annual basis, the inclusion of contingent rentals will be workable. There will be firms who attempt to make annual adjustments to assets and liabilities for small changes in future estimates that will increase the cost of compliance with the proposed standard. We believe this is an inherent problem in the audit process, not the proposed standard, but the standard will be blamed for this increased cost and complexity. For that reason, we think it is reasonable for an example to demonstrate that small estimate changes do not always result in changes in assets and liabilities. We believe that the Board and staff are made up of reasonable individuals and can use their judgment to craft an appropriate example that would be educational and illustrative for practitioners, preparers and users.

This is another area where we had substantive debate. The debate centered around whether an event that might happen is relevant to users. We believe that probability weighted liabilities are not as relevant as certainties but realize that structuring may cause some relevant items to be excluded. We believe that a substance-over-form recognition screen should apply to accounting transactions in order to prevent “in form” manipulation (such as 1-year renewable lease periods) and that the “in substance” guideline should be “MLTN”. We recognize that we are compromising our view of theoretical purity in order to account for the practical reality that form over substance manipulation is the problem with existing lease guidance and needs to be avoided in some way.

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?

Yes, we agree that remeasurement is appropriate if facts and circumstances change in a significant way. We believe it would be wise to show examples of when changes occur but do not result in remeasurement. We would suggest that the phrase significant be further explained with examples that show the difference in significant or insignificant. A discussion of the meaning of the word significant or insignificant could be included in the basis for conclusion as well. We believe that without a better understanding of the word significant, diversity in practice will occur and lead to unnecessary expense to some private companies that rely on auditors more than their public company counterparts. We understand that the accounting standard cannot dictate audit processes, but we believe it is important to explain the word significant from an accounting principles standpoint in as clear a fashion as possible in order to help ensure consistent application of the proposed standard’s intent.

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).

We agree with the sale leaseback treatment.

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?

We believe the criteria are appropriate.

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?

(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?

We agree that lease liabilities should be separately stated on the face of the balance sheet, only if they are a material source of financing but not separately presented only because they are leases. We understand that the proposed standard only applies to material items, but the definition of materiality is somewhat subjective. If a lease is immaterial, maybe it is not subject to lease treatment at all, for example a lease for \$1 a month. However if a lease is material enough to be recognized as a lease for asset and liability

treatment, it may be logical to some that it is therefore required that it be separately stated on the face of the balance sheet. We believe leases should be treated like any other asset or liability – separate statement on the face of the balance sheet if they are significant enough to warrant separate presentation. Otherwise, we believe requiring separate presentation without this significance qualification will lead to clutter on the face of the balance sheet that will not improve the presentation of relevant financial information to users.

We would like to point out that some companies ‘lease’ spare parts or other items of inventory as a means of financing. We believe it would be more appropriate to require presentation of the right of use asset in the same section of the balance sheet as the asset would appear if it were acquired for cash, rather than to require presentation as a part of property, plant and equipment.

We believe the disclosure of lessor assets and liabilities is difficult to present simply on the face of the balance sheet. For entities whose business is predominately leasing, the gross to net presentation may be more appropriate than for an accounting firm who owns its office building and leases a small amount of space to unrelated tenants. Would the accounting firm move the entire building out of PP&E and show it as a leased asset or only the portion of the building that is leased? Would moving the entire asset improve the information to users? We believe not. We believe only assets that are substantially leased or whose purpose is ‘held for leasing’ should be separately stated from operating PP&E if the business of the entity is not generation of rentals or capital gains through the ownership and operation of rental properties.

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?

We believe this separation could be presented in the notes to financial statements without sacrificing the need or access to the information. There are many presentation differences on the income statement among companies and industries. Depreciation and amortization are often combined on the face of the income statement. Interest income and expense are often combined on the face of the financial statements. Existing rental expenses are rarely disclosed on the face of financial statements but disclosed in the notes. The changes in recognition and measurement are the significant improvements to lease accounting. The previous problems were not disclosure or presentation, separate from the recognition and measurement.

