



December 15, 2010

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Members and Staff of the Financial Accounting Standards Board and the International Accounting Standards Board:

Thank you for the opportunity to comment on the Leases exposure draft. Luxottica Group S.p.A. and its subsidiaries operate in two industry segments: (1) manufacturing and wholesale distribution and (2) retail distribution. Through its retail operations, as of December 31, 2009, the Company owned and operated 5,682 locations worldwide and franchised an additional 535 locations.

Leasing is a critical element of our business model. The terms of our leases include percentage rent, term renewal options, co-tenancy clauses, and landlord funded lease incentives. We also operate optical and sunglass departments under license agreements. We are very interested in the Boards' proposed changes to lease accounting as these changes will have a significant impact on our financial statements and ongoing financial accounting operations.

Overall, we support the Boards' efforts to improve accounting for leases. However, we do not agree with some of the proposed changes to lease accounting. The following represents our views on selected questions posed in the IASB's exposure draft.

*Questions #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?*

Response: We agree with the Boards' proposal that a lessee should recognize a right-of-use asset and a liability to make lease payments. A lease conveys rights and obligations that meet the definition of an asset and liability as described in CON 6: Elements of Financial Statements and the IFRS Framework. We also agree that a lessee should amortize the right-of-use asset consistent with other tangible and definite lived intangible assets. We agree that interest expense should be recognized on the liability to make lease payments. However, we have concerns around the measurement of more complex leases – in particular regarding extensions or options, contingent rent, and those that contain service components. These concerns are discussed in more detail in our responses to questions # 6, 8 and 9.

We do not agree that an effective interest method is the proper way to recognize interest expense. This approach recognizes higher interest expense in the initial years of each lease. We do not believe that accelerated recognition matches the economics of leasing transactions in the retail industry. It is also a complete change from current accounting where rental costs are recognized on a straight-line basis. This approach will distort earnings during periods in which a significant number of new stores are opened, or after an acquisition. We believe a preferable approach would be to recognize expense on a straight-line basis over the duration of the lease term as long as no other better time pattern of physical use is known.

### *Question #3 - Short-term leases*

*(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 profit or loss over the lease term.*

*(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 profit or loss, nor derecognize any portion of the underlying asset. Such lessors would continue to recognise the underlying asset in accordance with other IFRSs and would recognize lease payments in profit or loss over the lease term (paragraph 65).*

*Do you agree that a lessee or a lessor should account for a short-term lease in this way? Why or why not? If not, what alternative approach would you propose and why.*

Response: We agree with the Boards' proposal to simplify the accounting model for short-term leases. The cost of implementing a more complex model does not justify the benefit for short-term leases. However, we recommend that the criteria to qualify as a short-term lease be expanded to those leases with initial terms of twenty-four months or less. Very few leases have a term of twelve months or less, which will limit the usefulness of this, simplified treatment. Also, please clarify in the final standard whether a lease with month-to-month terms qualifies for this simplified approach.

*Questions #4 - Definition of a Lease*

*The exposure draft proposes to define a lease as a contract in which the right to use a specified asset or assets is conveyed, for a period of time, in exchange for consideration.*

*(a): Do you agree that a lease is defined appropriately? Why or why not? If not, what alternative definition would you propose and why?*

Response: We agree with the Boards' definition of a lease. However, we have concerns about how to apply the proposed concepts to more complex leases. These concerns are discussed in more detail in our responses to questions # 6, 8 and 9.

*Question #5 - Scope exceptions*

*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.*

*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?*

Response: In the retail industry, it is common to close or relocate a store; however, a buyout may not be negotiated with the landlord. As a result, the lessee remains obligated for original term of the lease. Currently, the accounting for such leases is provided in ASC 420-10 and IAS 37. IAS 37 provides that an onerous contract shall be recognized and measured as a provision at the unavoidable cost under the contract defined as "the least net cost of exiting from the contract." ASC 420-10-25 provides further guidance on when to recognize a liability for a contract with no future benefit. A liability for costs to terminate a contract before the end of its term shall be recognized when the entity terminates the contract in accordance with the contract terms (for example, when the entity gives written notice to the counterparty or has otherwise negotiated a termination with the counterparty).

The estimation of the fair market value of a retail space is very judgmental. Retail stores with similar characteristics, such as square footage and geographic location, may command different rental payments based on the specific site within a mall. For instance, retail space located next to a department store with a strong customer base will often result in a higher rent than a site in a more remote part of the same mall. Due to the significance of these judgments and estimates, the quality of financial reporting may be impaired by applying the concepts proposed in the exposure draft.

It is not clear whether the exposure draft is meant to supercede the current accounting for onerous contracts. We modeled the financial impact of an onerous contract applying the principles in the exposure draft, compared this to current accounting and determined that the timing differed. Also, small changes in the estimated fair value of sublease income would change the timing of when these costs are recognized. We propose that leases which provide no future benefit should be excluded from the scope of the proposed lease standard. The current accounting for such leases, described in ASC 420-10 and IAS 37, should be retained.

