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Technical Director – File Reference No. 1850-100
Financial Accounting Standards Board
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International Accounting Standards Board
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London, EC4M 6XH
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Via Electronic Mail: director@fasb.org, File Reference No. 1850-100

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

Dear Sir/Madam:

Standard & Poor’s Ratings Services (Standard & Poor’s) appreciates the opportunity to provide the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) (collectively, the Boards), our comments on the Boards’ Proposed Accounting Standards Update, Leases (Topic 840) (the Proposed Standard). The views expressed in this letter represent those of Standard & Poor’s Ratings Services and do not address, nor do we intend them to address, the views of any other subsidiary or division of Standard & Poor's Financial Services LLC or of its parent, The McGraw-Hill Companies. We intend our comments to address the analytical needs and expectations of our credit analysts.¹

GENERAL

We continue to support international harmonization of accounting standards, and believe a common set of high quality and consistently enforceable accounting standards would best facilitate efficient global capital markets. We believe convergence between U.S. Generally Accepted Accounting Principles (U.S. GAAP) and International Financial Reporting Standards (IFRS) should be a significant consideration and a priority for the

¹ The opinions stated herein are intended to represent Standard & Poor’s Ratings Services’ views on potential changes in accounting and financial reporting standards. Our current ratings criteria and the application of their related principles, methodologies, and assumptions are not affected by our comments on the Proposed Standard.
Boards in their respective deliberations of their standards. Because we rate companies globally, comparable accounting is important to our peer analysis and comparisons. We commend the Boards for eliminating many of the differences between their respective approaches that were present in the 2009 Leases: Preliminary Views (Lease Discussion Paper), but several remain, and we encourage the Boards to eliminate them in the final standard.

Given the importance of leasing as a source of business financing and the extensive use of leases by many of our rated companies, we have always considered that the use of leases can meaningfully alter the financial and liquidity characteristics of an issuer. Understanding an issuer’s leasing activities is important to our credit analysis.

As such, we maintain our continued support for the Boards’ decision to reconsider existing lease accounting standards so that financial statements will provide more useful, transparent, and complete information about leasing transactions. We continue to support the Boards’ objective to address what we believe are certain shortcomings of the existing accounting model for lessees (e.g., off-balance sheet treatment for operating leases, rules-based nature, ability to structure around bright line tests, and overall complexity of existing standards) by producing a significantly improved common standard. We also favor the Boards’ efforts to enhance financial statement disclosures to provide better information about the amounts, timing, and uncertainty of cash flows arising from leases.

We do not, however, support the Boards’ decision to provide a dual approach to lessee accounting as further discussed under Specific Areas of Concern/Recommendations, below.

**THE RIGHT-OF-USE MODEL FOR LESSEE ACCOUNTING**

We generally agree with the right-of-use model presented in the Proposed Standard. We believe the most significant impact of the new model for lessees will be the removal of the accounting distinction between operating and finance leases (capital leases), placing obligations formerly classified as operating leases on the balance sheet—a result we very much support. We have long viewed the accounting distinction between operating and finance leases as substantially artificial because, in both cases, the lessee contracts for the use of an asset, entering into a debt-like obligation to make periodic rental payments. As a result, we historically have adjusted reported amounts to eliminate the operating or financing distinction by capitalizing lease obligations accounted for as operating leases by corporate issuers. We principally adjust by capitalizing the net present value of disclosed future minimum lease payment commitments and by adjusting profitability and cash-flow measures used in our analysis to reflect our view of the financing nature of this activity. (For further details on our adjustments for operating leases, please refer to the "Encyclopedia of Analytical Adjustments" section of Standard & Poor's Corporate Ratings Criteria 2008, published April 15, 2008 on RatingsDirect and www.sandp.com.)

We believe the model in the Proposed Standard could potentially capture the economics of our operating-lease-adjustment methodology. We expect the proposed model to improve the financial reporting of the underlying economics of leasing transactions, and
provide better, decision-useful information to financial-statement users than current accounting standards.

