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Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

File Reference No. 1850-100

Dear Sir/Madam,

United Technologies Corporation (UTC) welcomes the opportunity to share its views on the proposed Accounting Standards Update “Leases” (Topic 840). UTC is a $60+ billion global provider of high technology products and services to the building systems and aerospace industries, operating in nearly 190 countries around the world.

We support the Boards’ efforts to converge the accounting standards and develop an enhanced approach to lease accounting. Although the proposed model contains significant changes, we commend the Boards for working together on this project and attempting to provide users of financial statements with a more comprehensive representation of leasing transactions.

While we understand and agree with the conceptual changes that would ensure that all the rights and obligations arising under leases are recognized in the statement of financial position, we are concerned with the implementation and practical application of this proposal.

We believe that the proposed definition of a lease is clear and appropriate. However, the exposure draft does not provide sufficient guidance for distinguishing leases from service contracts. Although the proposal includes some guidance for determining whether a contract should be treated as a lease on the basis of the contract substance, it is not apparent when a contract should be considered a service contract rather than a lease. It is not uncommon for companies such as UTC to outsource the administration, service and supply of large quantities of assets including computer equipment, office equipment and vehicles. We believe that this area is extremely challenging and could lead to potential misinterpretations. In order to ensure the consistency of accounting, we encourage the Boards to establish specific guidance for these types of contracts and to provide certain criteria for distinguishing a lease from a service and supply contract.

Overall, we support the proposal to determine the term of the lease as the longest possible term that is more than likely than not to occur. We believe that this approach would lead to the most accurate results and would truly represent the entity’s expectations. Conversely, the example described in the application guidance is based on the highest probability of occurrence approach, which is unlikely to correspond to the longest possible term. We believe there is a fundamental difference between a likelihood and cumulative probability of occurrence. Thus, we suggest the Boards review and clarify the proposed guidance and application guidance examples in order to avoid inconsistent application of the proposed methodology. Further, we agree that an estimate of contingent rentals payable, an estimate of amounts payable under residual value guarantees and an estimate of expected payments under term option penalties meet the definition of a liability and should be included in determination of the present value of the lease payments. However, the proposed expected-outcome technique, including probability-weighted average calculation of the lease payments, is a rather complex approach with no adequate guidance. We
recommend that if the Boards chose to retain this concept, then the exposure draft should be expanded and considerable guidance should be developed, including detailed application examples.

In general, we support the proposed dual model approach for lessor accounting. We agree that the lessor should utilize the performance obligation approach or derecognition approach depending on a lease's exposure to significant risks or benefits associated with the underlying asset during or after the expected lease term. However, we do not believe that the proposed guidance on assessing whether the lessor retains exposure to significant risks or benefits associated with the underlying asset is sufficient. While the proposal identifies certain factors that lessor should assess during, or after the expected lease term, it is not clear how to apply this guidance and how to make a determination that the lessor retains or relinquishes the exposure to significant risks or benefits associated with the underlying asset. We recommend that the exposure draft be clarified and expanded to incorporate additional guidance and examples on this matter.

We are extremely concerned by the proposed requirement to recognize and measure all outstanding leases as of the date of initial application. This approach suggests accounting for all the leases in existence as of the beginning of the first comparative period presented and reinstating all of the leases that expired prior to the adoption date but existed during the periods presented. We believe that for a company like UTC, this approach would require dual reporting during those periods, the costs of which would be far more excessive than the benefits provided by the information. We strongly believe that the suggested approach will create a significant unwarranted administrative burden on preparers. We think that the requirements of the exposure draft could be simplified by applying them to all outstanding leases as of the adoption date rather than as of the date of the initial application. This approach would still allow comparability for the leases that are currently in effect but would not result in significant deviation from the actual financial results.

As noted above, in general we agree with proposed exposure draft. However, we believe that the Boards' assessment of the practical application of certain issues noted above is not completely accurate and could result in significant complexity, inconsistency of accounting and non-value added costs associated with the administration of thousands of leases (in the case of UTC) every reporting period.

We thank the Board for its consideration and would be happy to discuss our views in more detail with the Board members or the FASB staff.

Sincerely,

/s/ John Siantial
Interim Vice President, Controller
United Technologies Corporation

/s/ Maria Romanovska
Specialist, Financial Reporting
United Technologies Corporation
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?

We agree with proposed principles for lessees, including a right-of-use asset and a liability to make lease payments as well as amortization of the right-of-use asset and interest on the liability to make lease payments.

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 that a lessor should apply 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 apply the derecognition approach otherwise. However, as noted above, we think that proposed guidance on assessing whether the lessor retains exposure to significant risks or benefits associated with the underlying asset should be expanded further. The proposal identifies certain factors that a lessor should assess during or after the expected lease term, such as significant contingent rentals, options to extend or terminate the lease, material non-distinct services under the lease, etc. However, it provides very little guidance on how an existence of one or more indicators would influence the decision making process and provide a basis for conclusion. We suggest incorporating additional guidance and examples on how each of the factors would add or reduce the lessor's exposure to significant risks or benefits associated with the underlying asset. Further, we support the Boards' proposals for the recognition of assets, liabilities, income and expenses for the performance obligation and derecognition approaches to lessor accounting. We also agree that there should be no separate approach for lessors with leveraged leases.

