December 15, 2010

Financial Accounting Standards Board
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Response to Proposed Accounting Standards Update – Leases (Topic 840)

The Related Companies, L.P. is a real estate developer and owner with over 5,100 units of residential market rate rental properties, 13,400 units of affordable housing, and 8.9 million sq. ft. of commercial properties under lease. We believe that the proposed model for lessors contains several provisions which cannot be reasonably estimated, and therefore is not practical to implement in its current form. We also believe that it has the potential to influence the creation of new leases with shorter terms, which may have unintended implications for the real estate industry and the U.S. economy.

Our responses to the questions in the Exposure Draft follow:

Question

1a. We agree with a lessee’s recognition of a right to use asset and corresponding liability; however, we believe that leases with terms less than 5 years should be excluded. Furthermore, we believe that the lessee’s estimated lease term is subject to arbitrary judgment and few lessees will voluntarily disclose their real intentions, effectively reverting to the shortest contractual term, i.e., the initial lease term. Accounting considerations may cause economic terms of future leases to change, reducing extension options, and creating greater turnover in the commercial real estate market. We believe that the standard should use the same concept of minimum lease term which currently is used for disclosing future noncancellable lease obligations. We believe that any term longer than the minimum creates a liability which may not meet the definition of a liability, since it is not enforceable.

1b. We agree with the lessee’s amortization of a right-to-use asset and amortization of the corresponding liability. However, we believe that the amortization method should be straight-line for both, to avoid recognition of a larger expense in the early years, which we believe does not reflect the economic cost of the use of the property under lease.

2a. We agree that the derecognition approach is appropriate if the significant risks and rewards of ownership are transferred; however, we believe that the threshold for derecognition should be quantified in terms which are similar to the existing FAS 13 criteria for capital leases.
2b. We agree with the lessor accounting model, with the following exceptions: (a) leases with terms under five years should be treated as operating leases (b) other leases not subject to derecognition should apply straight-line amortization for both the asset and liability. However, we believe that receivables for leases in which the underlying asset was derecognized should be amortized using the interest method, since this is equivalent to a sale, with a financing of the receivable; in these cases, the liability should also be amortized using the interest method.

2c. While we do not have leveraged leases, we agree in principle that they should not be treated differently.

3a. We do not agree that lessees should have the option to record assets and liabilities for leases with terms of 12 months or less. We believe that all leases with terms of five years or less should be accounted for as operating leases.

3b. We do not agree that accounting for short term leases should be subject to the lessor’s option; we believe that all leases with terms of five years or less should be accounted for as operating leases.

4a. Yes, we agree with the definition of a lease.

4b. Yes, we agree with the criteria which distinguishes a lease from a sale.

4c. Yes, we agree with the criteria which distinguishes between leases and service contracts.

5. Yes, we agree with the scope limitations for intangibles, oil and gas and similar arrangements.

6. We agree with separating the service components to the extent possible. For example, a real estate lease which includes payments for future common area maintenance expenses and taxes should exclude these components from the lease component, and the lessee should expense them as incurred.

7. We agree that lease accounting should terminate when purchase options are exercised, and that the options should only be recognized at that time.

8. No, we do not believe that a lease term should be determined based on management’s judgment as to the longest possible term that is more likely than not to occur. We believe that this allows for manipulation by management and also may create liabilities which are not enforceable since there is no legal obligation to extend a lease beyond its noncancellable term. We believe that the noncancellable term should be used.
9. No, we do not believe that contingent payments should be included in measuring lease assets and liabilities, because by their nature, they cannot be reasonably estimated. In our real estate business, we cannot predict future operating results of our tenants, since the information on which they are based is often unaudited and not always provided on a timely basis. Furthermore, past results are not always indicative of future contingent payments, particularly in uncertain economic times, with potential changes in competitive conditions. We believe that giving lessors the option to estimate these payments may result in significantly different results under identical conditions, simply based on management’s inclination to estimate high or low or not at all.

10. We do not agree with including contingent payments (see response to 9); however, if they were required to be included, we believe that changes in estimates should be accounted for prospectively.

11. We agree that a sale-leaseback must first meet the criteria for a sale.

12a. While we agree that a lessee should present lease assets and liabilities separate from other assets and liabilities, we believe that a net asset or liability should be presented on the face of the balance sheet; footnote disclosure of gross lease assets and liabilities should be presented, to support the net asset or liability.

12b. We believe that a lessor should present a net lease asset or liability on the face of the balance sheet; footnote disclosure of gross lease assets and liabilities should be disclosed, to support the net asset or liability. Since the physical asset is already shown gross on the balance sheet, we believe that a gross lease presentation on the face of the balance sheet would be confusing, since the asset would be represented twice.

12c. In cases where a leased asset is derecognized, we agree that the receivable should be presented on the face of the balance sheet, separately from other assets; the residual value should be part of PP&E, with disclosure of this component in the footnotes.

12d. We agree that separate disclosure of a sublease is appropriate, but only in the footnotes.

13. We believe that separate disclosure of income and expenses relating to leases on the face of the Income Statement is not necessary, unless deemed material; footnote disclosure is sufficient.

14. We believe that separate disclosure of lease cash flows in the Statement of Cash Flows is not necessary, unless deemed material; footnote disclosure is sufficient.

15. We agree with footnote disclosure of all significant lease terms, assumptions, and contingencies.
16a. We agree that measurement of existing lease assets and liabilities at the date of transition should be based only on remaining lease payments, as a practical matter.

16b. We believe that full retrospective application should not be permitted, since it would reduce comparability among companies.

16c. We do not believe that accounting for existing capital leases should be adjusted for contingent payments.

17. We agree that the benefits of the revised lease accounting (as amended to reflect our comments) are significant to a limited number of financial statement users, despite the costs, because it will enhance comparability with other companies. However, we believe that the great majority of financial statement users, who are interested primarily in the company’s own performance, will not benefit from the changes in accounting, since it will reduce comparability with prior years. We believe that enhanced footnote disclosures alone would suffice.

18. None

19. No, we do not believe that GAAP should be different for non-public companies, since some of these companies may eventually become public, and the use of different GAAP will confuse potential investors and financing sources.

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