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Financial Accounting Standards Board

We appreciate the opportunity to comment on the recent Exposure Draft (ED) on lease accounting.

The ELEX Group, Inc. is an independent leasing company that has been in the leasing industry for over 35 years. As a 2nd generation small business we have focused on middle market lease transactions ranging from \$100K to \$2.0M. We provide a needed service for our customers and the business environment, and that is another source of capital to finance their needed capital equipment. My fear is that with the new proposed accounting changes companies such as ours that provide a needed service to the business community will disappear. I believe that due to the administrative burden and extreme cost for lessees to account and comply with the new lease accounting rules that customers will move away from the lease financing option. With the current proposed accounting regulations the benefits that lease financing provides will not outweigh the costs associated with compliance of the new accounting model.

Please don't just take my comments as self serving because we are a lessor and in the leasing industry. As a provider of financing to our customers we are also a reader of financial statements. Since we grant credit to our customers to acquire the necessary equipment to run their businesses we need to analyze our customers credit worthiness and financial position. We also are a lessee as we lease some of our office space and equipment to operate our business. So we are a stakeholder in all facets of the leasing industry.

We commend the FASB & IASB for their efforts. I agree that it is of most importance that readers of financial statements are provided with the necessary information to determine the true obligations of a company and the financial position of that company. The primary objective of the ED was to eliminate differences in accounting by two separate lessees for two economically similar transactions. However with the proposed changes I feel that with the increased amount of estimation required on the part of the lessee it will create more areas where differences in accounting could come out and more likelihood that economically similar transactions would be treated differently. While I agree that it is important that users of financial statements should be provided with information to determine their operating lease obligations, I do not feel that this would require recognition of an asset and liability. I believe that the current requirement of footnote disclosures is sufficient in accomplishing this objective in a cost effective manner. I would like to comment on several areas of the ED and concerns and issues I have specific to each area and other overall concerns regarding the proposed accounting changes.

Increased Cost for Compliance:

The proposed accounting changes would drastically increase costs for the lessee to comply with these new regulations. Not only will there be increased cost for the lessee in the initial reclassification of existing leases or when a new lease is put on the books, but also the requirement to continually reanalyze and reclassify each lease for every reporting period. This administrative burden will prove too costly for lessees and will create situations where management will make a cost / benefit analysis and either 1) make it a policy not to lease or 2) not diligently comply with the regulations (which would defeat the purpose of the ED). We have estimated the cost of compliance on behalf of lessees and lessors and this number is staggering. If you look at a small or medium sized organization that has 1,000 leases, the cost for the staff to review the leases at approximately \$100 / hour, and assume an average of 2 hours per lease, this would equate to \$200,000 in added cost. Since the ED requires that the leases be reanalyzed at each reporting period this \$200,000 cost would be quarterly (or an added annual expense of \$800,000 for compliance).

Job Losses:

The leasing industry is broad and is utilized for the acquisition of both equipment and real estate. The majority of users in the equipment leasing industry are small and medium sized enterprises (SME). The SME group utilizes the leasing option because it provides another source of capital that is easily available to operate their business and it is an efficient way to acquire equipment necessary to run their business. The SME sector is not the group that is manipulating the current accounting rules for off balance sheet treatment. The small business sector is the largest potential for job growth and the proposed lease accounting changes will increase costs and create a huge compliance burden for both lessees and lessors that will eliminate any potential job growth for the current economy. Not only will there be an increased cost for compliance with lessees and lessors, but there will also be a direct increase in expenses on a lessee's income statement. With the proposed accounting changes, due to the front loading of expenses for the lessee, lessees will have to either lay off employees and or increase prices to their customers to compensate for lower income that they will be showing to their shareholders. As an example it is estimated the Walgreens who leases all of their locations will be capitalizing over \$30Bill in operating leases thus creating an increase in front loaded expenses of over \$100mill which will inevitably require them to look at how to reduce other expenses to show the income demanded by their shareholders, hence potential lay offs.

Increased Complexity:

The proposed accounting changes are much more complex and leave to much room for interpretation which creates more areas where manipulation of the accounting can be done. The proposed changes have too many areas where estimation is required on behalf of the lessee as to what should and should not be included in the asset and the liability calculation (i.e. lease term, contingent rents, renewal options, residual guarantees, etc.). The purpose of the ED was to have transparency in accounting for economically similar transactions but with the amount of estimation and interpretation the ED missed the mark in accomplishing this. There is no distinction made between the small equipment leases that make up the majority of lease transactions with SME and the more extremely complex operating leases that were structured with the sole purpose of off balance sheet treatment in mind. In trying to combat the presumption of inconsistent treatment in a very small percentage of leases, the ED imposes substantial costs for all entities. It is our belief that the requirement of recording an asset and liability on the lessees books, provides no greater assistance for a reader of their financial statement in determining their obligations and financial strength than the current footnote requirements. Further, the requirement to book this asset and liability by the lessee creates more complexity in their financial statements and makes it that much

more difficult to determine a companies true financial obligations. Under the current FASB 13 rules any reader of a financial statement will include the operating lease liabilities in their calculations and knows where to readily find them.