Question 3: Short-term leases
(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, or 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 support the simplified requirements proposed for short-term leases for lessees and lessors. Given the short duration of these leases, it appears reasonable to disregard the time value of money for these leases and recognize undiscounted amounts for lessees and omit recognition of assets and liabilities for lessors.

**Question 4: Definition of a lease**

(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 a lease is appropriately defined 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. We also agree with the proposed guidance on distinguishing between a lease and a contract that represents a purchase or a sale, and the proposed factors for determining whether a contract transfers control of the underlying asset at the end of the contract. However, as noted above, we think that additional guidance should be provided for determining whether a contract is a lease or a service and supply agreement. It is not obvious whether an agreement with an outside service provider for a service of a fleet of assets contains an implicitly specified asset and whether the right to control the use of that asset was conveyed. We believe that specific guidance on this issue could benefit financial statement users and help ensure consistency of reporting.

**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 scope in this guidance.

**Question 6: Contracts that contain service components and lease components**

(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 agree with the Boards’ proposal to account separately for distinct service components in a contract that contains both service and lease components. We support the decision to apply the lease accounting requirements to the combined contracts.
Question 7: Purchase options
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 agree that a lessee or a lessor should account for purchase options only when the purchase options are exercised.

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 support the proposal to 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. We agree that the lease term should reflect the term that has the highest likelihood of occurrence and reflects the entity’s expectations. However, we do not support the cumulative probability approach described in the application guidance appendix. The probability is a statistical measure that may result in an outcome that significantly differs from the entity’s expectations. Thus, we encourage the Boards to address this issue and eliminate any conflicting guidance.

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 that contingent rentals, 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. We support the proposed expected outcome approach, including identification of a number of reasonably possible outcomes and approximation of present value and probability of those outcomes. However, we foresee some complexity surrounding the contingent rentals approximation and expected outcome technique application. Thus, we believe that the proposal should be modified to incorporate specific guidance and examples for this approach to prevent any misinterpretation and ensure accurate calculations.

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?

We support the proposed approach and agree that lessees and lessors should remeasure assets and liabilities arising under a lease on the basis of new facts or circumstances that indicate that there would be a significant change in the liability to make lease payments or in the right to receive lease payments. This approach appears reasonable and eliminates the burden of reviewing thousands of leases every reporting period. However, we are somewhat concerned by the requirement to reassess contingent payments every reporting period and recognize the changes that relate to current or prior periods in net income. In order to determine if changes are significant and would result in adjustments to the current or
prior periods, we would have to potentially evaluate and review hundreds of leases every reporting period. Thus, we encourage the Boards to reconsider this proposal and require the reassessment only on the basis of new facts and circumstances, or only on an annual basis.

**Question 11: Sale and leaseback**
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 agree with the criteria for classification as a sale and leaseback transaction.

**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, totaling 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?

Overall, we support the proposed financial statement presentation for a lessee and lessor. We agree that lease assets and liabilities are different in nature from other financial assets and liabilities and, if significant, should be presented separately. However, for a company that utilizes each of the approaches described above, reporting each asset and liability separately may result in overly extensive financial statements. Thus, we believe that preparers should have an option of presenting these details in the accompanying notes to financial statements.

**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?

See #12 above.

**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 support the proposed financial statements presentation for a lessee and lessor.
Question 15: Disclosure
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?

Overall, we support the proposed disclosure requirements for a lessee and lessor. However, we are slightly concerned by the level of details required for qualitative and quantitative disclosures. We agree that an entity shall disclose information that would be useful to financial statement users. We also support the approach of aggregating or disaggregating information based on the management judgment and usefulness of the information. However, some of the requirements (e.g. reconciliation of the opening and closing balances, amounts recognized for short-term leases, maturity analysis, etc.) are extremely specific and allow no opportunity for management judgment and evaluation of the usefulness of the information.

Question 16: Transition
(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?

While we support the simplified retrospective approach and agree that the cost of the full retrospective approach would far outweigh the benefits of the information provided, we believe that recognition of all outstanding leases as of the date of initial application could be also expensive and complicated. As noted above, for a large company with thousands of leases, this approach would necessitate dual reporting requirements during the periods presented, which would create a significant administrative burden for the companies. Furthermore, it is unclear how short term leases, lease terms, and contingent payments would be estimated during prior periods as the facts and circumstances are changing and may vary considerably from the initial conditions. We suggest that the Boards consider simplifying this proposal by requiring recognition of all outstanding leases as of the adoption date rather than as of the date of the initial application. This approach would provide comparable information for the leases in existence at the date of adoption but would eliminate the cost of dual financial reporting for earlier periods.

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?

As noted above, in general we agree with the proposed exposure draft. However, we believe that the Boards’ assessment of costs and benefits associated with proposed requirements are not entirely accurate and could still result in excessive implementation costs for the companies involved.

Question 18: Other comments
Do you have any other comments on the proposals?

We believe that the Boards should also address the U.S. government cost accounting issues and applicable IRS regulations. A portion of the interest expense, as oppose to rent expense, would be unallowed and not reimbursed under U.S. government cost accounting rules. Thus, the new lease
accounting model could create a real economic impact for U.S. government contractors. Further, the discontinuance of operating lease treatment may not be permissible when determining U.S. federal taxable income which would require companies to maintain two sets of records for each lease adding considerably to the administrative burden.

**Question 19 Non-public entities**
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?

No, the final guidance should apply to public and nonpublic entities.