October 14, 2013

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

RE: Proposed Accounting Standards Update, “Applying Variable Interest Entity Guidance to Common Control Leasing Arrangements” (File Reference No. PCC-13-02)

Dear Technical Director

We appreciate the opportunity to comment on Proposed Accounting Standards Update, “Applying Variable Interest Entity Guidance to Common Control Leasing Arrangements.” We support the proposal to provide an exemption from applying the variable interest entity (VIE) consolidation requirements to common control leasing transactions. However, we believe the Board should not limit its consideration of the applicability of the VIE consolidation requirements to private companies or to common control leasing transactions.

The guidance on VIE consolidation is difficult to understand and apply to leasing transactions and has created diversity in application for all entities subject to the VIE consolidation requirements, not just for private companies. This is due to a lack of clarity on a number of issues, including:

- When does a lessee have an implicit variable interest in the lessor;
- Whether the risks that the lessee was designed to create and pass through to its variable interest holders include risks from operations of the leased asset during the lease term;
- When is it appropriate to consider the operations of the leased asset during the lease term to be activities that significantly impact the lessor’s economic performance, which affects the determination of whether the lessee meets the power criterion in ASC paragraph 810-10-25-38A(a) solely as a result of the leasing arrangement;
- Whether it is appropriate for a lessee to consolidate a VIE lessor when doing so would result in replacing liabilities with noncontrolling interests on the lessee’s balance sheet; and
- How to identify circumstances in which a lessor should consolidate a VIE lessee.

In view of the foregoing issues, we recommend that the Board comprehensively address application of the VIE consolidation requirements to leasing arrangements. However, if the Board does not undertake a holistic consideration of VIE consolidation guidance for leasing arrangements, we believe the Board should consider expanding the scope of the proposed exemption to all entities.
subject to the VIE consolidation requirements, including public companies, and to arrangements involving lessees and lessors under common ownership but not under common control.

As noted in our previous responses to private company proposals, we believe that differences in Generally Accepted Accounting Principles for private companies established by the FASB should meet the following criteria:

(1) They should be based on differences in information needs of users of private company financial statements as compared to users of public company financial statements. The assessment of whether there are differences in information needs should include consideration of the information needs of both users of private company financial statements and users of public company financial statements and a comparison of those information needs.

(2) They should be supported by an analysis and explanation of how the differences and alternatives meet the Private Company Decision-Making Framework.

(3) They should not create a fundamentally different conceptual basis for preparing financial statements of private companies as compared to the conceptual basis for public company financial statements. We understand that the decision of the Financial Accounting Foundation (FAF) to require endorsement by the FASB of the recommendations of the Private Company Council (PCC) is intended to avoid the creation of two fundamentally different GAAPs for public and private companies.

(4) They should reduce unnecessary complexity in the overall standard-setting process and financial reporting system. The assessment of the impact of modifications and alternatives to accounting standards for private companies on cost and complexity should consider the potential implications on the overall standard-setting process and financial reporting system, not just the application of a specific provision of an individual standard.

We believe these criteria are consistent with the objectives of the FAF and the FASB in establishing the PCC and the related operating procedures. The proposed ASU does not describe the differences in information needs of users of public company and private company financial statements with respect to the matters covered in the proposed ASU. The proposed ASU also does not address how the FASB considered whether it would result in creating two fundamentally different GAAPs with different conceptual bases for public and private companies.

While we are supportive of the proposed ASU’s proposed relief from applying the VIE consolidation requirements to certain leasing arrangements, it is not clear how the information needs of private company financial statement users differ from those of other entities, including public companies, that are subject to the VIE consolidation requirements with respect to these arrangements. We believe differing financial reporting requirements for public versus non-public entities is a source of complexity in the accounting literature. As a result, we believe the scope of the guidance should be expanded to all entities that are subject to the VIE consolidation requirements, including public companies. We also believe optionality is a source of complexity in the accounting literature. We do
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not see a benefit from the proposal to permit the relief from the VIE consolidation guidance to be
applied on an elective basis. Accordingly, we recommend that the transactions addressed by the
proposed ASU be excluded from the scope of the VIE consolidation subsections of ASC 810-10.

However, we believe a more comprehensive reconsideration of the application of the VIE guidance
to leasing arrangements and other potential implicit variable interests is necessary.

We also note that the example that is codified in paragraphs 810-10-55-87 through 55-89 is the only
illustrative guidance related to implicit variable interests within U.S. GAAP. We believe that rather
than eliminating that example, the FASB should consider revising it or providing a replacement
example related to implicit variable interests that is not contradictory to the proposed standard.

