



Madrid, 13 September, 2013
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir/Madam,

Re: Leases

Repsol is very pleased to provide comments on the Exposure Draft *Leases* (ED2013/6), issued by the IASB on 16 May 2013.

Further information about the Repsol Group and its activities is available on our Website: www.repsol.com.

If you would like to discuss any of the points described in this letter, please do not hesitate to contact us by e-mail to normativacontable@repsol.com.

Thank you for your attention.

Yours sincerely,

Emilio Linares-Rivas Balius

Accounting Policy and Compliance Manager

GENERAL COMMENTS

Although we acknowledge the huge effort in terms of time and resources that the Boards have expended in the Lease Project with the objective of providing a more complete and understandable picture of the leasing contracts of an entity, and that the Exposure Draft Leases (ED 2013/6) operationally simplifies several key issues of the 2010 Exposure Draft, we are not convinced that the proposed standard represents a substantial enough improvement to financial reporting for the extremely costly implementation effort (accounting and reporting systems, processes, internal controls, training...) and further on-going effort required to reassess lease terms and variable lease payments. We believe that IASB should carefully reconsider the incremental benefits of the proposals.

It is not at all clear for us that the proposed recognition and measurement provisions improve comparability, forecasts of cash flows, or quality of information, or result in reduced costs for stakeholders who use the information for leases currently provided in notes to the financial statements.

We believe that the proposals would increase complexity and even may reduce transparency and comparability across companies, for example in the case of the accounting for joint operations which are very common in the Oil&Gas industry.

On the other hand, we believe that the proposed dual measurement approach may affect the ability of the users of the financial statements to understand which rights are and which are not recognised in the statement of financial position and how they are measured. The inclusion of a dual measurement approach seems to be an indicator that the right-of-use model may not fit all the arrangements in scope of the proposals. We consider that in order to avoid any future inconsistency it would be necessary to finish the Conceptual Framework Project before to introduce a new concept like the proposed right-of-use model for leases.

For all the reasons stated above, we do not support with the recognition and measurement criteria proposed in the Exposure Draft *Leases* (ED 2013/6). We do believe that in order to ensure the provision of all the necessary information and to make it relevant, meaningful and useful to the users, the improvement of the disclosures in notes to the financial statements currently provided under the requirements of IAS 17 *Leases* would be a more suitable way to achieve a substantial and cost-effective improvement of the financial reporting in relation to lease arrangements.

RESPONSES TO IASB QUESTIONS

Please, take into consideration that the following responses are provided on the assumption that the IASB proceeds to issue a new Lease Standard based on the proposals in the Exposure Draft *Leases* (ED2013/6), and subject to our “General Comments” stated above.

Question 1: identifying a lease

This revised Exposure Draft defines a lease as “a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration”. An entity would determine whether a contract contains a lease by assessing whether:

- (a) fulfilment of the contract depends on the use of an identified asset; and
- (b) the contract conveys the right to control the use of the identified asset for a period of time in exchange for consideration.

A contract conveys the right to control the use of an asset if the customer has the ability to direct the use and receive the benefits from use of the identified asset.

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.

We believe the lease identification criteria should be clarified in regard to several issues such as the assessment of whether fulfilment of the contract depends on the use of an identified asset, whether the contract conveys the right to control the use of identified asset and the accounting for joint operations.

- Assessment of whether fulfilment of the contract depends on the use of an identified asset. The ED sets that *a physically distinct portion of an asset can be an identified asset. However, a capacity portion of an asset cannot be an identified asset because it is not physically distinct from the remaining capacity of the asset.* Although we do agree with the proposal in the ED, we believe that further guidance would be required in situations where, for example, an entity has a firm commitment for 70% of the capacity of an asset (for example, a pipeline) and in addition, a preferential right or enforceable option over 30% of the remaining capacity of the asset, in order to determine if the fulfilment of the contract depends on the use of an identified asset.
- Assessment of whether the contract conveys the right to control the use of an identified asset. The proposals in the ED introduce apparent differences from current lease standards when assessing the right to control the use of an

identified asset and it seems that certain contracts that are currently accounted for as leases would not be considered leases under the proposed criteria (for example, certain take-or-pay and outsourcing contracts). In this sense, we believe that further guidance would be very useful when assessing contracts (for example, drilling rig contracts) which require significant on-going involvement by personnel representing the asset owner to conduct all day-to-day operations and maintenance of the asset. In order to avoid diversity in practice and ensure comparability between companies, we think that it would be necessary to provide further guidance in relation to whether the substance of a contract has more economic attributes in common with a 'service arrangement' (which is not a defined term in IFRSs) than a lease transaction; and when or how, an entity would consider its involvement in determining its ability to make decisions that most significantly affect the economic benefits to be derived from the asset during the contract term.

