



September 13, 2013

Technical Director, File Reference No. 2013-270
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Re: File Reference No. 2013-270 Exposure Draft of the Proposed Accounting Standards Update (Revised) –
Leases (Topic 842)

We are writing on behalf of the Emerging Standards Committee (ESC) of the Kentucky Society of Certified Public Accountants (KyCPA). The KyCPA is the sole professional organization representing CPAs in the Commonwealth of Kentucky. Its 5,100 members are engaged in business communities throughout the Commonwealth and have a comprehensive grassroots view of the needs of businesses, ranging from large public companies to small owner-managed businesses. KyCPA's ESC consists of a group of KyCPA members organized to monitor the activities of accounting and auditing standard setters, as well as government authorities, with the objective of participating in the standards-setting process by providing thoughtful comment on developing issues.

Our comments for your consideration are as follows:

Overall Comments – We have very serious concerns whether this proposed standard meets user needs in a cost-beneficial manner or at all. The proposed standard is excessively complex, causing a substantial increase in costs to comply. Notwithstanding costs, we question whether the proposed standard improves financial reporting by providing better information to users. In particular, it is not clear that cash flows analysis is improved with the information provided by this proposed new standard.

We suggest a more modest approach to revising accounting standards for leases. We suggest the criterion for recording a capital lease be reduced to the “greater than 50%” level, representing “most” of the leased assets’ economic benefits. This can be embodied using both the economic life criterion (lease term to asset life) as well as the economic value criterion (present value of minimum lease payments to asset value). We believe this threshold has substantial conceptual support in current standards, with symmetry to consolidation criteria; that is, the primary beneficiary or majority owner is the party with “most” of the risks and rewards associated with the entity under consideration. Recording a capital lease should be similar insofar as considering whether the lessee controls most of the economic benefits of the leased asset.

If this approach is used, the overwhelming majority of existing lease accounting guidance would not need to change. This would reduce costs and make the standard easier for users to understand.

We believe that necessarily recording all lease payments as assets/liabilities is tedious, extraneous and makes the financial statements more difficult to understand for users. We also question the theory and consistency for such a requirement as other executory contracts and similar payment commitments are not recorded in such a manner.

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It is also noted the concepts of capital and operating leases do not change for tax return purposes. This will require entities to create a second system for financial statement compliance, while retaining the prior system for tax purposes, thereby significantly increasing costs of maintaining two complex systems. These consequences should not be ignored by the Board in its deliberations, and should not be subordinated to any objectives of convergence with IFRS.

We believe the basic approach outlined above provides simplification, conceptual consistency, enhanced user understandability and represents an improvement in existing lease accounting standards.

Other specific comments are as follows (assumes the Board does not follow our overall approach as noted above):

Type A versus Type B approach – We agree with a dual income statement approach whereby Type B leases would be on a straight line basis. However, we believe the proposed approach for non-property leases versus property leases is flawed. The criterion included in the proposal notes “whether a lessee is expected to consume more than an insignificant portion (“MTIP”) of the economic benefits” of the non-property leased asset. The MTIP criterion relates to both economic life and value. The criterion for property leases is different: “major part” for economic life and “substantially all” for value.

We believe these three new criteria – insignificance, major part and substantially all – represent unnecessary complexity that will cause confusion. The lack of any authoritative guidance defining terms such as “insignificant” and “major part” will likely contribute to inconsistency and misunderstandings. We are concerned such a condition will naturally cause the SEC, and to some degree the PCAOB, to require further action be taken.

Additionally, we are unaware of any conceptual reason why property and non-property leases should be treated differently for purposes of lease classification. Further, the MTIP criterion for non-property leases is simply too “low” to warrant financing presentation.

We believe the criterion (for Type A versus B) should be the same for both property and non-property leases, allowing preparers, auditors and users to more easily understand and consistently apply it. Further, we suggest the appropriate criterion to be applied is the “greater than 50%” of the economic benefits of the leased asset, as further described in the “Overall Comments” section on page one. If the lessee consumes “most” of the economic benefits of the leased asset, the Type A approach is appropriate. Similarly, if “less than most” is consumed, a Type B, or straight line approach, is appropriate. This criterion should be applied equally to both property and non-property leases.

Further, we wish to convey a concern related to federal grant/contract reimbursements and federally approved overhead/indirect cost rates. Under the Federal Acquisition Regulation, entities can include rental expense within reimbursement requests and overhead/indirect cost rates, but generally cannot include interest costs. The Type A approach could result in costs previously allowable as rental expense becoming unallowable (and hence excluded from reimbursement or overhead/indirect rates) due to the proposal’s requirement that the unwinding of the discount on the lease liability be recognized as “interest” within the income statement. This should be considered by the Board when evaluating the Type A versus B criterion.

Our suggested approach would improve operationality and understandability of lease accounting standards.

Question 9: (Nonpublic Entities) – We agree with all of the specific reliefs granted to nonpublic entities and believe they will help reduce costs.

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Question 10: (Related Party Leases) – We agree with the Board’s determination that the recognition and measurement requirements for all leases should be applied by lessees and lessors that are related parties based on the legally enforceable terms and conditions of the lease. Full and clear disclosure is critical so that users understand the arrangements in place.

Effective date considerations for nonpublic entities – We suggest the effective date for nonpublic entities be two years after the effective date for public entities. We believe this deferral will provide valuable time that will reduce the cost of implementation for such entities as well as allow for various operational issues to be addressed. We do not believe financial statement users for private companies will be adversely affected by such a deferral as such users generally have a working knowledge of the nature and existing accounting for the entity’s leasing transactions.

Thank you very much for considering our thoughts.

Sincerely,

A handwritten signature in blue ink that reads "Glenn Bradley". The signature is written in a cursive style.

Glenn Bradley, CPA, Chair
On behalf of the Emerging Standards Committee
Kentucky Society of CPAs