Our responses to certain Questions for Respondents are included in Appendix A.

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If you have any questions about our comments or wish to discuss any of the matters addressed
herein, please contact Mark Bielstein at (212) 909-5419 or Kimber Bascom at (212) 909-5664.

Sincerely,

KPMG LLP

KPMG, LLP
Appendix A: Responses to Select Questions for Respondents

Question 2: Do you agree that the accounting alternative in the proposed Update should apply to all entities except public business entities, not-for-profit entities, or employee benefit plans within the scope of Topics 960 through 965 on plan accounting? If not, what type of entities should not be included in the scope of this accounting alternative?

We do not agree that the accounting alternative in the proposed ASU should apply to all entities except public business entities, not-for-profit entities, or employee benefit plans within the scope of Topics 960 through 965 on plan accounting. We believe differing financial reporting requirements for public versus non-public entities is a source of complexity in the accounting literature. We also do not believe the information needs of users of private company financial statements are sufficiently different from those of other entities, including public companies, that are subject to the VIE consolidation requirements to warrant the need for separate accounting standards as it relates to the application of the VIE consolidation requirements to leasing arrangements. As a result, we believe the scope of the proposed ASU should be expanded to apply to all entities that are required to apply the VIE consolidation subsections of ASC 810-10, including public business entities. Further, we do not believe the scope exception for not-for-profit entities is necessary because those entities are excluded from the scope of the VIE consolidation requirements.

The guidance on VIE consolidation is difficult to understand and apply to leasing transactions and has created diversity in application for all entities subject to the VIE consolidation requirements, not just for private companies. This is due to a lack of clarity on a number of issues, including the following:

- It is not clear when an implicit variable interest should be deemed to exist in leasing arrangements, especially those between entities under common control or common ownership.
- It is unclear how to determine whether an explicit variable interest exists in a capital lease because there is insufficient guidance about whether the risks that the lessor was designed to create and pass through to its variable interest holders include risks from operations of the leased asset during the lease term.
- There are differing views in practice about whether the activities related to operating a leased asset during the lease term should be considered activities that significantly impact the economic performance of the lessor. As a result, there are differing views about whether a lessee can meet the condition in ASC 810-10-25-38A(a) solely as a result of the leasing arrangement even if the lease is considered to give the lessee an explicit or implicit variable interest in the lessor. If the activities related to operating a leased asset during the lease term are not considered activities that significantly impact the economic performance of the lessor, then it would be highly unusual for a lessee to meet the condition in ASC 810-10-25-38A(a) solely as a result of the leasing arrangement because the lease typically would not give the lessee the right to make decisions about the lessor’s other activities (e.g., decisions about how the lessor is financed, etc.).
- It is unclear whether it is appropriate for a lessee to consolidate a VIE lessor when doing so would result in replacing liabilities with noncontrolling interests on the lessee’s balance sheet. Many in

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practice believe the only situation in which the FASB intended for a lessee to consolidate a lessor is when not doing so would inappropriately exclude debt from the lessee’s balance sheet.

- It is unclear how to identify circumstances in which a lessor should consolidate a VIE lessee. The lack of clarity around when a lender should consolidate a VIE borrower contributes to the confusion in this area.

It would be helpful for the Board to clarify the guidance in ASC Subtopic 810-10 as it relates to these issues regardless of whether the scope of the proposed ASU is expanded as we recommend.

**Question 3:** Do you agree that the proposed Update does not apply to public business entities and employee benefit plans because they lack the arrangements that the accounting alternative addresses? If not, please describe the arrangements that exist for those types of entities that the Board should consider in determining whether any public business entities or employee benefit plans should be included in the scope of the proposed accounting alternative.

We do not agree that entities other than private companies lack the arrangements that the proposed ASU addresses. Although less frequent than may be the case for private entities, we understand that other entities could have these types of arrangements. For example, these types of arrangements may exist where a public company is controlled by a single shareholder that also controls an entity that leases property to the public company.

**Question 4:** Do you agree with the required criteria for applying the proposed accounting alternative? If not, please explain why.

We believe the Board should consider expanding the scope of the proposed guidance to situations that are similar to common control leasing arrangements. The situation addressed by the proposed ASU also may arise when the lessee and lessor are under common ownership but not under common control. For example, a group of family members may control the lessee and lessor with no individual family member having unilateral control. Expanding the scope of the proposed ASU to include these types of arrangements, if they meet the other proposed criteria would be helpful in achieving the Board’s objectives.

