16 September 2010

International Accounting Standards Board
(IASB)

Dear Sir/Madam,

Response to ED/2010/9 ***Leases***

1. I thank the IASB for the opportunity to comment on the aforementioned ED. Before I proceed to articulate my views on this ED, I would like to emphasise upfront that the comments that are expressed herein are solely my ***personal views*** and strictly do ***not*** reflect those of any organisation to which I may be associated presently and/or previously in various capacities.

2. I welcome the joint efforts of the IASB and FASB in coming together to develop and promulgate a common accounting standard for leases. Indeed, the distinction made between finance and operating leases in the present IAS 17 has been the source of problems that investors and other financial statement users face when estimating the extent of financial leverage and earnings of entities that actively engage in such arrangements. It has also been the subject of ethical abuse by some entities who resort to “off-balance sheet financing” tactics to mask the true extent of their financial gearing. The headline proposal in ED/2010/9 to abolish the distinction between finance and operating leases is therefore a step in the right direction. I believe this will improve the financial reporting for lease arrangements, making it more transparent for investors and other financial statement users.

3. However, while I fully support the key proposal to eliminate the finance/operating lease dichotomy, I have some reservations on the principles underpinning the new approach to lessor accounting that the Boards are proposing. The ED requires lessors to account for a lease using either a performance obligation or derecognition approach, depending on the lessor’s exposure to the “risks or benefits” of the underlying asset. This seems to be conceptually inconsistent with the paradigm shift from a “risks and rewards” to a “control” model that the Boards have recently proposed in ED/2010/6 *Revenue from Contracts with Customers*. In my view, the lease income that lessors receive is in substance a form of revenue. As such, for conceptual consistency, lessor accounting should be based on the same model as revenue accounting. It perturbs me that the Boards are retaining the “risks and rewards” model for lessor accounting whilst transitioning to the “control” model for revenue accounting. As I see it, this appears to be a sign that the Boards are undecided as to which model is conceptually superior for financial reporting. I strongly urge the Boards to

"put the horse before the cart" and to initiate a conceptual debate on the merits of the "risks and rewards" model vis-a-vis the "control" model. As I had earlier suggested in my response to ED/2010/6, this should be done in the context of the joint Conceptual Framework project.

4. I am aware that the Boards are under tremendous time pressure to complete the projects under the Memorandum of Understanding (MOU) by June 2011. Notwithstanding this, it would be strategically myopic to sidestep difficult conceptual issues just for the sake of meeting aggressive project timelines. Conceptual inconsistency would not only defeat the purpose of the current reforms to enhance the financial reporting standards, but would also undermine investors' confidence in financial reporting and the accountancy profession at large. In the ultimate analysis, the development of a set of high-quality global accounting standards has to be based on sound, rigorous and consistent conceptual foundations. I fervently hope that the Boards will not compromise sound principles for short-term expediency in their ongoing work to revamp and converge the accounting standards.

5. My comments to specific questions posed in the ED can be found in the **<u>Appendix</u>** to this comment letter.

Yours faithfully,

LINUS LOW

Appendix

Question	Comments
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?	(a) I agree with the proposed lessee accounting model. I think the recognition of a right-of-use asset and a liability in the books of the lessee provides a more faithful representation of the economic substance of a lease arrangement than the existing finance/operating lease accounting model in IAS 17. As I mentioned in my covering letter, the abolition of the distinction between finance and operating leases will significantly eliminate the problem of "off-balance sheet financing" and thus improve the financial reporting for lease arrangements, making it more transparent for investors and other financial statement users.
(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?	(b) I have no issues with the proposal to amortise the right-of-use asset and recognise interest on the lease liability. The amortisation of the right-of-use asset is consistent with the principles espoused in the IAS 16 and IAS 38 for non-current tangible and intangible assets. The same is true of the proposed recognition of interest on the lease liability, which is aligned with the effective interest method for the subsequent measurement of financial liabilities at amortised cost.

