director@fasb.org

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

Dear Sir:

We appreciate the opportunity to provide our comments regarding the Exposure Draft – Proposed Accounting Standards Update – Topic 840, Leases, issued on August 17, 2010.

We would like the FASB and IASB to know that Pitney Bowes recognizes the difficulty of the undertaking and appreciates the significant effort that went into developing the proposed accounting standards update. We do however ask the FASB and IASB to consider our responses to certain of the “Questions for Correspondents” as enumerated in exposure draft pages 4 through 11.

*Question 1: lessees*

(a) Do you agree that a lessee should recognize a right-of-use asset and a liability to make payments? Why or why not? If not, what alternative would you use 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 would you propose and why?

One of the primary drivers to revise the accounting rules for operating leases is the absence of presentation of leased assets and lease obligations on the balance sheet of lessees. The proposed recording of an asset and an obligation to make payments corrects this deficiency. We therefore support this proposed change.

While we agree that lessees should record an asset and liability and recognize amortization of the right-of-use asset, we request that the boards' consider allowing utilization of an alternative methodology such as the straight line method, with
appropriate footnote disclosures, which would be consistent with a principles based approach.

Question 2: lessors –  
2a. 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 leased term and (ii) the derecognition approach otherwise? Why or why not? If not, what alternative approach would you propose and why?

(i) We disagree with the concept of recording a performance obligation. Recording an obligation implies that a future liability to either perform a service or financially compensate the lessee, exists. As a manufacturer and lessor of office equipment we believe that we have completed our performance obligation upon delivery of the asset to the lessee. Once delivered, we have surrendered our control of the asset to the lessee.

(ii) We agree conceptually with derecognition of the asset because placing the asset with a lessee for a period of time for their use is clearly indicative that a sale (of the entire asset or a portion thereof) has occurred. We disagree with the proposed methodology for determining the residual amount as it is a “forced” result of a mathematical calculation. This ignores the fact that a residual is the expected value of the equipment at termination and, as such, is a cash flow to be considered in the overall financial return on the lease. Using a “forced” number for the residual asset creates an accounting result that may not be representative of the true economic value of the asset under lease and would likely require adjustment at the end of the lease term. This will increase volatility through revenue adjustments at lease termination, which could be misleading to readers of the financial statements.

We respectfully believe that the current rules for lessor accounting are more representative of the economics of a lease transaction. We previously noted that one of the primary drivers to revise lease accounting was the absence of assets and liabilities on the books of lessees utilizing operating leases. Lessors however, record assets and related debt for both capital and operating leases under current guidance and lessor accounting is widely understood by readers of the financial statements. In addition, certain lessors, with related manufacturing and sales channels, record sales-type leases whereby the fair value of the asset under lease is presumed “sold” for accounting purposes, and subsequently financed, correctly depicting the economics of the asset placement and financing. A manufacturer or sales entity should be entitled to record a sale to recognize the placement of equipment. If the manufacturer or sales entity chooses to finance the equipment in an effort to facilitate the sale, they have agreed to finance the asset today in exchange for a financial return over time.

There are two components of a transaction whereby equipment is placed with a customer under a sales-type lease:
- **Recording a sale** - Recognizing a sale at fair value, at the point equipment is placed with the lessee, properly reflects the economic transaction for placement of the asset with the user, at the correct amount, and in the proper period.

- **Financing** - Recording the lease stream inclusive of the residual value (expected fair value of the asset at termination) is a correct depiction of the economics of the financing of an asset. The financing revenue is equal to the lessee rent payments over the term, plus the expected cash flow from the disposition of the residual at termination, less the fair value of the asset recognized as sale revenue at inception. Recognizing this income stream under the interest method, gives proper effect to the amount and timing of interest revenue to be recognized.

2b. Do you agree with the board's proposals for 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?

Recording a performance obligation appears to be in conflict with the concept of having a lessee record a right-of-use asset. If the lessee has an asset by virtue of taking a piece of equipment in return for agreeing to make payments to the lessor, it would be an indicator that the lessor has sold something. The lessor has completed its performance obligation to the lessee upon delivery of the asset under lease.