*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?*

Response: We agree with the Boards' proposal that lessees should apply the principles in the Revenue from Contracts with Customers exposure draft to the service component when a contract contains both lease and service components and the service component is distinct. However, we believe that significant judgment will be required.

In the retail industry, license agreements are a common way of engaging a specialty retailer to operate a certain department or provide services within a large general retailer or grocery. Under these agreements, it is common for the licensor to have multiple performance obligations that include providing the space, telephone services, utilities, administrative services and the right to use the licensor's marks in advertising. However, sufficient information is not always readily available to discern the relative fair value of the lease and service components for these contracts.

Significant judgment will be required to allocate the consideration between the lease and service components of these contracts. Many of these agreements have lease components based on a percentage of sales. Please refer to our response to question #9 for our views on contingent lease payments. Due to the significance of these judgments and estimates, reasonable people could reach different conclusions for similar arrangements and the quality of financial reporting may be impaired. Thus, the notes to the financial statements will need to clearly disclose the key judgments and assumptions utilized to bifurcate the lease component of such contracts.

*Question #8 - Lease term*

*Do you agree that a lessee or 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?*

Response: We disagree with the Boards' proposal that a lessee should measure assets and liabilities arising from a lease as the longest possible term that is more likely than not to occur taking into account the effect of any options to extend the lease. We believe that a renewal option does not meet the definition of a liability under CON 6 or the IFRS Framework. CON 6 defines a liability as follows, "Liabilities are probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past (emphasis added) transactions or events." The IFRS Framework states, "An essential characteristic of a liability is that the entity has a present obligation. A distinction needs to be drawn between a present obligation and a future commitment. Liabilities result from past transactions or other past events."

Prior to its exercise, a renewal option is not a liability arising from a past event. It is a contingent liability whose existence will be confirmed by future events. Current IFRS principles do not recognize contingent liabilities. Similarly, under SFAS 5, an entity only recognizes a contingent liability when it is probable that a loss has been incurred at the date of the financial statements and the amount can be reasonably estimated. These criteria have not been satisfied until the option is exercised.

In the retail industry, the likelihood of renewal of an individual store lease requires careful consideration and is typically not estimable at lease inception. A period of time must elapse to assess whether a store's performance justifies its continued operation. Economic conditions can also have a significant impact on store performance and the decision on whether to exercise a renewal option. For these reasons, a reliable estimate of the likelihood of renewal at lease inception is not possible.

We recommend that the cash flows associated with the renewal option term should be included only when the option has been exercised. The notes to the financial statements should disclose renewal options that have been excluded from lease term due to uncertainties regarding the likelihood of renewal.

#### *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 lessor should account for contingent rentals and expected payments under term option penalties and residual value guarantees and why?*

Response: We disagree with the Boards' proposal that a lessee should measure assets and liabilities arising from a lease including contingent rentals for the full term of the lease. Many of our leases contain contingent rentals based upon store sales. We do not agree that contingent rentals fit the definition of a liability as described in CON 6 or the

IFRS Framework . Both CON 6 and the IFRS Framework define a liability as an obligation arising from a past transaction or event.

Our obligation to pay contingent rentals is not a liability at the inception of the lease; instead, it is incurred over time based on a store's performance. This arrangement fits the definition of a contingent liability, as our obligation will be confirmed only by the occurrence of one or more uncertain future events which are not estimable with sufficient reliability. Due to the significance of these judgments and estimates, the quality of financial reporting may be impaired by applying the concepts proposed in the exposure draft to contingent rentals.

Further, if contingent rentals are included in the initial measurement of right-of-use asset, the resulting lease-related expenses will not match the recognition of the sales which gave rise to this obligation and the right-of-use asset. Retail sales do not occur on a straight-line basis over the lease term.

We believe performance-based contingent rentals should be excluded from the scope of the proposed lease standard. Instead, these arrangements should continue to be accounted for under existing literature. The terms of these arrangements should also be disclosed in the notes to the financial statements.

#### *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 payment 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?*

Response: Please refer to our responses to questions #8 and 9 for our views on lease term and contingent rentals. We agree with the Boards' proposal that the assets and liabilities arising under a lease should be re-measured whenever a significant change in facts or circumstances occurs. However, it will be very challenging for retailers to implement this proposed accounting. Contingent rental payments, based on store performance, will differ from initial estimates on a regular basis. Recent store performance provides us with some insight into contingent rentals in the near term. However, store performance alone is not sufficient information to predict contingent rental on a long-term basis. Other factors, which affect store performance, include economic conditions, competitive factors and changes in the attractiveness of a particular location. Due to the large number of store leases in a retailer's portfolio, reassessment will be a significant and time-consuming effort. Please provide additional guidance on what factors would trigger a reassessment and clarify how changes in estimates associated with current or past periods should be classified in the statement of comprehensive income. It is not clear whether the

earnings impact associated with these adjustments should be presented as depreciation expense, interest expense or some other financial statement line item.