PROVIDE COMPREHENSIVE DISCLOSURES

We believe comprehensive disclosure about the nature of the lease including potential for variability in lease payments as well as purchase, renewal, and termination options will be an important facet in allowing financial-statement users to better understand the application and consequences of the new leasing standard and leasing arrangements undertaken by both lessees and lessors. Disclosures are even more important, given the complex nature of many leasing transactions, the options, guarantees, and contingencies that are common in lease arrangements, and the principles-based accounting framework of the proposal.

Robust disclosure of leasing activities is important to provide better understanding of the economics of the business and its leasing activities; their accounting aspects; and the assumptions and estimates used to arrive at the reported amounts. In this regard, we support the FASB’s separate project to establish an overarching disclosure framework aimed partly at making all financial statement disclosures, including those for leasing transactions, more effective and coordinated. We strongly encourage the Boards to work together on this project and on a comprehensive disclosure framework, giving further consideration to additional relevant disclosures related to leasing activities.

We provide specific recommendations regarding disclosure throughout this letter, and in our responses to the Boards’ questions (including Question 15, Disclosure).

SPECIFIC AREAS OF CONCERN/RECOMMENDATIONS

Despite our general agreement with the principles proposed in the right-of-use model, we do have some broad areas of concern and recommendations, including:

- **Two lessor-accounting approaches (Question 2)** – We are concerned with the complexity associated with the proposed dual approach and whether the proposed guidance will result in consistent application of the two approaches among lessors. We prefer the Boards provide a single approach to lessor accounting, because we believe the consistency, complemented by robust disclosures, would be more helpful in performing peer comparisons. We believe the Boards should undertake field-testing, including with users of financial statements, before finalizing an approach to lessor accounting.

- **Lease definition (Question 4)** - We are concerned that for some arrangements (e.g., certain long-term power purchase agreements, in-substance purchases or sales, etc.), the definition and application guidance provided in the Proposed Standard may still lead to inconsistent application. Accordingly, we recommend that the Boards require disclosures of significant contracts not treated as leases but that otherwise commit an entity to pay for the use of an asset or receipt of services that are substantially dependent on assets. These disclosures will outline
information on the types of contracts that may or may not contain a lease and the nature and amounts of the related off-balance sheet commitment.

- **Scope exclusions (Question 5)** - We urge the Boards to consider a second phase for the lease project that would address the remaining lease issues not fully addressed in the Proposed Standard, such as leases of intangible and similar assets. We view many of these contracts as substantially akin to a lease and suggest their accounting treatment should be harmonized.

- **Service components of a lease (Question 6)** – We are concerned that the guidance could lead to inconsistent application as it relates to distinguishing between a lease and a service component. We recognize that inconsistency may be inherent in a principles-based standard and therefore recommend the Boards require additional specific disclosure requirements concerning the service component of leases by both lessees and lessors.

- **Lease term and lease payments (Questions 8 and 9)** – We believe the Proposed Standard could result in inconsistent application regarding the assignment of probabilities to lease-term options and in the identification of reasonably possible outcomes regarding lease payments. We therefore recommend that the Boards require disclosures that would allow users of financial statements to understand how lease liabilities may differ under different plausible lease-term and lease-payment assumptions from those chosen by management, including estimates of such amounts.

- **Reassessment (Question 10)** - We recommend the Boards provide additional disclosure requirements that identify what constitutes a significant change in a lease and how management arrived at its conclusions on reassessment.

We have provided more details to the above comments and responses to specific questions listed in the Proposed Standard in the appendix to this letter.
We thank you for the opportunity to provide our comments on the Proposed Standard. We would be pleased to discuss our views with any member of the Boards or your staff. If you have any questions or require additional information, please contact the undersigned.

