September 7, 2010

by: e-mail

Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116

Dear Sir or Madam:

You have asked for comments on the Exposure Draft on Lease accounting dated August 17, 2010. As the Chief Financial Officer for a large not-for-profit organization (annual revenue of approximately \$400 million) that incurs approximately \$8.5 million of annual rent expense for facilities and equipment, this proposed pronouncement is of great interest and concern to me. I am submitting this comment in opposition to the overall change in approach for operating leases for the following reasons:

- 1. The recording of an asset and liability on the lessee's books unnecessarily grosses up the balance sheet and, in my opinion, provides no greater assistance to the financial statement reader than comparable disclosures in the footnotes would do. In fact, I believe it will draw unnecessary attention to the lease-related captions in the balance sheet and, due to the materiality of these figures, potentially divert the reader's attention from other important items. With respect to the lessee, there could be an impact on debt covenants calculations that, while a problem that can be addressed, seems unnecessary to me.
- 2. Far more importantly than #1 above, I believe the proposed guidance provides a poor matching of expense to revenue. Under current guidance, using a leased asset in the generation of revenue provides a level charge to expense in the form of rent over the lease term. If a lease has annual inflationary increases, that charge to expense would similarly increase over time. This would generally match revenue, which the enterprise would expect to be relatively constant, preferably even increasing with inflation over that same lease term. Accordingly, the current accounting treatment does a good job of matching expense to revenue.

The proposed guidance unravels this process. Rather than provide a level, or slightly increasing, charge to expense over the lease term, the use of the effective interest method to amortize the balance sheet liability will result in the highest charge to earnings in the first year, with the charge decreasing in each subsequent year. In a typical scenario, revenue would increase during the same term, creating a greater mismatch in the later years of the lease.

In addition to a matching problem, consistent measurement of expenses also comes into play. At the end of the original lease term, or whatever term is utilized under the "more likely than not" approach, so long as the business need remains, the lessee will either

renew the existing lease or execute a replacement one. At this point, the annual expense charge will jump dramatically as the lessee moves from the last year of the old lease (ie. the lowest expense period) to the first year of a new lease (ie. the highest expense period, at then-current market conditions). There could be situations where annual expense doubles or triples in one year after 5 or 10 years of steady declines. Thus, the lessee would experience significant fluctuations in expense based solely on the timing of lease terms, even though the asset being utilized remains basically unchanged. This further exacerbates the matching issue previously discussed.

In Devereux's industry, predictability of expenses is important. We provide behavioral health and educational services to individuals with special needs. The vast majority of services are provided under contracts with governmental agencies as we relieve the government of its burden to serve this population. Our programs are heavily regulated, with reimbursement for services often driven by the actual expenses of providing them. In many cases, "allowable" or "audited" expenses of one year provide a maximum reimbursement ceiling for a subsequent year. Then, in the subsequent year, our total revenue will be capped at the lesser of "trended" prior year expenses (ie. actual expenses in a prior year, adjusted for market basket inflation, if any) or actual current year expenses. Assuming all other expenses remain equal, the reimbursement for lease expenses in the declining years of the original lease will be capped at actual costs for that year. However, in the year of crossover to a new lease, the trended prior year cost would become the baseline, effectively resulting in the entire "one-time" increase to be incurred outside of the reimbursement ceiling, negatively impact bottom-line results. Thus, the change in accounting guidance, in addition to creating a mismatch of expense to revenue, would actually have a negative impact on our organization's finances and those of others subjected to similar rules. This would be one of the unintended consequences of the FASB's effort to improve financial reporting.

It is my understanding that accounting principles and procedures are designed to provide timely, accurate and consistent measurement of financial results and financial position. In my opinion, this proposed guidance compromises these goals and, as illustrated above, has the potential to adversely impact the organizations whose financial reporting it is trying to improve. Most definitely, we do not support the concepts outlined in this Exposure Draft and are concerned about the negative impact it will have on our operations.

Thank you for the opportunity to comment. If you would like to discuss this further, I can be reached at 610-542-3063.

Sincerely,

Robert C. Dunne, CPA Chief Financial Officer The Devereux Foundation

Cc: Mr. Robert Shope, Partner – Ernst & Young