December 15, 2010

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

Re: Proposed Accounting Standards Update – Leases (Topic 840)

Dear Board Members and Staff:

The Pep Boys - Manny, Moe & Jack and subsidiaries ("Pep Boys") appreciate the opportunity to comment on the Proposed Accounting Standard Update, "Leases" (Topic 840). Pep Boys is the only national chain offering automotive service, tires, parts and accessories. Pep Boys operates over 600 stores located in 35 states and Puerto Rico with sales of approximately $2 billion annually.

The Company leases certain property and equipment primarily under operating leases which contain renewal clauses, rent escalation provisions, capital improvements funding and other lease incentives. As of October 30, 2010, the Company had approximately 370 store locations and three warehouses under operating leases. Approximately 100 of these locations were previously owned by the Pep Boys and sold in sale leaseback transactions.

In general, Pep Boys supports the Boards’ goal of establishing a principles-based approach to lease accounting that eliminates many of the bright line tests to determine whether a lease should be classified as an operating or capital lease and support the Boards’ efforts to converge the accounting standards and develop an enhanced approach to lease accounting.

As more fully described in our responses to the Board’s questions noted below, we are concerned that including optional lease renewals that are “more likely than not” and contingent rentals in the measurement of a right-of-use asset and liability will result in reporting liabilities which do not meet the conceptual definition of a liability. In addition, we believe the proposed measurement guidance would result in entities nearly always being required to remeasure right-of-use assets and liabilities.

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 the concept of a right-of-use asset and a liability; however, we are concerned that including optional lease renewals that are “more likely than not” and contingent rentals in the measurement of a right-of-use asset and liability will result in reporting liabilities which do not meet the conceptual definition of a liability. We believe a lessee should recognize a right-of-use asset and a liability based on the non-cancellable term of the lease and for optional renewals that are probable of occurring.

We agree that a lessee should recognize amortization of the right-to-use asset and interest on the liability to make lease payments as this is conceptually consistent with the recognition of assets and liabilities associated with the right-of-use.

**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?

Given our lack of significant lessor transactions, we have no comments on this question.

**Question 3: Short-term leases**

This 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 12 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 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, nor 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 agree with the simplified requirements proposed for short-term leases for lessees. It makes sense to ignore the time value of money given the short duration of these leases and recognize undiscounted amounts on the lessee’s balance sheet.

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?

Generally, we agree that the proposed standard defines a lease appropriately and we also agree with the criteria for distinguishing a lease from a contract that represents a purchase or a sale based on the underlying economics of the transaction, specifically the transfer of the risks and benefits of ownership.

We are concerned that the Exposure Draft did not provide sufficient guidance in paragraphs B1-B4 with respect to clarifying the distinction between a lease and a service contract and whether a contract with a service provider contains implicitly defined assets for which the right to control the use of those assets had been conveyed to the lessee. In certain contract situations, it is difficult or impractical for a lessee to determine if the underlying assets are “specified assets” as described in paragraphs B2 and B3. We believe more guidance is necessary in this area for the proper and practical application of the standard.

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 exclusions included in the Exposure Draft, except for the sufficiency of the guidance included in paragraphs B1 through B4, as discussed in our response to question 4.

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 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 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 Board’s proposal to account separately for distinct service components in a contract that contains both service and lease components. We also agree with the proposal to apply lease accounting requirements to the combined contract if the service component is not distinctly identified.

Question 7: Purchase options
This exposure draft proposes that a lease contract should be considered 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?

On a conceptual basis we find it difficult to explain why the measurement of a right-of-use asset and liability would not include the option to purchase the asset, but would include options to extend the term of the lease. An option to purchase offers the lessee at least the same amount of control, if not more, over an asset as an option to extend the term of the lease. Accordingly, both should be reflected in the measurement of the right-of-use asset and liability. In keeping with our view that the right-of-use liability should reflect only the incurred obligations, the purchase option should be reasonably assured in order to be included in the measurement of the right-to-use asset and liability.

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 believe the right-of-use asset and liability should represent an obligation as defined in the Accounting Standards Codification. Accordingly, the lease term should be based upon decisions management has made to commit to future payments or obligations that are probable of being incurred. Once renewal is determined to be probable, the entire renewal option should be incorporated into the determination of the lease term. We believe that the quality and reliability of financial reporting would be negatively impacted by recording assets and liabilities that are merely more likely than not to occur as of the initiation of the lease, given the substantial uncertainty involved in predicting outcomes many years in the future.

**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 believe that contingent rentals, such as those based upon future sales activity, and expected payments under term option penalties should be reflected in the right-of-use asset and liability in the periods in which the underlying economic events that give rise to those payments occur or are probable of occurring. This results in a better matching of revenues with expenses and limits the reported right-of-use liability to an obligation that meets the definition of a liability.

We believe that residual value guarantees should also be reflected in the right-of-use liability to the extent such payments are reasonably assured of occurring.

**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 do not believe the proposal to require reassessment where there has been a “significant change” in each leased asset is feasible. We believe that there is an unnecessary level of judgment involved in determining “significant change.” In addition, the proposed measurement guidance includes optional renewals and contingent rents that are “more likely than not” to occur, which increases the volatility of the measure of the liability to make lease payments and could result in frequent reassessments of each leased asset. We recommend changes to the measurement criteria consistent with our response to questions 8 and 9, which would remove these unreliable measures, as well as reconsidering the “significant change” guidance included in the proposed standard.
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?

We agree with the criteria for classification as a sale and leaseback transaction. In our opinion, the criteria accurately reflect the economic substance of the transaction and accurately report the results in an entity's financial statements.

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?

With respect to lessee presentation, we believe that entities should present right-of-use assets and liabilities separately from other, non-lease related assets and liabilities through enhanced footnote disclosure rather than on the face of the statement of financial position.

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?
We believe that lessees should present lease income and lease expense through enhanced footnote disclosure rather than on the face of the income statement.

**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 agree with the Board's proposal to present cash flows arising from leases separately from other cash flows in the statement of cash flows.

**Question 15**
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?

For lessees with a large amount of disparate lease activity, we believe that the disclosure requirements identified in paragraph 73 and 77 are too detailed to be effectively met without dedicating an inordinate amount of time and effort to the disclosures. In addition, the aggregation of leases with similar characteristics will still result in broad qualitative disclosures that will fall short of the Board’s proposed disclosure goals. We believe that the disclosure requirements should be limited to broad, qualitative, policy related disclosures rather than the details of lease arrangements described in paragraph 73.

**Question 16**
(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?

We agree with the simplified retrospective approach as the best balance of comparability and cost between the full retrospective and full prospective approaches.

**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?
No additional comment.

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

No additional comment.

**Question 19**  
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?

We have no comment with respect to application of the proposed guidance to non-public entities.

We appreciate your consideration of our comments. We are available to discuss any of these comments with you at your convenience.

Sincerely,

Sanjay Sood  
Vice President – Controller and Chief Accounting Officer