Very truly yours,

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Enclosure:
Appendix – Response to Specific Questions in the Proposed Standard
Appendix – Response to Specific Questions in the Proposed Standard

The accounting model

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?

a) We agree with the Proposed Standard’s view that lessees should recognize a right-of-use asset and a liability to make lease payments. The proposed approach is consistent with our long-held view that the accounting distinction between operating and finance (capital) leases is substantially artificial, because in both cases, the lessee contracts for the use of an asset, entering into a debt-like obligation to make periodic rental payments.

b) We agree that a lessee should recognize amortization of the right-of-use asset and interest on the liability to make lease payments. This is consistent with our long-held view that payments under operating leases should be recharacterized from rent expense to an amortization (depreciation) component and an interest expense component. We believe amortization treatment for the decrease in value of the right-of-use asset is more appropriate than treatment as rent expense, given the concept that a right-of-use asset is created under the new model. Amortization treatment would be consistent with how the carrying value of fixed and intangible assets is reduced in the financial statements over time.

Question 2: Lessor

(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? (FASB only)

a) and b) We recognize there are conceptual advantages and disadvantages to both the performance obligation approach and the derecognition approach to lessor accounting, including potential inconsistencies with lessee accounting for the performance obligation approach and with the Proposed Accounting Standards Update, Revenue Recognition (Topic 605): Revenue from Contracts with Customers (Revenue Recognition Exposure Draft) for the derecognition approach. We are concerned with the complexity associated with the Proposed Standard’s dual approach, and whether the proposed guidance will result in consistent application of the two approaches among lessors for economically similar types of arrangements.

Our preference is for a single approach to lessor accounting, because we believe the consistency from a single approach, supported by robust disclosures, would be more helpful in performing peer comparisons. Before deciding on a final model for lessor accounting, we suggest the Boards perform comprehensive field-testing, including with users of financial statements, of the two approaches as currently proposed. The additional information provided by the testing should assist the Boards in assessing whether a single or dual approach will result in more useful financial information, and whether either would be preferable to existing lessor accounting standards. We also suggest that the lessor accounting model be evaluated in conjunction with the Revenue Recognition project and be conceptually harmonized as it relates to akin or analogous revenue generating activities.

c) We agree that a separate approach for lessors with leveraged leases is not needed; however, please see our response to Question 16(c) regarding Transition.

**Question 3: Short-term leases**

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 stated in our comment letter response to the Lease Discussion Paper that the proposed standard should not provide exclusions for short-term leases and that the financial statements would be most informative and consistent if all material leases were subject to a single model without exception to avoid mixed-attribute accounting measures. We also stated our belief that exempting short-term leases could be an invitation to structuring contracts around the new model and that varied subjective interpretations as to what constitutes "short-term" could lead to inconsistent treatment. We, therefore, support the Boards’ decision to not provide a blanket exclusion for short-term leases.

Notwithstanding the above, we recognize the costs and complexities involved in applying the proposed model, and therefore support the use of the proposed simplified
requirements for short-term leases for both lessees and lessors. However, our support hinges on adequate disclosure regarding short-term leases (i.e., that the disclosure of amounts recognized in the statement of financial position for short-term leases required by Paragraph 75 of the Proposed Standard remains in the final standard). We further recommend that the disclosure requirement provided in Paragraph 75 be extended to amounts recognized in the income statement.

Further, rather than allowing a lessor that has a short-term lease the option to elect on a lease-by-lease basis not to recognize assets and liabilities arising from a short-term lease, we recommend that the Proposed Standard provide that any election would apply to all short-term leases of the same or similar nature.

**Definition of a lease**

**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) As stated in our comment letter response to the Lease Discussion Paper, further clarification of the types of arrangements that meet the definition of a lease are needed to address issues not fully resolved by ASC 840-10-15 (formerly EITF 01-8) and its international equivalent, IFRIC 4. As the Proposed Standard’s definition of a lease remains generally the same as under existing standards, we still are concerned that, for certain arrangements (e.g., certain long-term power purchase agreements), the definition and application guidance provided in the Proposed Standard may still be difficult to apply and may lead to inconsistent application. Accordingly, if the Boards finalize the Proposed Standard as written, we recommend the Boards require disclosures of significant contracts not treated as leases but that otherwise commit an entity to pay for the use of an asset or receipt of services that are substantially dependent on assets. These disclosures will outline information on the types of contracts that may or may not contain a lease and the nature and amounts of the related off-balance sheet commitment.

