



금융감독원 FINANCIAL SUPERVISORY SERVICE

Corporate Accounting System Office
38 Yeoui-Daero, Youngdeungpo-Gu, Seoul 150-743 REPUBLIC OF KOREA
Telephone: +82-2-3145-5039. Facsimile: +82-2-3145-5085 E-mail: abjyc@fss.or.kr

September 13, 2013

Mr. Hans Hoogervorst
Chairman
International Accounting Standards Board
20 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Re: ED/2013/5 Leases

Dear Chairman Hoogervorst:

I am pleased to submit to the IASB our comment on the revised Exposure Draft *Leases* (ED/2013/6 *Leases*). The enclosed comments to the questions raised in the ED/2013/6 *Leases* represent the official views of the Financial Supervisory Service, Korea's integrated financial supervisor. For follow-up on our comments, please contact me (abjyc@fss.or.kr) or Ms. Ju Soyeon (syju@fss.or.kr), Associate, Corporate Accounting System Office.

Respectfully yours,

Choe Jin-yeong
Chief Accountant / Deputy Governor

Enclosure: FSS Comments on ED/2013/6 *Leases*

Cc: Mr. Ko Inmook, Director, Corporate Accounting System Office
Mr. Sung Gilhyun, Assistant Director, Corporate Accounting System Office

Comments on ED/2013/5 *Leases*

Question 1: identifying a lease

Do you agree with the definition of a lease and the proposed requirements in paragraphs 6.19 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.

Responses to Question 1

We do not agree with ED/2013/6 *Leases*.

While the exposure draft proposes to classify leases as Type A and Type B based on the underlying asset, it only provides a single definition of a lease: a contract that conveys the right to use an asset for a period of time in exchange for consideration. We believe it is important and necessary for the proposal to provide definitions for each type of leases if this classification were to result in different accounting for different type of leases.

In addition, we note that there is no clear guidance available on accounting for leases in which consideration provided in exchange for the right to use an asset includes financial instruments. For instance, under a *Jeonse* contract in Korea, a lessee makes a lump-sum deposit, instead of paying monthly rents, in exchange for the right to use a house and the entire amount of the deposit is returned to the lessee at the end of the lease term. Thus, a deposit made under a *Jeonse* contract would be considered a financial instrument under IFRS, which defines a financial instrument as a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Thus, the proposed standards should be able to provide clear guidance on how to account for a contract which includes both a lease component and a financial instrument component.

According to the proposal, a contract must use an identified asset to be defined as a lease. However, even if a leased asset does not meet the criteria for identified asset, it would still meet the definition of a liability. Thus, additional guidance is necessary to account for such cases. If a contract that does not meet the definition of a lease is subject to other standards, this should be noted in the proposal (e.g., in the basis for conclusions).

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?

Responses to Question 2

We do not agree with ED/2013/6 *Leases*.

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According to the proposed definition of a lease, a lease causes all lessees to acquire the right to use an underlying asset regardless of the lease type. Thus, it would represent a logical inconsistency on the part of the proposal to require different accounting, including amortization of the right to use an asset, for different type of leases.

Instead, we suggest applying the straight line method for all types of leases. Since the right to use an underlying asset is similar in nature to intangible assets, straight line amortization can be used for leases. But we also note that users should still be allowed to use of another systematic basis if it is more representative of the pattern in which the lessee expects to consume the right-of-use assets' future economic benefits.

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?

Responses to Question 3

We do not agree with ED/2013/6 *Leases*.

The proposed lessor accounting standards could give rise to a problem when a leased asset is subsequently subleased to a third party. Because the proposal requires the lessor to continue recognizing the underlying asset, the lessor in a sublease would be put in a situation where he/she is required to amortise an asset which no longer exists. Thus, exclusion criteria should be provided in the proposal to allow the lessor who subleases an underlying asset in a Type B lease to derecognize the right-of-use asset.

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 28-34, which differ depending on whether the underlying asset is property? Why or why not? If not, what alternative approach would you propose and why?

Responses to Question 4

We partially agree with the proposals of ED/2013/6 *Leases*.

While the proposed principle classifies leases into two types on the basis of the expected consumption of a portion of the economic benefits embedded in the underlying asset, there is no clear objective guidance or criteria to evaluate the consumption of "insignificant" portion. This leaves a room for subjective judgment

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and could potentially result in situations where leases with similar terms are accounted for differently.

In our view, there is little or no practical benefit in classifying leases into different types under the proposed definition of a lease (i.e., the conveyance of the right to use an asset): it would be more beneficial to treat all lease assets equally.

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?

Responses to Question 5

We agree with ED/2013/6 *Leases*.

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?

Responses to Question 6

We agree with ED/2013/5 *Leases*.

Question 7: transition

Paragraphs C2-C22 state that a lessee and a lessor would recognise 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?

Responses to Question 7

We agree with ED/2013/6 *Leases*.

Question 8: disclosure

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Paragraphs 58-67 and 98-109 set out the disclosure requirements for a lessee and a lessor. Those proposals include maturity analyses of undiscounted lease payments; reconciliations of amounts recognised 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?

Responses to Question 8

We partially agree with ED/2013/6 *Leases*.

The proposal requires leases to be classified based on the nature of the underlying assets. Thus, additional disclosure requirements would be necessary where the classification is not performed based the nature of underlying assets. For instance, where a lease of property is classified as Type A lease or a lease of a non-property asset as Type B, the lessee/lessor should be required to disclose the accounting policy used or other quantitative information, such as the scale of the lease and the schedule of lease payment.

Question 12: Consequential amendments to IAS 40

The IASB is proposing amendments to other IFRSs as a result of the proposals in this revised Exposure Draft, including amendments to IAS 40 Investment Property. The amendments to IAS 40 propose that a right-of-use asset arising from a lease of property would be within the scope of IAS 40 if the leased property meets the definition of investment property. This would represent a change from the current scope of IAS 40, which permits, but does not require, property held under an operating lease to be accounted for as investment property using the fair value model in IAS 40 if it meets the definition of investment property.

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?

Responses to Question 12

We agree with ED/2013/6 *Leases*.

The right-of-use asset arising from a lease of property has similar underlying economics as the ownership of such property. Thus, including a right-of-use asset where the lease property meets the definition of investment property in the scope of IAS 40 seems logical and in line with the overall approach taken by the proposed standards.