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Sir David Tweedie IFRS Foundation First Floor 30 Cannon Street London, EC4M 6XH

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Not Confidential

Dear Sir David,

ED 2010/9 Leases

Nationwide Building Society welcomes the opportunity to respond to the exposure draft ED 2010/9 Leases.

Nationwide is the largest Building Society in the United Kingdom with 824 branches and total assets of approximately £190 billion. It is the third largest savings provider and third largest residential mortgage lender in the UK.

We have not separately contributed to any other bodies' responses to the ED.

Overall Comments

We recognise the concerns of the inconsistency in IAS 17 of the treatment of finance and operating leases and thus the need for an updated Standard. In our view, however, the proposals presented in ED 2010/9 are not practicable, in particular for organisations with several hundred leases (in our case, mainly as lessees of properties and ATM sites) and add unnecessary complexity to financial statements.

Under the lessee model our preference is that operating leases are not included in the balance sheet. However, if lease liabilities are to be recognised, the requirement to determine assets and liabilities on the basis of the longest possible lease term that is more likely than not to occur, in addition to the requirement to estimate contingent rentals and residual value guarantees introduces a significant level of judgement and will result in significant implementation costs for preparers of financial statements.

It is likely that organisations will need to implement new systems and employ additional resource - costs which we believe will far outweigh the benefits of the proposals.

To address these concerns we would recommend the recognition of assets and liabilities on the balance sheet is based on the minimum lease term and cash flows, with additional disclosures to provide an overview of options to extend/terminate, contingent rentals etc.

We also consider that accounting for the lease liability can be simplified by removing the requirement to account for interest on an effective yield basis. This would both reduce the implementation burden for the preparer and the complexity for the users of financial statements.

We also have concerns over the complexity of the operating lease proposals, in particular for those companies where leasing is not part of the 'core' business.

Our detailed responses to certain of the specific questions posed in the exposure draft are presented below in the annex to this letter. We have no comment on the other questions.

We hope that you find the above comments useful and would hope they are taken into account in seeking a practical solution. If you would like to discuss our comments in more detail please contact myself on 01604 852087 or via ian.cragg@nationwide.co.uk.

Yours sincerely

lan Cragg Finance Manager

Annex to Nationwide Building Society's response to ED 2010/9 Leases

Responses to Specific Questions

We have responded only to those questions where we have specific comments to raise:

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?

In general, we consider the lessee model to be too complicated to apply, particularly where an entity has potentially several hundred property lessees previously accounted for as operating leases. We consider that the costs of meeting the requirements outweigh the benefits and do not provide decision useful information.

Currently, operating lease liabilities are disclosed in the notes and an alternative approach could be to enhance these disclosures (e.g. by including the best estimates of renewals and contingent rentals).

(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 the right-of-use asset needs to be amortised, but consider that recognising interest on the liability on an effective yield basis is too complex and inconsistent. We suggest accounting for the interest on a straight line basis which thus matches the straight line amortisation of the right of use asset. Thus, assuming that the period of the lease and right of use asset life are equal, the interest charge and the amortisation will equal the amount paid in any period.

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?

We do not consider that current lessor accounting requires significant revision. Furthermore, we consider the proposed two model approach for lessors confusing to users. If necessary, our preference is to have the performance obligation approach only, with the alternative of full derecognition if significant risks and rewards are not retained.

We note that the ED does not apply where the lessor applies the fair value model in IAS 40 (Investment Properties). However, it should be noted that a number of properties leased out by a retailer may not satisfy the definition of Investment Properties because the portion let may not be capable of being sold separately (ref IAS 40 par 10). Thus the option of using IAS 40 to avoid the complexities of this ED may not be available.

(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?

In respect of the performance obligation approach, we do not agree with the creation of a further asset in addition to the existing fixed asset because of the complexity of the calculation and potential confusion.

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 do not agree with the proposal to determine the lease term by reference to the longest period that is more likely than not to occur. We believe that this requires too much judgement and for several hundred leases the proposed methodology is impracticable. We consider that the lease term should be the minimum payments that are (in practice) non-cancellable and that would better reflect the usual understanding of a liability.

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?

As with question 8, we consider that this requires too much judgement and for several hundred leases the proposed methodology is impracticable.

Question 12 – Presentation - Statement of Financial Position (Balance Sheet)

(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?

We consider that the right-of-use asset should clearly be distinguished from owned property, plant and equipment or investment property. We would expect the split to be in notes, unless so material that disclosure on the face of the balance sheet is appropriate. A similar treatment for the liabilities is appropriate.

(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?

As detailed above, we do not agree with the proposed lessor model. However, we would agree that the three items should be netted off as described. The netting off should be in the notes and not on the face of the balance sheet.

Question 13 – Presentation - Statement of Comprehensive Income

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

We agree that, for example, lease amortisation and lease interest expense should be disclosed separately within the amortisation and interest expense notes (reference ED par 26).

Question 15 - Disclosure

Do you agree that lessees and lessors should disclose quantitative and qualitative information that: (a) identifies and explains the amounts recognised in the financial statements arising from leases; and (b) describes how leases may affect the amount, timing and uncertainty of the entity's future cash flows (paragraphs 70–86 and BC168–BC183)? Why or why not? If not, how would you amend the objectives and why?

We agree with the disclosure principles in (a) and (b), but are concerned with the burden imposed by the quantity of information requested in par 70 - 86 of the ED. In the UK, Annual Reports in the Banking industry are already very long. Furthermore, the Financial Reporting Council in the UK is currently engaged in a project to reduce the complexity in Corporate Reporting.

Question 16 – Transition

(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? (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?

Under the lessee model, we agree that it may be intellectually difficult to make a case for 'grandfathering' existing operating leases where these are material to an entity's operations. However, we are concerned with the burden imposed in obtaining the information retrospectively for a large number of leases and would prefer the enhancement of existing disclosures noted in question 1 above.

In respect of the lessor model, we consider that existing leases should be 'grandfathered' because the existing lessor model can still be regarded as 'fit for purpose'.

Question 17 – Benefits and Costs

Paragraphs BC200–BC205 set out the boards' assessment of the costs and benefits of the proposed requirements. Do you agree with the boards' assessment that the benefits of the proposals would outweigh the costs? Why or why not?

We are concerned with the burden of the ED proposals as already outlined by the Retail industry in BC203. Whilst we acknowledge that BC205 states that 'detailed examination of every lease is not required unless a significant change in the lease payments is expected...' this does not affect the requirement to examine each lease initially on adoption.