Further, as noted in our response to Question 5, we believe accounting for leases of intangible and similar assets currently not encompassed by the proposed definition, should be considered by the Boards.
b) We agree with the criteria in the Proposed Standard for distinguishing a lease from a contract that represents a purchase or sale (i.e., an in-substance purchase or sale) whereby a contract would represent a purchase or sale if a company transfers control of the entire underlying asset and all but a trivial amount of the asset’s risks and benefits. We further agree that control normally would be transferred when a contract automatically transfers title at the end of the contract term or if it includes a bargain purchase option. Because companies would not apply the Proposed Standard to such purchase or sale contracts, resulting in different accounting treatment from leasing arrangements, we recommend that the Boards provide for disclosures of the nature and amounts pertaining to in-substance purchases or sales contracts.

c) See our response to Question 6 comments on distinguishing leases from service contracts.

**Scope**

**Question 5: Scope exclusions**

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 support the Boards’ decision to provide scope exclusions for the enumerated areas that the Boards believe require further consideration. We recognize, however, that there is a need to address, in a reasonably acceptable amount of time, issues that are excluded from the scope of the Proposed Standard, such as leases of intangible and similar assets. This would include addressing the significant scope differences that currently exist between IAS 17 and ASC 840 (e.g., inclusion of some intangible assets under IAS 17) and differences with regard to investment property. We urge the Boards to consider a second-phase lease project that will soon thereafter address remaining lease issues that were not fully addressed by the Proposed Standard or in a separate project (e.g., the FASB’s separate project on investment property).

We also refer the Boards to our discussion of in-substance purchases or sales, in our response to Question 4(b).

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

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 Proposed Standard’s approach that distinguishes the service and lease components of a contract by whether or not the services are distinct. For lessees, we agree with both Boards’ proposal that, when the service component is not distinct, the
lease accounting requirements of the Proposed Standard be applied to the combined contract.

Regarding differing treatments for lessors proposed by the FASB and IASB, we understand the merits of both Boards' positions and recommend the Boards agree on a joint position for the final standard. We believe the FASB's approach is simple, practical, and in our view, preferable to the IASB's approach.

We are concerned about the guidance defining when a service is distinct in the Proposed Standard and in the Revenue Recognition Exposure Draft: It may be difficult to apply it to certain industry-specific transactions. This may be especially true when a company is faced with determining a distinct profit margin for a sale involving bundled goods and services that may not be sold separately. We believe that the proposed guidance could lead to inconsistent application as currently proposed, and therefore recommend the Boards require disclosures that would clarify how a company determines whether a service component is distinct. We recommend both lessees and lessors be required to provide disclosure on the amounts of the service components contained in their lease contracts, including a breakdown of the amounts considered to be distinct (and thus accounted for under the Revenue Recognition Exposure Draft) and the amounts accounted for as leases under this Proposed Standard.

We support the exclusion of executory costs (i.e., insurance, maintenance and taxes) from the lease components. Capitalizing them in the asset/liability would make them inconsistent with those companies that purchase assets and account for these costs as period costs.

**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 exercised. We agree with the Boards' conclusion that, when a lessee exercises a purchase option, it terminates the lease and results in a purchase of the underlying asset by the lessee and a sale by the lessor. As a result, we agree that the exercise price of the option should not be viewed as a lease payment and should not be included in the measurement of the lease asset and liability if the option is at the money at the lease inception. Any favorable or unfavorable amount should be reflected as an adjustment to the lease payments.