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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?	(a) As I understand it, the phrase "risks or benefits" is equivalent in meaning to "risks or rewards". If so, then the Boards are essentially espousing a "risks and rewards" model for lessor accounting. This seems to be conceptually inconsistent with the paradigm shift from a "risks and rewards" to a "control" model that the Boards have recently proposed in ED/2010/6 *Revenue from Contracts with Customers*. In my view, the lease income that lessors receive is in substance a form of revenue. As such, for conceptual consistency, lessor accounting should be based on the same model as revenue accounting. It perturbs me that the Boards are retaining the "risks and rewards" model for lessor accounting whilst transitioning to the "control" model for revenue accounting. This appears to be a sign that the Boards are undecided as to which model is conceptually superior for financial reporting. I strongly urge the Boards to "put the horse before the cart" and to initiate a conceptual debate on the merits of the "risks and rewards" model vis-a-vis the "control" model. As I had earlier suggested in my response to ED/2010/6, this should be done in the context of the joint Conceptual Framework project. A further discomfort that I have with the proposed lessor accounting model concerns what the ED terms as the

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	"derecognition approach". This requires the lessor to derecognise a portion of the underlying asset representing the lessee's rights and to reclassify the remaining portion as a "residual asset" representing its right to the underlying asset at the end of the lease term. I question the relevance and usefulness of including a "residual asset" in the statement of financial position when the lessor determines that it no longer retains significant risks or benefits in the underlying asset. In fact, I would argue that if the lessor deems that it no longer retains significant risks or benefits in the underlying asset, an asset sale has in substance taken place and the entire carrying amount of the asset should be derecognised. From a practical standpoint, requiring lessors to decide between the "performance obligation approach" and "derecognition approach" introduces unnecessary subjectivity and complexity into lessor accounting and hardly provides financial statement users with more decision-useful information. On the basis of the foregoing argument, I urge the Boards to jettison the "derecognition approach" in the proposed lessor accounting model. In my view, lessors should all consistently apply the "performance obligation approach", as this provides a more faithful representation of the economics of the lease

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	arrangement. (b) As explained and stated in my response to part (a), I do not agree with the principle and mechanics of the proposed "derecognition approach". However, I do agree with the Boards' proposal on the principle and mechanics of the "performance obligation approach".
Question 3: Short-term leases The 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 twelve 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 recognise lease payments in profit or loss 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 recognise assets and liabilities arising from a short-term lease in profit or loss, nor derecognise any portion of the underlying asset. Such lessors	I welcome and support the Boards' proposal to provide some relief to both lessees and lessors for short-term leases. Given the short-term duration of such leases, the costs of complying with the full requirements proposed in the ED would be substantial and most likely outweigh the benefits in practical terms. For lessees, the discounting effect is expected to be immaterial because of the short lease duration. Hence, it makes sense to relieve lessees from the requirement to discount the lease payments. I believe that the majority of preparers will elect to employ the proposed simplified treatment for short-term leases when such transactions arise in practice. This should result in consistency and comparability of the financial statements with respect to the reporting of short-term leases.

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would continue to recognise the underlying asset in accordance with other IFRSs and would recognise lease payments in profit or loss 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?	
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?	(a) I think the proposed lease definition in the ED is appropriate. The proposed definition is largely consistent with the principles in the existing IAS 17 and IFRIC 4. (b) In paragraphs 8 and B9, I again see the Boards vacillating between the "control model" and the "risks and rewards model" (see also my comments to Question 2(a)). Specifically, the segments "…transfers…*control*" and "…all but a trivial amount of the *risks and benefits*…" [emphasis added] in paragraph B9 appear to be a confounding concoction of the two models. Let me reiterate my earlier point that the Boards should seriously evaluate the conceptual merits of the "risks and rewards" model vis-a-vis the "control" model and take a consistent stance on which model to adopt for financial reporting.

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	Furthermore, it is unclear as to what threshold corresponds to "trivial" in paragraph B9. For clarity and to pre-empt inconsistent application in practice, I think the Boards should define "trivial" clearly in Appendix A to the proposed IFRS, and also provide examples in the application guidance to illustrate its meaning. (c) I think the guidance in paragraphs B1 – B4 for distinguishing leases from service contracts is adequate. I have nothing further to add.
Question 5: Scope exclusions The exposure draft proposes that a lessee or a lessor should apply the proposed IFRS 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 IFRS? Why or why not? If not, what alternative scope would you propose and why?	I broadly agree with the ED's proposed scope, but I beg to differ on the Boards' proposal to scope out leases of intangible assets. I am not convinced by the Boards' rationale for excluding leases of intangible assets (paragraph BC36 of the Basis for Conclusions). In my view, if there is no conceptual reason to exclude intangible assets from a leasing accounting standard, it should be duly deliberated and included in the proposed IFRS for Leases. Furthermore, if it is the Boards' intention to consider leases of intangible assets as part of a broader review of the accounting for intangible assets, then the revenue accounting of licences that do not amount to a sale of an entity's intellectual property (IP) should similarly be scoped out of the proposed IFRS for Revenue (as exposed recently via ED/2010/6 *Revenue from Contracts with Customers)*.