As we previously stated, it is our opinion that current accounting guidance for lessors is more appropriate than what has been proposed by the boards’ in the exposure draft. One of the primary drivers to revise the lease accounting rules was the absence of assets and liabilities on the books of lessees. We generally agree with the boards’ proposal to capitalize the right-of-use assets and the liability to make payments on the books of the lessee. By making this revision, the boards’ have corrected that deficiency and eliminated inconsistent accounting presentations for similar transactions. We disagree that it was also necessary to revise lessor accounting guidance. We do not believe that the proposed changes to lessor accounting provide an improvement from current standards as the current accounting guidance for lessors more closely follows the economics of the transaction and is widely understood. We do not believe there would be a benefit to readers of the financial statements by converting to the proposed guidance that would justify the complex and costly effort to modify systems and perform related evaluations.

Under current guidance, if the characteristics of the financing provided by the lessor to the lessee bears similarity to the financing arrangement a lessee would obtain if they purchased and financed the asset, then some lessors would record both a sale at inception and financing revenue on the “loan” aspect of the transaction. If the transaction more closely resembles an arrangement to finance the use of an asset for less than a substantial portion of its cost or economic life the lessor would record the financing as a rental, depreciating the asset and recognizing rental revenue straight line over the lease/rental term. We believe this guidance more closely represents the economics of the transactions than the methodology proposed by the boards’.
2c. 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). Why or why not? What approach should be applied to these leases and why?

The exposure draft indicates that the board decided to eliminate the current distinction for leveraged leases because:

- The cash inflows from the tax attributes of a leased asset are the same to the lessor whether the asset is financed with recourse or non-recourse debt and,
- A difference in financing should not affect the pattern of income recognition or influence how the lessor presents in the statement of financial position its positions in the separate transactions, the borrowing from the lender, and the lease with the lessee.

We respectively disagree with the board’s view regarding leveraged leases because:

- The current guidance whereby an investment in a leveraged lease is recorded net of non-recourse debt as an asset on the balance sheet is the appropriate presentation because it reflects the true underlying risk in the transaction. In the event of default under a non-recourse debt arrangement, the lender can recover their investment only through the cash flows and equipment under lease. The lessor has no risk beyond their equity in the lease therefore it would be inappropriate for a lessor to show a non-recourse debt obligation it is not legally obligated to pay. Presenting the leased asset and debt “grossed up” on the balance sheet misleads the reader who would presume there is a greater debt obligation on the books of the lessor than actually exists. It misrepresents the legal and economic liabilities of the lessor.
- The income recognition pattern of a leveraged lease is based on an after-tax constant rate of return to the lessor. This concept considers all components of the net cash flows to the lessee (lessee rents net of debt payments assigned to the lender, and related tax effects). The income pattern is a more accurate depiction of the transaction to the lessor based on their net investment and maximum financial risk in the transaction.
- We would also observe that entities with leveraged leases have recognized revenue for their leveraged lease portfolios using the current methodology prescribed by existing lease accounting guidance. Modifying the current revenue recognition pattern and recording an adjustment mid-stream on significantly large transactions with long lease terms could be both confusing and misleading.

We are therefore recommending that leveraged lease accounting remain as is, or at a minimum, grandfathered for existing leveraged leases so as to not confuse readers of financial statements and eliminate one significant burden related to the implementation of the new lease accounting guidance.
**Question 5 - Scope exclusions:** This exposure draft proposes that a lessee or 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 would you propose and why?

The boards’ stated objective in issuing the new guidance is to establish “principles that lessees and lessors shall apply to report relevant and representationally faithful information to users of financial statements about the amounts, timing and uncertainty of the cash flows arising from leases.”

In doing so, the boards have limited scope exclusions to those leases as defined in question 5 above and short term leases (12 months or less) as stated in paragraphs 64 and 65 of the exposure draft.

We believe that the scope limitations should be extended to “non-core” leases and/or leases that have a low dollar value. The reporting of “non-core” or low value leases does not provide readers of financial statements with more relevant information, yet the effort to report such leases under the new guidance is just as costly and complex as reporting large value, core leases, that comprise the bulk of the lease exposure of an entity. While recognizing that a scope exemption for low value, “non core” leases, would require additional guidance to determine which leases meet this criteria, such an exemption would be consistent with the boards’ stated objective and would ease the cost of compliance with, and transition to, the new guidance.

**Question 6. Contracts that contain service components and lease components:** This exposure draft proposes that lessees and lessors should apply the guidance in proposed Accounting Standards Update, Revenue Recognition (Topic 605): 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 BC45 – BC 54. If the service component in a contract that contains service components and lease components is not distinct:

(a.) The FASB proposes the lessees and lessor should apply the lease accounting requirements to the combined contract.
(b.) The IASB proposes that:
   a. A lessee should apply the lease accounting requirements to the combined contract.
   b. A lessor that applies the performance obligation approach should apply the lease accounting requirements to the combined contract.
   c. 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 components 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 recommend recognizing revenue (lessor) or expense (lessee) related to service components embedded within an offering that includes a lease to be recognized straight line over the service period.