In addition to disclosure regarding the existence and principal terms of any options for the lessee to purchase the underlying asset, we further recommend that disclosure of the aggregate amount paid each reporting period to exercise purchase options be provided in the final standard.
**Measurement**

**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 agree with the Proposed Standard’s view that lessees and lessors should determine the lease term as the longest possible lease term that is more likely than not to occur, taking into account any extension or termination options. We recognize that lease options can significantly extend the life of the lease and we believe the cumulative approach proposed would likely result in management’s best estimate of the term. While the Proposed Standard provides guidance on the contractual, noncontractual, business, and other factors (lessee’s intentions and past practices), we realize that there is the potential for the Proposed Standard to result in inconsistent application regarding the assigning of probabilities to lease term options. As such, we stress the importance of disclosure in this area. We recommend that additional requirements for quantitative disclosures about management’s judgments regarding lease term options, beyond the narrative disclosure provided by the Proposed Standard (Paragraph 73 (a) (iii)), be added to the final standard. Such expanded disclosure, which could include a schedule summarizing both the amounts related to the term options recognized and those that were not, would allow users to better understand the company reported information, assess lease liabilities under different lease term assumptions than those chosen by management, and better enable peer analysis.

**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 support the Proposed Standard’s approach of including estimates of amounts payable for contingent rentals, residual value guarantees, and expected payments under term option penalties in the measurement of lease assets and liabilities. Exclusion of these amounts could result in significant understatement of the economic assets and liabilities.
under leases. Therefore, we believe measuring them initially is preferable to excluding them from the calculation of estimated lease payments and then recognizing the expense when incurred, as is generally the case under existing standards.

We also support the proposed approach to using the present value of the probability-weighted average of the cash flows for a reasonable number of outcomes to represent the expected outcome. However, we realize that there is the potential for the Proposed Standard to result in inconsistent application regarding how companies identify reasonably possible outcomes. Further, probability-weighted expected outcomes may represent a value that is not representative of any of the actual outcomes. We, therefore, stress the importance of disclosure in this area.

We recommend that, for material leases or groups of leases, additional quantitative disclosures about management’s judgments regarding contingent rentals, residual value guarantees, and expected payments under term option penalties, beyond the disclosure provided by the Proposed Standard (Paragraph 73 (a) (ii) and (vi)), be added to the final standard. This disclosure should include the factors considered by management in determining the range of outcomes and their probability. Such disclosure would allow financial statement users to better understand the reported information, estimate the potential for change in lease liabilities under different assumptions than those chosen by management, and compare peer information.

We agree with the Proposed Standard’s concept that lessors should only include contingent rentals and expected payments in the right to receive lease payments if they can be reliably measured. This concept also appears to be consistent with the Revenue Recognition Exposure Draft. However, we recommend that the Boards require companies to disclose the factors they considered to discern the “reliability of measurement” threshold as well as information on possible amounts when the reliability thresholds were not met.

**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?*

As outlined in our response to the Lease Discussion Paper, we support the Proposed Standard’s requirement for lessees and lessors to reassess estimates of the lease term and contingent rental payments. While we believe requiring reassessment at each reporting date, as was proposed in the Lease Discussion Paper, would lead to better financial reporting, we recognize the Boards’ desire to balance the benefits to financial statement
users with the costs incurred by reporting entities. Therefore, we support the significant modification made by the Boards to require reassessment only upon an indication of a ‘significant change’ in the lease asset or liability since the previous reporting period. However, we recommend that the Boards provide additional detailed disclosure requirements for companies to identify what constitutes a significant change and how management arrived at its conclusions on reassessment. Amounts arising from significant changes should also be separately identified from those attributable to new leases entered into or terminated during the period.

We recognize the possibility of a material change in circumstances that would affect management’s view of the most likely lease term, (e.g., the addition of significant leasehold improvements could make it more likely that a company will extend the lease term). Likewise, we recognize there can be a material change in circumstances surrounding a contingency that will affect the estimated rental payment (e.g., where a sudden increase in retail sales because of the failure of a major competitor leads management to a new conclusion that a sales contingency that had not been likely will now be easily reached).

We believe financial statement users would be well served if these types of changes in circumstances are reflected in the lease asset or liability, because this would give users a more current depiction of the long-term asset or liability resulting from the leasing transaction and an indication of changes to what was previously estimated. We believe detailed disclosure of the changes in circumstances considered in the reassessment of lease terms and contingent rental payments are essential, allowing analysts and other users to understand the effects of the variability to the company’s lease assets, liabilities, earnings, and cash flows.