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	More specifically, I refer to Question 16 of ED/2010/6. The said question dealt with the proposed revenue recognition principles for licences that do not amount to a sale of an entity's IP. In my comment letter dated 16 August 2010 to the said ED, I contended that in substance, a licence to use an entity's IP - if it is not considered to be an IP sale - entails the granting of a "right-to-use" asset by the IP owner to the IP user, and ipso facto, amounts to a leasing arrangement. I expressed the view that it would be more appropriate to consider the accounting for IP licences under the scope of the joint Leases project, and further urged the Boards to re-expose the issue under the joint Leases project. On the basis of the above arguments, I call on the Boards to include intangible assets in the scope of the proposed IFRS for Leases and to re-expose the accounting for licences that do not amount to a sale of an entity's IP as a follow-up to the current ED/2010/9.
Question 6: Contracts that contain service components and lease components The exposure draft proposes that lessees and lessors should apply the proposals in *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	I direct my comments to the IASB's proposal in part (b) of the question. As stated in my earlier response to Question 2(a), I do not believe that the "derecognition approach" in the proposed lessor accounting model provides relevant and useful information. In my view, the Boards should jettison the "derecognition approach" and instead, require all lessors to consistently apply the "performance obligation

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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 proposals in *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?	approach". Therefore, I do not agree with the IASB's proposal in part (b)(iii) of the question. Consistent with my recommendation to require all lessors to apply the "performance obligation approach", I would very much prefer all lessors to apply the "performance obligation approach" to the combined contract in cases where the service components are non-distinct. Nonetheless, should the Boards finally decide to retain the proposed "derecognition approach" in lessor accounting, I am more inclined to support the FASB's proposal in part (a) of the question to apply the lease accounting requirements to the combined contract. I find the FASB's rationale in paragraph BC52 of the Basis for Conclusions to be more convincing than the IASB's arguments in paragraph BC53. For the IFRS to be a strong set of principle-based standards, consistency in the application of fundamental principles is paramount. Deviations from those fundamental principles, while seemingly innocuous when seen at a "case-by-case" level, could well trigger a creeping trend towards "rules" in standard-setting. This would be undesirable, as it vitiates the conceptual foundations of the IFRS over time.

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Question 7: Purchase options The exposure draft proposes that a lease contract should be considered as 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?	I agree with the Boards' conclusion that a lessee or lessor should only account for a purchase option at the point of exercise. I think it is logical and sensible to treat the lease contract as terminated when the purchase option is exercised, and to account for the transaction as a purchase by the lessee and a sale by the lessor. In my view, the proposed accounting treatment faithfully reflects the legal and economic intent of incorporating a purchase option in a lease contract. However, in more complex lease contracts, it may be necessary to consider the purchase option clause in relation to other contractual clauses to ascertain the economic significance of exercising the purchase option.
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?	In principle, I concur with the Boards that the effect of any option to extend or terminate a lease should be duly factored into the measurement of the lease term. This would result in a more faithful representation of the lease transaction in both the lessee's and lessor's books as compared to the simplistic alternative of assuming the minimum, non-cancellable lease term. However, I find the wording of the Boards' proposed lease term definition - "the longest possible term that is more likely than not to occur" (paragraph B16 in the ED) – conceptually problematic. In particular, I do not quite agree with the application of this definition in the illustration in paragraph B17 in the ED. In that

