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Hans Hoogervorst, Chair  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH, United Kingdom

Russell G. Golden, Chair  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
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Re: File Reference No. No. 2013-270 – Proposed Accounting Standards Update (Revised) – *Leases* (Topic 842), ED/2013/6

Dear Chairman Hoogervorst and Chairman Golden:

The American Council of Life Insurers (ACLI)<sup>1</sup> appreciates the opportunity to comment on the *Leases* Exposure Drafts jointly issued by the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB).

We support the objectives of achieving convergence, simplifying lease accounting, and improving the transparency, credibility and usefulness of leasing information, such that users of financial information can gain an understanding of an entity's leasing activities. We believe this exposure draft is an improvement over the 2010 exposure draft, and appreciate that the Boards have addressed many of the concerns raised by constituents. We particularly welcome the principle-based dual model which appropriately limits cost and complexity when the lessee is not expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset. Nonetheless, we still believe that the costs to implement the proposed standard are significant and have a specific concern that for some leases, the benefits in providing the proposed information do not justify the related costs.

We have identified two possible solutions to our cost/benefit concern and we believe applying either solution would significantly reduce the costs of compliance while only marginally reducing benefits to users of financial statements. Appendix A contains detailed feedback in response to the “*Questions for Respondents.*”

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<sup>1</sup> The American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association with more than 300 member companies operating in the United States and abroad. ACLI advocates in federal, state, and international forums for public policy that supports the industry marketplace and the 75 million American Families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing more than 90 percent of industry assets and premiums. Learn more at [www.acli.com](http://www.acli.com).

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## **Solution 1: Short-Term Lease Simplified Accounting**

We appreciate that the Boards have amended the definition of a short-term lease which better aligns the cost of applying this proposal to the benefits provided to users, investors and analysts. We are also sympathetic to the Boards' rationale for not extending this exception to 2 or 3 years for all leases since it is conceivable that structuring opportunities could result in material off-balance sheet liabilities. We are still concerned, however, that certain leases such as fax machines, computers, copiers, water coolers etc., which are ancillary to an entity's operations and insignificant to its results, do not satisfy the proposed short-term lease definition. We acknowledge that the Boards already considered providing exclusion for assets that are not core to an entity's operations; however, this exclusion was considered independently from the short-term lease exclusion.

The Boards have stated in the Basis of Conclusion, BC 335, that they have consciously attempted to avoid bright-lines when determining whether leases are to be classified as Type A or Type B, yet they have established a bright-line (12-month maximum lease term) for short-term leases where an entity may elect not to apply the proposed requirements (i.e., simplified accounting similar to today's operating lease accounting). We believe a more principle-based approach (rather than a bright-line) for determining when the simplified accounting is appropriate would favorably tip the cost/benefit scale without providing restructuring opportunities to circumvent the proposed standard's intent.

A possible principle-based approach would neither distinguish between core and non-core assets nor set a bright-line maximum lease term but, instead, would provide qualitative indicators or a set of conditions to assist entities in determining when the simplified accounting is appropriate. Examples of such factors could include:

- Maximum possible lease term (simplified accounting more appropriate for shorter term leases)
- Significance of lease payments to the entity (simplified accounting more appropriate for less significant lease payments)
- Nature of leased asset relative to the company's business (simplified accounting more appropriate for leases of assets that are ancillary to the operations of an entity)

Considering these factors, companies would be able to evaluate, based on their specific facts and circumstance, when to apply the simplified accounting. Implementing the proposed guidance will result in significant costs, including system modifications, internal control and process enhancements, and human capital investments. We believe the cost of compliance would decrease significantly by extending the application of the simplified accounting, while still achieving the Boards' objectives. It may then be appropriate for companies to disclose the types of assets and rationale for determining when it applies the simplified accounting.

## **Solution 2: Separating Lease and Non Lease Components of a Contract and Modified Retrospective Transition**

Should the Boards decide not to implement Solution 1, we suggest that the Boards use the same principle-based approach described above to provide specified relief from some of the more onerous requirements, including separating lease and non lease components of a contract and modified retrospective transition.