**Sale and leaseback**

**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 in the Proposed Standard for determining classification as a sale and leaseback transaction. We believe that using the same criteria for a sale as is used to distinguish between purchases or sales and leases is a logical and consistent approach for both lessees and lessors.

We also believe that the specific disclosure requirements provided by Paragraph 76, which require that lessees disclose the terms and conditions of the transaction and identify gains and losses from such transactions separately from other gains and losses on disposal of other assets, will provide useful information to analyze such transactions.
Presentation

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, 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 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?

a) We agree with the Proposed Standard’s requirement that a lessee should present its liabilities to make lease payments separately from other financial liabilities in the statement of financial position. Because we view the liability to make lease payments as debt-like, we believe it would also be appropriate to present the obligation as a separate component of debt in the debt footnote.

We also agree with the Proposed Standard’s view that a lessee should present right-of-use assets in the statement of financial position within property, plant and equipment (rather than as an intangible asset) separately from owned assets. We believe, aside from separate presentation in the statement of financial position, additional footnote disclosure similar to that required for other fixed assets and intangible assets should be required. This should include a description of the nature of the lease transactions, a breakdown of leased assets by type of asset, and the depreciable lives and lease term for each type of asset. Considering the subjectivity and judgment involved in establishing the related assets and liabilities, it is important for users to be able to identify those items so that they
can consider a range of plausible outcomes and assess the data as necessary (e.g.,
consider the impact of different renewal periods, probabilities, etc.).

Separate presentation of both the liabilities to make lease payments and the right-of-use
assets would provide the most direct presentation of these significant assets and liabilities
and is preferred for our analysis. However, we could also retrieve information for our
analysis if entities disclosed them separately in the footnotes. However, this may affect
the timeliness of the information for users for public registrants since balance sheets are
often included in earnings release data whereas footnote disclosures are only available
later in conjunction with the periodic regulatory filing.

b) If the performance obligation approach is adopted as provided in the Proposed
Standard, we agree that lessors should follow the “linked” presentation, presenting
separately the 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.

c) If the derecognition approach is adopted as provided in the Proposed Standard, we
agree that lessors should present rights to receive lease payments separately from other
financial assets and should present residual assets separately within property, plant and
equipment.

d) We agree with the Proposed Standard’s requirement that lessors entering into sublease
arrangements (intermediate lessors) should distinguish assets and liabilities that arise
under a sublease in the statement of financial position. It is important that our analysts be
able to analyze separately rights to receive lease payments under sublease agreements and
liabilities to make lease payments arising from the head lease. However, when considered
insignificant for separate presentation within the statement of financial position, we could
also retrieve information for our analysis if entities disclosed such sublease assets and
liabilities separately in the footnotes.

**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 and lessors should present lease income and lease expense
separately from other income and expense in the income statement, with supplemental
footnote disclosure. Where considered insignificant for separate income statement
presentation, we could retrieve information for our analysis if entities disclosed the
information separately in the footnotes, however, separate presentation within the income
statement would be our preference, also due to the timeliness consideration as we
discussed in Question 12.
For lessees, it would be important for our analysts to be able to determine the company’s total cost of leasing, with a breakdown of lease expense between amortization and interest expense. Also, disclosure related to total interest expense and total amortization should provide a breakdown between the leasing component and the non-leasing component. These disclosures should be provided in the footnotes if not included directly 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 believe lessees and lessors should present cash flows arising from leases separately in the statement of cash flows, as the amount of cash lease payments (lessees) and receipts (lessors) is an important component of our analysis. Where considered insignificant for separate presentation within the statement of cash flows, we could also retrieve information for our analysis if entities disclosed the information separately as a supplemental item within the statement of cash flows, or alternatively in the footnotes, however, separate presentation within the statement of cash flows would be our preference.

Disclosure

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?