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	illustration, the ED concluded that the lease term was 15 years, because: "…there is a 60 per cent chance that the term will be 15 years or longer, but only a 30 per cent chance that the term will be 20 years. *Therefore there is a 60 per cent chance that the term will be 15 years, which is the longest possible term more likely than not to occur*." [emphasis added] Firstly, while it is statistically valid to say that there is a 60 per cent chance that the term will be "15 years or longer" but only a 30 per cent chance that the term will be 20 years, I do not think it is statistically correct to say that "…there is a 60 per cent chance that the term will be 15 years, which is the longest possible term more likely than not to occur". This is because the estimated probability distribution of the lease term clearly indicates that the probability of a 15-year term was 30 per cent. Secondly and more importantly, I do not agree with the line of argument that because there is a 60 per cent probability that the lease term will be 15 years or longer vis-à-vis a 30 per cent probability that it will be 20 years, it follows that 15 years is the longest possible term more likely than not to occur. According to the probability distribution estimated by the entity, there is merely a 30 per cent chance that the lease term will be 15 years. If "more likely than not to occur" implies a probability of at least 50 per cent, then it does not seem valid to conclude that 15 years is the longest possible term more likely than not to occur. In fact, none of the three possible lease

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	terms is "more likely than not to occur" because the estimated probability of occurrence in each case is below 50 per cent. In this scenario, it is perhaps more sensible to use 10 years as the lease term, since this is the "baseline" lease term that is non-cancellable. It appears to me that there are inherent conceptual and practical problems with the Boards' proposed lease term definition and application. I therefore urge the Boards to revisit the proposed lease term definition with a view to providing more clarity on the intended meaning.
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 measured reliably? Why or why not?	I have no issues with the Boards' proposal that residual guarantees that are specified in the lease contract should be factored into the measurement of lease assets and liabilities. This is very much similar to the requirement under the existing IAS 17. In my view, it is clear that residual guarantees give rise to financial liabilities and assets at the inception of the lease contract. However, I do not agree with the Boards' conclusion that there automatically exists a financial liability to pay contingent rentals and a financial asset representing a right to receive contingent rental payments at the inception of a lease contract containing such clauses. The specific facts and circumstances surrounding the lease contract must be considered to ascertain the existence of a lessee's financial liability and a lessor's financial asset relating to contingent rental arrangements. For instance, if the rental payments are contingent upon future realised sales or units of output produced, I do not think

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	there is an unconditional obligation on the part of the lessee to pay contingent rentals at the inception of the lease contract. As the triggering contingent events are in the future, the lessee could avoid paying the rentals by selling or producing only up to the stipulated threshold above which it is obligated to pay contingent rentals. The same would also apply in the case of expected payments under term option penalties. In my view, presuming that an unconditional financial obligation to pay contingent rentals and term option penalties exists at the lease's inception - regardless of the specific facts and circumstances - is inconsistent with the principle-based approach that the Boards are championing. I urge the Boards to revise the proposal to permit entities to consider the specific facts and circumstances on a lease-by-lease basis, and to factor the estimated contingent rental and term option penalty amounts into the measurement of the lease liability and asset only when it is determined that the liability and asset exist at the inception of the lease concerned. The revised provision could perhaps assume the form of a rebuttable presumption that unless specific facts and circumstances indicate otherwise, the effect of contingent rentals and expected payments under term option penalties should generally be included in measuring lease liabilities and assets. In terms of the measurement basis, I concur with the Boards' proposal to require an expected outcome technique. I note that this is very much in line with the measurement approach for dealing with prospective cash flow uncertainties that is being proposed under the IAS 37 revamp project. Nonetheless, on the practical front, an

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	expected outcome approach may impose significant costs for many entities who are heavily involved in lease arrangements. Subject to the determination that there exists a financial asset to receive contingent rentals and term option penalty payments at the onset of the lease, I agree that lessors should include contingent rentals, expected term option penalty payments and residual value guarantees in the measurement of the right to receive lease payments only when these components are capable of reliable measurement. This is consistent with the fundamental recognition criteria for financial statement elements as reflected in paragraph 83(b) of the IASB's *Framework for the Preparation and Presentation of Financial Statements.*
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?	Generally, I share the Boards' view that periodic evaluation of the initial lease asset or liability estimates for changes in facts or circumstances and remeasurement of those estimates in the event that significant changes have transpired, would provide financial statement users with more economically decision-useful information (vide paragraph BC134 in the Basis for Conclusions). I also note that the Boards have sought to address preparers' concerns that reassessment of lease terms could be costly for those entities with many leases by requiring detailed reassessment only when there are indications of a significant change in the lease asset or liability (see paragraph BC133). Notwithstanding this, I think lessees – especially those with large lease portfolios spanning multiple international