We conceptually agree with the proposed guidance that requires separate accounting for distinct lease and service components in a contract. We are concerned, however, that entities will need to track and

analyze a large volume of leases in order to separate the non lease components, and the result of that componentization for certain leases will provide minimal benefit to users. We believe the same principle-based approach discussed above could be used to eliminate this specific requirement for certain leases in order to significantly reduce the cost of compliance, while still achieving the Boards' objectives.

Similarly, we agree that for certain long term and/or significant leases, the proposed modified or full retrospective approaches are appropriate. However, for leases such as fax machines, computers, copiers, water coolers etc., we do not believe the information provided by these transition approaches justifies the related cost. We believe it is more appropriate to apply the principle-based approach discussed above in order to exclude these types of leases from the scope of the more onerous transition accounting requirements. This solution would still require all new and/or significant existing leases to apply a retrospective approach. Without this solution, companies would be required to gather and analyze information for all leases, which would take considerable time, cost and effort while providing only marginal benefit to users.

ACLI is pleased to comment to the Boards on this matter. We hope that you will carefully consider our input and welcome your feedback and questions.

Sincerely,



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## **Appendix A - Questions for Respondents**

### ***Question 1: Identifying a Lease***

Do you agree with the definition of a lease and the proposed requirements in paragraphs 842-10-15-2 through 15-16 for how an entity would determine whether a contract contains a lease? Why or why not? If not, how would you define a lease? Please supply specific fact patterns, if any, to which you think the proposed definition of a lease is difficult to apply or leads to a conclusion that does not reflect the economics of the transaction.

We agree with the definition of a lease, and that the guidance is adequate to make a determination about whether a contract contains a lease.

### ***Question 2: Lessee Accounting***

Do you agree that the recognition, measurement, and presentation of expenses and cash flows arising from a lease should differ for different leases, depending on whether the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset? Why or why not? If not, what alternative approach would you propose and why?

Yes we believe the dual approach model of identifying Type A and Type B leases is appropriate.

### ***Question 3: Lessor Accounting***

Do you agree that a lessor should apply a different accounting approach to different leases, depending on whether the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset? Why or why not? If not, what alternative approach would you propose and why?

As discussed in question 2, yes we believe the dual approach model of identifying Type A and Type B leases is appropriate.

A large number of real estate investment entities report real estate at fair value on a recurring basis in accordance with either ASC 946 or ASC 960-325. Under this reporting model, lessors generally report rental income on an accrual or contractual basis and not on a straight-line rent basis. In these instances rental income is not reflected on a straight-line basis because the value associated with the lease is embedded in the fair value of the leased (real estate) asset as reported. To record rental income on a straight-line basis would: result in an overstatement of the value of the entity's net assets, or require an adjustment to the fair value of the real estate. The bifurcation of the fair value of the real estate asset resulting from a straight-line requirement would be confusing for financial statement readers and be inconsistent with current financial and performance reporting measurements. Notwithstanding the comments in the paragraphs BC273-BC278 of *Background Information, Basis for Conclusions, and Alternative Views*, we recommend that the Board provide additional clarification in the actual forthcoming Accounting Standards Update that would scope out applicable real estate entities from the standard or specifically permit such entities to record rental income on an accrual or contractual basis.

### ***Question 4: Classification of Leases***

Do you agree that the principle on the lessee's expected consumption of the economic benefits embedded in the underlying asset should be applied using the requirements set out in paragraphs 842-10-25-5 through 25-8, which differ depending on whether the underlying asset is property? Why or why not? If not, what alternative approach would you propose and why?

Yes we agree with the approach outlined in the guidance.

***Question 5: Lease Term***

**Do you agree with the proposals on lease term, including the reassessment of the lease term if there is a change in relevant factors? Why or why not? If not, how do you propose that a lessee and a lessor should determine the lease term and why?**

We agree that if there is a significant change in the relevant factors, the lease term should be reassessed.