We also ask the boards’ to consider guidance relative to service arrangements that include the placement of equipment to perform the service. Although an embedded lease is implied by the placement of equipment at the customer’s place of business, the customer has signed up for a “turnkey” service agreement. The equipment is required to perform the service but is operated by the service provider. The customer views the agreement as a service, not as a means of equipment acquisition. We recommend that the boards’ consider exempting such equipment placements from the proposed lease accounting guidance in situations where the customer has no continuing interest in the equipment beyond the service period. An exemption of this nature would be more representative of the economics and intent of the agreement that the customer committed to.

Question 8, Lease Term: “Do you agree that a lessee or 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 lessor or lessee should determine the lease term and why?”

We recognize that the boards’ are attempting to present the full potential liability for which an enterprise is ultimately committing itself by including presumed renewal periods in the lease term. We disagree, however, with this approach because we believe it does not achieve its desired goal and instead encumbers an entity with liabilities for which there is no legal obligation or commitment and may likely require adjustment in future periods. Similar to today, we recommend determining the lessee’s liabilities under the lease by using the minimum payments and term for which the lessee is legally obligated. This will align the recorded liability with contractual obligations. Giving consideration to financial events that have not yet occurred either legally or economically may be misleading and does not represent the true economics of the lease commitment. Lessors have the potential to recognize revenue and lessees to recognize expense in current periods that will subsequently require adjustment in future periods if such options are not exercised as initially determined. We believe that this allows for greater volatility, the potential for numerous adjustments and potentially inconsistent or misleading results within different periods.
We also request additional guidance in applying the concept of renewal options in determining lease terms. In reading the exposure draft, we concluded that the proposed guidance relative to renewal terms and options is not referring to end-of-term activities, some which may be the result of a separate sales process or situations in which the lessee continues to use the equipment beyond the originally scheduled termination date. Many equipment lease contracts contain provisions that upon completion of the original term, the lease converts to a month-to-month renewal until the equipment is returned to the lessor. Many companies have a history of negotiating a new lease with a customer prior to the scheduled end of the original term, or negotiating a fixed term renewal at or near the end of term. We are assuming that the historical propensity of customers to either convert to month-to-month leases, enter into a new lease, or to renew for a fixed term, should not be considered in determining the lease term because:

- These activities can require significant sales involvement to complete.
- Application of such history to determine lease term would only be possible by applying portfolio averages. This requires a significant level of judgment that makes the accounting subjective and less representative of the legal obligations of both lessor and lessee. This also creates a significant and complex administrative burden even if the estimates are implemented at a portfolio or sub-portfolio level. Increasing each lease term by an average will result in an inaccurate depiction of any single lease and could increase financial risk and volatility should market conditions change to make it more advantageous for lessees to terminate at their originally scheduled lease termination date.
- Capitalizing lease renewal terms could result in capitalizing significantly more than the fair value of the asset under lease by capitalizing something the lessee has not legally committed to. We feel this is contrary to the goal of the revised lease accounting rules by which each lessee should capitalize their right-to-use the asset because inclusion of a renewal term that a lessee is not legally obligated to elect would require lessees to capitalize a right-of-use that does not yet exist. This process overly complicates the accounting process. Inclusion of obligations for which there is no current legal commitment will result in a “timing anomaly” as expense is recognized early in the lease term for a potential renewal to occur in the future. The renewal may never, in fact, occur because there is no legal obligation for the lessee to do so. Over encumbering the lease transaction puts leasing at a financial disadvantage.

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 lessor or lessee should account for contingent rentals and expected payments under term option penalties and residual 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 believe that lessees and lessors should recognize term option penalties and contingent rents as they occur:
- To reflect revenue and expense in the period of benefit and
- To be certain that the contingency will in fact occur and
- The “front loading” of revenue and expense under the proposed rules amplifies and compounds the recording of events not yet established in fact.

Capitalizing contingent rents and penalties at inception makes the accounting subjective as it is an attempt to predict future events. Lessees could be recognizing expenses that may never occur and lessors could be recognizing revenue that will subsequently be reversed, misleading the reader of the financial statements. Contingent rents and termination penalties based on usage are often inserted in leases to protect the lessor from residual risk that the asset will be worth less from extensive use and wear. Recognizing the receipt of such cash flows with the disposition of the residual at the time the residual loss is realized therefore makes the most sense to make the accounting resemble the financial implications and match revenue and expense in the period of benefit. The front loading effect of the proposed rules will result in lessors and lessees recognizing such events in the financial statements at times other then when the event giving rise to the revenue or expense occurs.