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	locations – could find complying with the requirement in paragraph 18 of the ED to be both costly and challenging. Allocating changes in contingent rentals, term option penalties and residual value guarantees to current or prior periods and future periods may not be as straightforward in practice as it may seem in theory. Significant changes to accounting systems may be necessary to enable lessees to determine such allocations reliably. I advise the Boards to reconsider the cost/benefit balance of the proposed requirement in paragraph 18 of the ED.
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?	I support and applaud the Boards' proposed classification conditions for sale and leaseback transactions. I think the proposed criteria are conceptually more robust than the corresponding requirements in IAS 17. This should contribute towards resolving the "off-balance sheet financing" issues that many financial statement users face when estimating the extent of financial leverage and earnings of entities that actively engage in such arrangements. In particular, the proposed condition that the "transfer" portion of the transaction must meet the conditions of a sale of the underlying asset would mean that many current "sale and operating leaseback" transactions – a prevalent form of "off-balance sheet financing" at present – would have to be reclassified as a financing arrangement per paragraph 67(b) of the ED. The overall impact would be more faithful and fairer reporting of such arrangements in the financial

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	statements, coupled with less opportunity for abuse. Many sale and leaseback transactions will appear on transferors/lessees' books as "on-balance sheet financing", because I expect many of such arrangements to fail the "sale-of-underlying-asset" test.
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 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? (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	I would not comment on Questions 12 – 14, because I do not think that this is an appropriate juncture for the Boards to be seeking constituents' views on the presentation of lease assets and liabilities. Although these questions are relevant to the subject matter and scope of this ED, my view is that they are conceptually related to the fundamental presentation issues that are presently being deliberated under the Boards' joint Financial Statement Presentation project. As I have mentioned in previous comment letters and reiterated in my covering letter, the Boards should "put the horse before the cart" and resolve issues at the conceptual level first before working on the specific details at the individual standard level. As I see it, such a logical approach affords the best assurance that the fundamental principles are consistently and coherently promulgated within the IFRS as an authoritative body of accounting standards. I strongly object to the Boards' proposed approach to revisit the presentation issues in this ED at a later date when the proposals of the Financial Statement Presentation project are available (vide paragraph BC142 in the Basis for Conclusions). There should be closer coordination among the various project teams to facilitate the Boards' deliberation of "cross-cutting" conceptual issues. The "project silo" approach that the Boards are taking heightens the risks

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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?	of the IFRS developing along disconnected and inconsistent paths. Taking "short-cuts" for the sake of meeting unrealistic project timelines could do more harm than good in the long run. I therefore urge the Boards to re-deliberate the subject matter of Questions 12 – 14 in conjunction with the proposals made under the joint Financial Statement Presentation project, before re-exposing them for constituents' comments.
Question 13: 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?	
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?	

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Question 15 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?	I have no issues with the broad disclosure objectives proposed by the Boards in paragraph 70 of the ED. I observe that this is consistent with the disclosure approach that the Boards have taken in recent projects, particularly ED/2010/6 *Revenue from Contracts with Customers*. In the latter ED, the Boards had set out similar disclosure objectives in paragraph 69. I welcome such a move. In my view, what is perhaps more significant is that this marks a paradigm shift towards "principle-based disclosure requirements" (see paragraph BC171 of the Basis for Conclusion to ED/2010/6). I hope to see the same disclosure approach being consistently adopted in future projects. In fact, as mentioned in my comment letter to ED/2010/6 dated 16 August 2010, I strongly urge the Boards to consider adopting a more holistic approach to principle-based disclosures through the development of a Disclosure Framework. The present absence of a Disclosure Framework has resulted in the IFRS disclosure requirements being developed on a standard-by-standard basis, without reference to a unifying set of principles espousing disclosure objectives and the extent to which disclosures should support the numbers reported in the financial statements. Going forward, I hope to see the Boards adding a project to develop a Disclosure Framework for Financial Reporting in their future technical agenda. In terms of the specific disclosure provisions proposed, I do not agree with paragraphs 85 – 86 in the ED. These paragraphs propose to