We strongly support the Proposed Standard’s inclusion of comprehensive quantitative and qualitative disclosures on companies’ leasing activities. We believe the disclosure requirements in the Proposed Standard would provide our analysts and other financial-statement users with information necessary to understand how the company engages in leasing transactions and how leases affect its financial position, earnings, and cash flows.
However, we believe there are some areas where our analysts could benefit from additional disclosures. In addition to those mentioned in our responses to the other specific questions, we further recommend the disclosures in Paragraphs 73 – 86 be expanded to the following:

For lessees:
- The general description of lease arrangements include specific disclosure on the nature of the assets leased and business purpose;
- For contingent rentals, additional information beyond the basis and terms on which they are determined be provided, including quantitative disclosure that will allow users to compute the change in lease liabilities under different plausible contingent rental assumptions;
- For term option periods, additional quantitative information beyond the narrative disclosure that will allow users to understand and estimate the change in lease liabilities under differing plausible lease term assumptions; and
- The required disclosure regarding the discount rate used, both at transition and for continuing application, include a table indicating the range of incremental borrowing rates applied and the company’s overall average incremental borrowing rate.

For lessors and lessees:
- Additional disclosure regarding ranges of lease rates and lease terms, as well as additional disclosure about lease restructurings and early termination of leases.

We also support the FASB’s separate project to establish an overarching disclosure framework. We strongly encourage the Boards to work together on a comprehensive disclosure framework, giving further consideration to additional relevant disclosures relating to leasing activities. We believe that users of financial statements would benefit from robust lease disclosures of key assumptions similar to other areas of accounting where significant estimates are employed (such as pensions), that would provide additional meaningful information allowing users to better understand the amount, timing, and uncertainty of an entity’s future cash flows. For example, as provided in our response to Question 8, we recommend additional requirements for quantitative disclosures about management’s judgments regarding lease term options, such as a schedule summarizing both the amounts related to the term options recognized and those that were not. This would help address the subjectivity inherent in determining the lease term under the new guidance and would allow financial statement users to better understand the company reported information, assess lease liabilities under different lease term assumptions than those chosen by management, and better enable peer analysis.
Transition

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?

a) Generally, our view is that full retrospective implementation is most helpful to our analysis. Retrospective implementation best suits period-to-period trend assessments. However, we recognize that some entities likely would encounter extensive operational burdens and costs in implementing the Proposed Standard under a full retrospective transition method. Therefore, we agree with the Proposed Standard’s proposed requirement that lessees and lessors should measure all outstanding leases as of the date of initial application using a simplified retrospective approach. We agree as well as with the Boards’ assessment that this approach balances the need for comparable information and the costs of full retrospective application.

b) As stated in our response to Question 16(a), our general view is that full retrospective implementation is most helpful to our analysis, therefore, we believe it should be permitted for those companies that prefer it over the simplified retrospective approach.

c) Since the Proposed Standard does not provide a separate approach for lessors’ treatment of existing leveraged leases (as accounted for under U.S. GAAP), we believe further clarification by the Boards as to how these existing leveraged leases are to be treated under the Proposed Standard would be helpful in achieving consistent application by lessors. Further, we recommend a specific disclosure requirement of the nature, amount, and accounting treatment of a company’s existing leveraged leases under U.S. GAAP so that users of financial statements will be able to understand how they are treated by lessors under the new standard.

Non-public entities

Question 19 (FASB only)

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 do not believe that the Proposed Standard should contain different guidance for nonpublic entities. Because we do not differentiate our general analytical needs on the basis of an entity’s share registration status, in our opinion, different accounting standards for public and nonpublic entities would add additional hurdles and complexity to our analysis.

We understand that certain nonpublic entities may be challenged by the transition to a new standard. We generally would be supportive of a limited extension of the effective date for nonpublic entities if the Boards deemed it appropriate; however, it would not be our preference due to decreased comparability during the extended period. Nevertheless, we believe a phased-in approach—accompanied by adequate disclosures—is appropriate, for example, for companies where there are significant operational and cost constraints.