**Question 10, Reassessment:** "Do you agree that lessors and lessees 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?"

Similar to our responses to questions 8 and 9, we believe that lease terms and lease payments should be recorded using the minimum contractual obligation of the lessee. Constant reassessment can result in inconsistent comparisons between periods with no change in the underlying contractual obligations of a lessee, thus potentially misleading the reader. If the minimum obligation is used as a determinant for lease term, lease payment stream and liability, the requirement to reassess becomes moot. Using the minimum contractual lease term aligns the liability with the legal obligation of the lessee and would also allow for the application of the accounting guidance across a global organization in a well controlled manner.

We also ask that the boards’ reconsider the reassessment requirement from the perspective of cost burden to implement versus the potential benefits to the reader. Pitney Bowes alone has an extremely large portfolio of leases of almost 900,000 separate lease schedules across the globe. Historically, renewal behavior does not vary significantly from period to period when viewed at a portfolio level as such behavior is largely predictable. Although we acknowledge that there can be much activity on a lease by lease basis, the overall financial change as a result of this activity would provide no
meaningful additional information to a reader, but the cost to perform such a reassessment would be prohibitively expensive with undue cost to our shareholders.

**Benefits and costs** - 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?

The boards’ basis for conclusions considerations (BC200 to BC205) included, but were not limited, to:

- A goal of providing more useful information to readers of financial statements that justify the costs of obtaining and reporting such information
- The costs incurred by reporting entities
- The costs of transition for users and preparers of financial statements

We ask that the boards’ reconsider the guidance in terms of cost and/or transition time to implement the new guidance. We feel that there will be unusually significant costs incurred by lessors and lessees to transition to the new guidance and comply with it over time. Some reasons for our concern are:

Complexity of implementation – The change in guidance will require modification to accounting processes for both lessors and lessees.

- From a lessee perspective, under the current proposal all leases would have an amortizing balance component requiring application of the interest method where before only direct financing leases had an interest method requirement.
  - This would require recalculation of all leases to ensure compliance.
  - It would no longer be possible to record straight line rent expense as each rent payment would have an interest and amortization component.
- Lessors and Lessees would need to perform a complex reassessment activity at each reporting date to review assumptions to give effect to renewal options and contingent rents. Pitney Bowes has a portfolio of almost 900,000 separate lease schedules that on a portfolio basis perform in a reasonably predictable manner over time. The costs to implement a reassessment process for this portfolio, in a well controlled environment on a global basis would be exceptionally costly yet, we believe, would not result in more meaningful information to a reader of the financial statements.
  - Accounting systems and/or processes will need modification to calculate and record “catch up” adjustments resulting from assumption changes
  - A process will need to be established and maintained to
    - analyze underlying assumptions
    - calculate whether an adjustment is required, and if so, the amount of the adjustment
    - document and support any and all adjustments or to document that there was no need for adjustment.
- Lessors will need to modify their systems to
  o determine lease classification (performance obligation or derecognition)
  o change sale recognition calculations under the derecognition model.
  o accommodate the performance obligation and revise income and expense
    recognition patterns.
  o lease management/accounting systems will need to accommodate multiple
    concurrent lease terms for any specific lease as the accounting term may differ
    from the contractual term as a result of including renewal options. This will
    be a difficult change as accounting and customer terms were previously linked
    and that conceptual framework is most likely embedded in the underlying
    “architecture” of lease accounting systems.

Costs of Transition - Retrospective application will involve an extremely complex and
costly process to determine the effects on each year presented. This may not be difficult
for organizations with a handful of leases, but will be an enormous undertaking for large
lessees with many assets and facilities under lease and large lessors with many assets in
their portfolio. Pitney Bowes has almost 900,000 individual lease agreements.
Retrospective transition will require the company to recalculate not only the active leases
in the portfolio at the effective date, but also any leases that were in effect during the
periods presented in the financial statements.

In conclusion, we do not believe that the benefits to be derived from converting to the
currently proposed guidance would outweigh the complex and costly effort required to
comply with that guidance.

Again, we appreciate the opportunity to provide our comments, and your time and effort
in considering them.

Sincerely yours,

Steven J. Green