One suggestion would be to apply a materiality test to all leases and require these larger more complex structures to be capitalized and leave the non material transactions and non manipulators of the rules as they are. The cost and burden of compliance for all leases will be very expensive and not add much transparency to their financials. If you carve out the non material leases from the ED it will significantly reduce the compliance costs for the majority of lessees and make the compliance to the new rules much more likely.

Lease Renewal Options:

On the issue of contingent rent and renewal options, I do not believe that renewal options and contingent rent should be included in the calculation for the capitalized liability. The very definition of a renewal option & contingent rent do not meet the definition of a liability and that is “an unconditional obligation to pay it”. These options are just that “Options” that may never be exercised and therefore would never become obligations and to put a valuation on these and capitalize them as a liability would be misrepresenting the true financial position of the lessee. Creating a system that requires a lessee to estimate the probability that a renewal option would be exercised and to continually reevaluate that agreement at every reporting period will bring too much subjectivity into the process thus reducing the comparability of the transactions. Again, creating more opportunity for economically similar lease transactions to be accounted for differently, which is the opposite of the Boards objective with the ED. It is our opinion that the lessee should only be required to capitalize the actual contractual obligations / lease payments at the inception of the lease and at the end of the initial term of the lease, if the renewal options are exercised then re-book the lease based on the new contractual rent obligations. This is the time when these “options” are converted to a true liability and a contractual obligation and this is the time that they should be reflected as a liability on the lessees books.

Amortization and expenses:

The requirement of booking a ROU asset and corresponding liability creates front end loaded expenses on the part of the lessee and makes it more difficult for a reader of financial statements to understand the true cash obligations of the lessee. The proposed accounting for a lease does not follow the cash. Readers of financial statements are more concerned with the cash obligations and the cash flow of a company, not the amortization of the ROU of an asset. By amortizing the ROU asset and expensing the liability, the lessee will have front loaded expenses for all their leases which will 1) make it more difficult for a user to determine the true cash obligations of a company and 2) make it less attractive as a financing option on the part of the lessee. With the old accounting method it was much easier to determine the true cash obligations for a lease. Readers are used to seeing rent expense on the income statement and expect these costs to be reflected on a straight line basis, which under the ED model they will not. The lease payments are level throughout the lease term and the recorded costs of the lease should reflect this as apposed to being higher in the earlier months. The lease cost to the lessee is the same in the first month as it is in the last and the accounting of this expense should reflect that.

The monthly rental requirements should be accounted for to reflect what they actually are, an expense item and not an asset or liability. This allows the lessees income statement to match the true expense to the company – the monthly rent payment and not a front loaded expense model that reflects amortization of a ROU asset and interest expense. This way the expense reflected on the income statement is really what the lessees cash expense obligation is.

In summary we feel that the new ED does not meet its primary objective and that is to create transparency for users of financial statements and simpler financials for a user to read. Due to the complexity of the reporting requirements and the multiple areas of interpretation on the lessees part to capitalize the lease obligation, there is more confusion for lessees to comply and more opportunities for manipulation of the accounting treatment. All of these concerns will create a much higher probability that economically similar leasing transactions will be recorded and treated differently. The accounting of leases should be transparent and reflect the true economics of the transaction but the ED falls short of this goal. While we feel it is important for readers of financial statements to be presented with the lease obligations of a lessee, we do not feel that this would require recognition of an asset and a liability. At the very least we feel strongly that a materiality test should be applied to all leases and only those leases that are of material consequence be subject to capitalization. There is too much cost and burden for a lessee to capitalize and account for a lease transaction that is of little financial significance to a customer's overall financial position. By establishing a materiality test you won't be punishing those companies who lease the necessary equipment to operate their business and focus the scrutiny and compliance requirements to those companies who are entering into financially structured and financially sophisticated transactions solely for their accounting treatment.

I thank you for this opportunity to comment on the ED and should the board like to discuss any areas of my comment letter please do not hesitate to contact me.

Sincerely,

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