*Question #12 - Presentation*

*(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 or investment property, as appropriate, but separately from assets that the lessee does not lease? 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?*

Response: We disagree with the Boards' proposal that a lessee must present the right-to use asset separate from other tangible assets and the liability to make lease payments separately from other financial liabilities. We believe that each entity should form their own conclusion as to whether lease-related assets and liabilities should be shown separately in their statement of financial position, or combined with similar assets and liabilities, based on the materiality of the amounts and the needs of their financial statement users. The notes to the financial statements will disclose the opening and closing balances of the right-of-use asset and liabilities to make lease payments. If an entity chooses not to separately present these items on the statement of financial position, their notes should identify the financial statement lines which contain these amounts.

*(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? 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?*

Response: We propose that each entity should be permitted to choose how to disclose their leased assets and liabilities. The Boards' have recommended that lessors disclose their underlying leased asset, the receivable for the right to receive lease payments, and the lease liability separately, totaling to a net lease asset or liability, on the statement of financial position. We propose that lessors be permitted to choose either a gross or net presentation on the face of the statement of financial position based on the materiality of these amounts. The notes to the financial statements will disclose the opening and closing balances of the lessor's right to receive lease payments and lease liabilities. If an entity chooses not to separately present these items on the statement of financial position, their notes should identify the financial statement lines which contain these amounts.

*Question #13 - Statement of comprehensive income*

*Do you think that lessees and lessors should present lease income and lease expense separately from other income and expense in the profit and loss? Why or why not? If*

*not, do you think that a lessee should disclose that information in the notes instead? Why or why not?*

Response: We do not agree with the Boards' proposal that lessees must present lease expense separately from other expense in the profit and loss statement. We recommend that each entity be permitted to choose how to disclose these items in their financial statements based upon materiality. A lessee may elect to combine the amortization of right-of-use assets with depreciation of tangible assets and interest expense on the lease liability be combined with other interest expense. Similarly, we believe that lessors should not be required to present lease income separately from other revenue. The notes to the financial statements should disclose these amounts if they are not separately presented in the financial statements.

*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? 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?*

Response: We do not agree with the Boards' proposal that cash flows arising from leases must be presented separately in the statement of cash flows. Consistent with our comments above, we believe that each entity should assess whether a gross or net presentation on the statement of cash flows would be beneficial to their investors based on materiality. The notes to the financial statements should disclose this additional information if it is not separately presented in the financial statements.

*Question #16 – Transition*

*(a) The 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. 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 requirements that Board need to consider? If yes, which ones and why?*

Response: We disagree with the Boards' proposal that lessees and lessors should recognize and measure all outstanding leases as of the date of initial application using a simplified retrospective approach. This approach will result in more adverse earnings impact than a full retrospective approach. Post-implementation earnings will show a



larger amount of amortization expense and interest expense using the simplified retrospective approach compared to full retrospective treatment. This approach will distort earnings and impair the usefulness of this information to investors.

We believe full retrospective treatment of the new standard would be a better transition approach. A full retrospective transition approach would provide more accurate earnings for investors trying to predict future trends. We do not believe that a full retrospective approach will be administrative burdensome. We prefer the full retrospective approach, as it will be more reflective of the ongoing effects of the new standard.

The transition guidance states that when lease payments are uneven over the lease term, a lessee shall adjust the right-of-use asset recognized at the date of initial application by the amount of any recognized prepaid or accrued lease payments. The transition guidance should also address whether the right-of-use asset and lease payment liability should also be adjusted for the unamortized portion of initial direct costs and landlord funded leasehold incentives.

*Question #17 – Benefits and Costs*

*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?*

Response: We understand that investors believe that the lease accounting model needs improvement. But from our perspective, the benefits of the proposal will not exceed the costs. We will need to add resources, implement new processes and systems, and design internal controls to assist with management the proposed accounting. The proposed approach will require new processes as a significant amount of judgments and estimates will need to be reassessed on a regular basis. The proposal will also create new assets which will add complexity to our impairment analyses.

*Question #18 – Other comments*

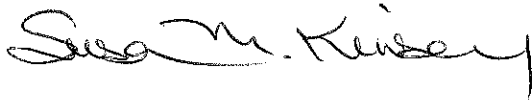
*Do you have any other comments on the proposal?*

Response: We suggest that the Boards provide further application guidance on how to assess impairment of right-to-use assets. We also recommend that the Boards converge their impairment models before the lease accounting changes become effective. We report our results under IFRS for parent company financial statements and under US GAAP for standalone subsidiary financial statements. We encourage the Boards to accelerate convergence of the impairment models so that financial results are similarly affected for both IFRS and US GAAP reporters.

We also suggest that the Boards include guidance in the exposure draft on how lessees should treat landlord funded lease incentives.

Thank you for the opportunity to share our views on this important topic.

Sincerely,

A handwritten signature in black ink that reads "Susan M. Kinsey". The signature is written in a cursive style with a large, sweeping initial "S".

Susan M. Kinsey  
AVP – Accounting Services