**Question 5:** Do you agree that paragraph 810-10-55-9, which describes the effects of guarantees and joint and several liability arrangements related to a mortgage on the lessor’s assets, provides sufficient guidance to clarify what constitutes a supporting leasing activity for applying paragraph 810-10-15-17A(c)? If not, please explain why.

We agree that the example provided in proposed paragraph 810-10-55-9 helps to clarify what constitutes a supporting leasing activity for purposes of the proposed criterion in paragraph 810-10-15-17A(c). However, we believe the Board also should provide guidance to illustrate the types of activities that do not support leasing activity for purposes of the proposed criterion in paragraph 810-10-15-17A(c).

In addition, we believe the Board should provide additional guidance to clarify how the lessee should account for joint and several liability arrangements related to a mortgage on the lessor’s assets. Specifically, it is not clear whether these obligations would be accounted for as part of the lease arrangement (e.g., as contingent rent) or would be subject to the guidance in ASU 2013-04.

**Question 6:** Do you agree that the following additional disclosures about lessor entities should be provided if a private company elects the proposed accounting alternative? If not, please explain why.
- The key terms of the leasing arrangement
- The amount of debt and/or significant liabilities of the lessor entity under common control
c. The key terms of existing debt agreements of the lessor entity under common control (for example, amount of debt, interest rate, maturity, pledged collateral, and guarantees)

d. The key terms of any other explicit interest related to the lessor entity under common control. Should other disclosures be required as a result of applying this alternative?

We agree with the proposed additional disclosures about lessor entities if a company applies the guidance in the proposed ASU.

**Question 7:** Do you agree that, generally, the primary purpose of establishing a separate lessor entity in a private company setting is for tax and estate-planning purposes and not to structure off-balance-sheet debt arrangements? If not, please explain why.

The purpose of establishing a separate lessor entity as identified by the PCC and FASB seems too narrow. There could be other business reasons that a company may have to establish a separate lessor entity. For example, a company might establish a separate lessor entity to legally isolate the leased assets from its creditors. We do not believe that the purpose of establishing these types of entities should impact the applicability of the proposed guidance.

**Question 9:** Do you agree that the proposed accounting alternative, when elected, is an accounting policy election that should be applied by an entity to all current and future lessor entities under common control that meet the criteria for applying this approach?

We believe optionality is a source of complexity in the accounting literature. We do not see a benefit from the proposal to permit the relief from the VIE consolidation guidance to be applied on an elective basis and believe it is a potential source of complexity. Accordingly, we recommend that the transactions addressed by the proposed ASU be excluded from the scope of the VIE consolidation subsections of ASC 810-10. However, we believe a more comprehensive reconsideration of the application of the VIE guidance to leasing arrangements and other potential implicit variable interests is necessary.

**Question 10:** Do you agree that the proposed accounting alternative should be applied using a full retrospective approach in which financial statements for each individual prior period presented and the opening balances of the earliest period presented would be adjusted to reflect the period-specific effects of applying the proposed amendments?

We agree that the proposed guidance should be applied using a full retrospective approach.

**Question 11:** When should the proposed alternative accounting be effective? Should early application be permitted?

We do not anticipate that the implementation of the proposed guidance would require significant time to implement. We believe early adoption should be permitted.

**Question 12:** Do you agree that the example that is codified in paragraphs 810-10-55-87 through 55-89 (described in paragraphs BC19 through BC20 of this proposed Update) should be removed? Do you agree that the removal of the example would not significantly affect public business entity stakeholders? If not, please explain why.

As discussed in our cover letter, we believe that the example should be revised or replaced to provide illustrative guidance to both public and private companies as it relates to implicit variable interests.
Question 13: The PCC considered two other alternatives (as described in paragraphs BC15 through BC18 of this proposed Update) to clarify the application of VIE guidance to common control leasing arrangements.

a. Would either of those alternatives better address the concerns raised by private company stakeholders?

b. Should the PCC and the Board consider either of those alternatives in conjunction with the guidance in this proposed Update to better address the concerns raised by private company stakeholders?

We do not believe either of the other alternatives considered by the PCC would better address the concerns raised by private company stakeholders about the application of the VIE guidance to leasing arrangements. We believe that those alternatives could lead to inappropriate analogies by financial statement preparers in the application of the VIE consolidation guidance in Subtopic 810-10. Therefore, we would be concerned if either of the alternatives considered by the PCC were somehow incorporated into the guidance in the proposed ASU.