Requiring separate income statement disclosure of lease expenses or income may not improve relevant information available to the user. To understand more fully the lease activity, the user should refer to the notes which should provide the additional details including where on the income statement the components of lease expense are included (i.e. COGS, depreciation and amortization, interest expense, selling expenses, etc.).

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 believe that the cash flow statement has structural issues that hinder the presentation of lease expenses in a way that is simple to understand. We believe that separating lease expense between its amortization

and interest components is not helpful to users in understanding cash flows. We also believe that lease expenses are normally operating in nature but could be seen as financing to some extent. We do not believe that the separation is meaningful or relevant in all instances.

We believe that presentation on the cash flow statement should allow for a combined lease expense in some way which would allow users to see the impact of leases on cash flow without having to deconstruct the cash flow statement. Whether that presentation is in one of the main sections of the cash flow statement, a subsection of the statement or as a note to the statement similar to income taxes paid, we believe it has to be shown as a total amount.

Our favored presentation is as a component of the operating section of the statement.

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?**

We believe certain quantitative information should be disclosed, such as discount rates used, terms and other significant assumptions. We believe some disclosure of qualitative information is necessary but that users of private company financial statements have access to this information in other ways. Reduced disclosures, especially of subjective or qualitative information, will help to keep annual audit costs down by reducing disclosures without reducing the relevant information available to users of private company 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?**

We believe the proposed transition methods are reasonable and appropriate.

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 believe that the cost benefit calculation is a cornerstone of standard setting. We believe that this proposed standard will add to ongoing costs of accounting for leased assets. We also believe that the accounting can be accomplished without adding significant expertise or the use of experts to comply with the guidance on an annual basis. The calculations for capital leases and the calculations required under the proposed standard are similar, the proposed standard only increases the scope of leases to which the calculations apply.

We believe the implementation costs may be significant to companies with many operating leases that will be capitalized as right of use assets. Not all systems will have the ability to allow for adjusting asset values without catching up accumulated depreciation as required under the proposed standard. Not all systems will have functionality to amortize loan balances. Processes for coding rental payments will have to change and systems will have to change and these changes may be significant to some companies. It is not true that software companies can issue a 'patch' to fix existing systems. Modern financial systems are complex and require significant testing, not all companies keep their systems up to date due to this testing requirement and new 'patches' often require bringing the systems up to date with previously unapplied 'patches'. In addition, not all companies pay for the maintenance required to keep their systems up to date or are on versions of systems that are no longer supported.

However, we believe the existing lease rules are a failure and the proposed standard is an improvement that will result in benefits to users of financial statements. We would suggest a significant amount of time be allowed between issuance of the final standard and the required implementation date. We believe four years may be required to implement such a costly standard without incurring higher costs to expedite the large-scale changes that may be required. A long implementation period may allow companies to absorb the additional costs and make the implementation changes without a 'Y2K-type' effort.

We also believe that the cost to private companies will be reduced if the standard is delayed for two years beyond the implementation date for public companies. This will allow software companies to focus on their public clients and allow the public companies to bear the burden of being first adopters.

We know this sounds like a long time to go without the benefits of the proposed standard, but changes to the leasing standards have been years in the making and rushing the implementation period will not change the end result, only make it more costly.

Other comments

Question 18

Do you have any other comments on the proposals?

We believe that some smaller private companies do not normally use long term debt as a source of financing. Some companies are owner financed and use leases as their only source of outside financing. The discount rate for these companies may not be as apparent as it would be to a company with a bank revolving line of credit. For this reason, we request that some form of safe harbor rate method be allowed as a proxy for the incremental borrowing rate used in lease discounting.

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?

We have tried to incorporate private company concerns in our responses above. We appreciate the Board's request for private company considerations and recognize this as an improvement in the outreach efforts to better meet the needs of private company statement users.

Thank you for considering our comments. If you have any questions or wish to discuss this letter, please feel free to contact me at (704) 365-7382 or by email at gwbeckwith@NationalGypsum.com, or Ronald Wei at FEI (973) 765-1025 or by email at rwei@financialexecutives.org.

Sincerely,



George W. Beckwith, Vice Chair

Committee on Private Company Standards
Financial Executives International