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	deviate from the IFRS 7 maturity analysis provisions and require lessees and lessors to disclose maturity analyses of liabilities to make lease payments and rights to receive lease payments annually for the first five years, followed by total amounts attributable to the remaining lease period. I do not see the need to prescribe specific time-bands for the maturity analyses. I think this is inconsistent with a principle-based disclosure approach. In my view, the existing IFRS 7 requirements that permit preparers to exercise judgement in determining the appropriate time-bands for a liquidity risk maturity analysis of financial liabilities is more aligned with a principle-based disclosure approach and should be consistently applied to lease maturity analysis disclosures as well.
Question 16 (a) The 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?	(a) On practical grounds, I support the Boards' proposed simplified retrospective approach for the transitional period. A full retrospective application of the proposed lease accounting requirements in accordance with IAS 8 would ideally provide the most faithful representation of an entity's financial position relating to its lease portfolio. However, the new lease accounting model that the Boards are proposing in this ED is significantly different from IAS 17. I think the majority of entities would find it extremely costly and challenging to gather or "reconstruct" the requisite information to operationalise the new requirements under a full retrospective approach. This is especially so for those entities with many lease arrangements

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	that are presently accounted for as operating leases under IAS 17. (b) I have no issues with the Boards permitting full retrospective application of the proposed lease accounting requirements, given that this is consistent with the intent and spirit of IAS 8. However, I would think that this transitional option would not be well received in practice, because of the steep accounting costs and challenges that it entails for many entities [as explained in my response to part (a)]. (c) I think the Boards would also need to address transitional issues in the following two additional areas: • Those existing arrangements that are presently reported as leases under IAS 17 but will be considered as purchases or sales of the underlying assets under the proposed lease accounting model; and • Those existing sale and leaseback transactions that are presently reported as such under IAS 17 but will not necessarily meet the proposed classification criteria for sale and leaseback under the new lease accounting model.

Question	**Comments**
	I note that the ED is silent on the abovementioned areas, and it is unclear whether the Boards require full retrospective application of the new lease accounting requirements for such circumstances. I urge the Boards to provide further clarifications with respect to the transitional provisions for these areas.
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?	With respect to the benefit side of the cost/benefit equation, I tend to agree with the Boards that the proposed lease accounting model for lessees significantly improves financial reporting in an area that has long been problematic for many financial statement users due to "off-balance sheet financing" issues and abuses. In particular, I think the headline proposal to abolish the distinction between finance and operating leases is a step in the right direction. This should contribute towards more relevant and decision-useful information for investors and other financial statement users. However, I have some reservations on the merits of the proposed lease accounting model for lessors. I urge the Boards to reconsider the proposed approach for lessors in light of the points that I have raised in my comments to Question 2. On the cost side of the equation, I note that the Boards have sought to reduce the costs of implementing and transitioning to the new lease

Question	Comments
	accounting requirements by providing more simplified accounting requirements for short-term leases, requiring detailed reassessment of the lease term only when there are indications of a significant change in the lease asset or liability as well as providing a simplified retrospective approach for the transitional period. Nonetheless, for many lessees and lessors, the proposed lease accounting model will be significantly more demanding than IAS 17 in terms of the gathering, maintenance and tracking of lease data and information to support the accounting requirements. This is especially the case for those who are presently reporting under the operating lease model in IAS 17. It is thus likely that significant investments would have to be made to either refine or develop IT financial reporting systems to cater to the more rigorous lease accounting requirements. Even more significant, in my view, will be the “boundary spanning” impact of the proposed lease accounting model. I foresee financial statement effects that extend beyond accounting, perhaps warranting senior management’s action. Financial statement ratios are likely to see dramatic changes. For lessees currently accounting for such arrangements as operating leases under IAS 17, several key leverage and interest coverage ratios may probably deteriorate even though there have been no changes in the business. Greater volatility in these ratios is also expected, in view of the proposed requirements to reassess the lease liability measurement assumptions. Of concern is that the deterioration of key financial statement ratios may affect lessees’ loan covenants and financing arrangements. There may thus

Question	Comments
	be a need for affected lessees to renegotiate the relevant terms in their loan covenants and financing agreements with their financiers. In view of the potentially pervasive change management impact of the proposed lease accounting requirements, I strongly urge the Boards to consider allowing a longer lead time from the issuance of the new Leases IFRS to its effective date. The Boards should seek the views of the global preparer community before determining an appropriate transitional timeline. If the Boards are able to do so, I think the costs of implementing the new Leases IFRS would be better managed and the transitional process would be less disruptive for many entities.
Question 18 Do you have any other comments on the proposals?	Please refer to my overall comments on this ED in the covering letter.