However, in addressing the reassessment of options, the Basis of Conclusion (BC 171), states that “...an entity should be required to remeasure lease assets and lease liabilities as a result of changes relating to options relatively infrequently, thus reducing costs associated with reassessment...” We would like the Boards to explicitly incorporate this in the lease term discussions within the body of the final standard. This is a placement issue, which we believe will provide more clarity to preparers and auditors as the guidance is implemented.

***Question 6: Variable Lease Payments***

**Do you agree with the proposals on the measurement of variable lease payments, including reassessment if there is a change in an index or a rate used to determine lease payments? Why or why not? If not, how do you propose that a lessee and a lessor should account for variable lease payments and why?**

We broadly agree with the proposal to reassess variable lease payments.

***Question 7: Transition***

**Subparagraphs 842-10-65-1(b) through (h) and (k) through (y) state that a lessee and a lessor would recognize and measure leases at the beginning of the earliest period presented using either a modified retrospective approach or a full retrospective approach. Do you agree with those proposals? Why or why not? If not, what transition requirements do you propose and why? Are there any additional transition issues the Boards should consider? If yes, what are they and why?**

As discussed in Solution 2 above, we agree that for certain long term and/or significant leases, the proposed modified or full retrospective approaches are appropriate. However, for leases such as fax machines, computers, copiers, water coolers etc., we do not believe the information provided by these transition approaches justify the related cost. Should the Boards decide not to implement Solution 1, we believe it is appropriate to apply the proposed principle-based approach in order to exclude these types of leases from the scope of the more onerous transition accounting requirements. This would alleviate the significant financial and human capital burden of entities having to compile and evaluate a great deal of information for a large number of insignificant leases that will have ended either prior to the transition date or shortly thereafter. Applying the guidance as written and gathering and analyzing the information would take considerable time, cost and effort to report these leases upon transition while providing only marginal benefit to users.

We also request further clarification on how to treat leasehold improvements at transition.

***Question 8: Disclosure***

Paragraphs 842-10-50-1, 842-20-50-1 through 50-10, and 842-30-50-1 through 50-13 set out the disclosure requirements for a lessee and a lessor. Those proposals include maturity analyses of undiscounted lease payments, reconciliations of amounts recognized in the statement of financial position, and narrative disclosures about leases (including information about variable lease payments and options). Do you agree with those proposals? Why or why not? If not, what changes do you propose and why?

We conceptually agree with the disclosure requirements, however, we do not believe they should be mandated broadly for all entities and all industries. For the insurance industry, leases are not generally a significant activity and we therefore encourage the Board to apply principles from its disclosure framework when establishing disclosure requirements for the leases project so that entities have greater flexibility in determining what disclosures are most relevant for the users of their financial statements.

***Question 9: Nonpublic Entities (FASB Only)***

Will these specified reliefs for nonpublic entities help reduce the cost of implementing the new lease accounting requirements without unduly sacrificing information necessary for users of their financial statements? If not, what changes do you propose and why?

We believe the proposal is reasonable.

***Question 10: Related Party Leases (FASB Only)***

Do you agree that it is not necessary to provide different recognition and measurement requirements for related party leases (for example, to require the lease to be accounted for based on the economic substance of the lease rather than the legally enforceable terms and conditions)? If not, what different recognition and measurement requirements do you propose and why?

We agree with the Boards.

***Question 11: Related Party Leases (FASB Only)***

Do you agree that it is not necessary to provide additional disclosures (beyond those required by Topic 850) for related party leases? If not, what additional disclosure requirements would you propose and why?

We agree that additional disclosure is not required.

***Question 12: Consequential Amendments to IAS 40 (IASB Only)***

Do you agree that a right-of-use asset should be within the scope of IAS 40 if the leased property meets the definition of investment property? If not, what alternative would you propose and why?

IAS 40 *Investment Property* currently permits, but does not require, property held under an operating lease to be accounted for as investment property using the fair value model if it meets the definition of investment property. We believe that the current scope of IAS 40 *Investment Property* should be maintained and that the lessee should recognize the right-of-use asset or investment property according to an analysis of the underlying usage of the asset.