



Add: 128 Xixi Rd., Hangzhou China  
P.C: 310007  
Tel: (0571) 8821 6888  
Fax: (0571) 8821 6999  
Web: <http://www.pccpa.cn>

International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

15 Dec. 2010

**Exposure Draft “Leases (ED/2010/9)”**

Dear Sir or Madam:

Pan-China Certified Public Accountants Ltd. (PCCPA) is pleased to respond to the above Exposure Draft (hereinafter the “ED”).

Our comments on the specific questions raised in the ED are attached. Should you wish to discuss the content of this letter with us, please contact Yingling Shen at [syl@pccpa.cn](mailto:syl@pccpa.cn)

Yours Sincerely,

Pan-China Certified Public Accountants Ltd.

## **Appendix**

### **RESPONSE TO SPECIFIC QUESTIONS IN THE EXPOSURE DRAFT**

#### ***Leases (ED/2010/9)***

*This Appendix sets out PCCPA's responses to part of the questions indicated in the exposure draft's Invitation to Comment.*

#### **Question 5**

The exposure draft proposes that a lessee or a lessor should apply the proposed IFRS 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 IFRS? Why or why not? If not, what alternative scope would you propose and why?

#### **Reply:**

We are in general agreement with the scope exclusion in the proposal. However, we think that leases of intangible assets shouldn't be included in the scope exclusion.

First of all, according to IAS38, intangible assets include computer software, patents, copyrights, motion picture films, licenses, import quotas, franchises, marketing rights etc. Most of intangible assets belong to right-of-use assets, since leases of such intangible assets are similar with leases of right-of-use assets in a sublease in substance, we suppose that they should apply the same standard.

Secondly, in China, state owns the land proprietary rights, enterprises can only obtain the use rights. Hence, according to the China Accounting Standard (CAS), land is not recorded in land account (applying lease standard) but in intangible assets account (not applying lease standard). Among them, for self-constructing building, the land use rights and building cost are presented in two items "intangible asset-land use rights" and "fixed asset-building" separately. For purchased property, they are presented in one item. "fixed asset-building" Actually, the owner of purchase property and self-constructing building both can obtain the property ownership certificate and land use right certificate. Based on the economic substance, leases of self-constructing building and leases of purchased building have no difference in nature, includes the leases of building and use rights of land at the same time. But according to the proposal, the use rights of land of self-constructing because of being classified as intangible asset couldn't apply the lease standard, but the use right of land of purchased building because of being classified as fixed assets could apply lease standard. Hence, it would result in a situation that the same economic substance is treated by two different ways.

So, we consider that the land which has only use rights should apply lease standard. In addition, the right-of-use items which are similar with the use rights of land in intangible assets should also apply lease standard.

### **Question 7**

The exposure draft proposes that a lease contract should be considered as 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?

### **Reply:**

We agree with the proposal based on the following reasons:

1. According to the proposal, the definition of lease is “a contract in which the right to use a specified asset (the underlying asset) is conveyed, for a period of time, in exchange for consideration.” It means that the right conveyed by lease activity is only the right to use an asset, not the ownership and whole control right of the asset. When a lessee exercises the purchase options, the right to use the asset is changed to the right of ownership and whole control, so the object which is conveyed by lessor is not the right to use anymore, and such business does not meet the definition of lease in this proposal, the lease contract should be terminated. From the perspective of lessor, a lessor has already lost the ownership and whole control right of the asset, the lessor does not retain exposure to significant risks or benefits associated with the underlying asset. Thus, the lease contract should be accounted for as a purchase (by the lessee) and a sale (by the lessor) when the purchase option is exercised.
2. In substance, exercising option to purchase the underlying asset is not different with normal sale / purchase, when the purchase option is exercised, a lessee accounts for the lease contract as a purchase, we believe that it reflect the nature of the transaction or event.

### **Question 10**

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?

### **Reply:**

We agree with the proposal based on the following reasons:

1. According to the proposal, at the date of commencement of a lease, a lessee shall recognise in the statement of financial position a right-of-use asset and a liability to make lease payments, a lessor shall account for a lease in accordance with the performance obligation approach or the derecognition approach based on the detail situation, but anyway, the lessor shall recognise in the statement of financial position an asset (a right to receive lease payments) and a liability (lease performance obligation). 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, if a lessee or lessor does not remeasure assets and liabilities, then the picture which is presented by the financial statements of lessee and lessor to reflect the assets and liabilities arising from leases couldn't be matched with the fact, then it would make the relevant financial information not provide faithful representation of entity's financial position and performance.

2. According to the materiality principle of qualitative characteristics of useful financial information, information is material if its omission or misstatement could influence the decisions that users make on the basis of an entity's financial statements, and material information should be faithfully represented in financial statements. So, when the changes 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 is significant, a lessee or lessor should remeasure the assets and liabilities arising from lease transaction.