- Accounting for Joint Operations. Joint arrangements are very common in the oil&gas industry activities. Under IFRS 11 a joint operator shall account for the assets, liabilities, revenues and expenses relating to its interest in a joint operation in accordance with the IFRSs applicable to the particular assets, liabilities, revenues and expenses, this practice lead to a high degree of comparability of the financial statements of the partners. As an example, when entering to in a joint arrangement which is not articulated through a separate entity (i.e. joint operation), the "operator" arranges for the services and then bills each partner proportionately to their share of costs. The proposed standard could lead to an asymmetry across partners in a specific project, since an operator entering in a lease arrangement will generally be required to reflect the whole right-of-use asset on its balance sheet, whereas other non-operating joint partners would recognise (as an expense or as a cost directly attributable to the construction of other asset) only the proportionate costs billed by the operator as an expense since they do not have the "control" of the underlying leased asset and this is a necessary requirement to recognize the right-of-use asset. Additional asymmetries would arise also both in the profit and loss accounts as well as in the cash flow statements. Therefore, we believe that the proposed standard will reduce the transparency and comparability across oil&gas companies, even for those involved in the same joint arrangement.

Other issue that we believe the IASB should take into consideration is the accounting for operating lease expenses when are directly attributable to the construction of other asset (i.e. property, plant and equipment) during the construction period. For many companies the retrospective initial application of the proposals would involve a high degree of operational difficulty, particularly in relation to operating lease expenses which have been capitalized in the past as directly attributable costs to the construction of an asset. In addition, we do not believe that the recognition of these costs as a right-of-use asset, rather than as direct costs attributable to the construction of an asset, would provide better information to investors and other users of financial statements.

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?

We believe that the Type B accounting model (i.e. single lease expense model for lessees) is based on a measurement notion linked to the lease liability that we do not believe to be consistent with the proposed right-of-use model. We do not think that the subsequent measurement of the right-of-use asset under Type B model reflects the pattern of consumption of the asset, and more important, that it provides relevant and useful information to the users of the financial statements.

We believe this lack of conceptual basis is an indicator that an improvement of the disclosures currently provided under the requirements of IAS 17 would be a more adequate way to achieve a substantial and cost-effective improvement of the financial reporting of lease contracts.

Subject to the comments stated above, if the IASB proceeds to issue a new Lease Standard based on the proposals in the ED, we think that the Type B model may be a 'pragmatic' way to avoid front-loaded profile of total lease expense.

In addition there are other issues within the proposals that would require significant judgement in order to apply the proposed criteria in the ED and that would require additional guidance. For example, according to the ED leases of assets that are not property would be classified as Type A leases, *unless one of the following two criteria is met (a) The lease term is for an insignificant part of the total economic life of the underlying asset (b) the present value of the lease payments is insignificant relative to the fair value of the underlying asset at the commencement date.* The proposals do not provide a definition for the term 'insignificant' in order to assess the exception criteria for classifying leases of assets other than property. Other examples of concepts that would require additional guidance are: the concept of 'property' (which is not a defined term in the ED); the determination of which is the 'primary asset' in a lease that includes the rights to use both a property asset and a non-property asset.

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?

Subject to our views stated above in our 'General Comments', if the IASB issues a new Lease Standard based on the proposals in the ED, although we could agree with the proposed Type B accounting model for lessors, we do not agree with the asymmetrical accounting treatment between lessors and lessees proposed in the ED for Type B leases. This asymmetry is equivalent to the use of a different unit of account by lessees and lessors. In our opinion, this fact provides additional support for the view stated above that the right-of-use model is not appropriate for Type B leases for lessees either.

In addition, we believe that the proposed model for Type A leases is too complex and would be difficult to understand by the users of the financial statements.

Again, we believe this lack of conceptual basis and additional complexity provide support for the view that the improvement of the disclosures currently provided under the requirements of IAS 17 would be a more adequate way to achieve a substantial and cost-effective improvement of the financial reporting of lease contracts.

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?

In our opinion, and subject to our views stated above in our 'General Comments', the fact that for most leases of equipment the consumption of the underlying asset's economic benefits is significant, while this is not the case for 'property', justifies a different classification between Type-A and Type-B leases.

We believe that, although generally the conclusion regarding the classification of a lease arrangement would be the same without the presumption based on the nature of the underlying asset, the inclusion of such a presumption may result in simplification and cost saving for preparers. This would be useful taking into account that the proposals in the ED would lead to a too complex and time-consuming implementation and on-going processes for preparers.

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?

Subject to our views stated in our 'General comments', we welcome the option for not applying the lease requirements to short-term lease contract.

On the other hand, in regards to the proposal that the lease term should include options to renew if the lessee has 'significant economic incentive' to exercise these options, it would require further application guidance in order to help preparers in this assessment. In this sense, we believe that it would be preferable to include a rebuttable presumption which indicates that if an entity has reasonable doubts about the existence of a "significant economic incentive", this fact is evidence that it does not exist.

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?

Subject to our views stated in our 'General comments', we agree with the inclusion of variable payments based on an index or rate, however we believe that it would be necessary to provide further guidance on the concept of "in substance fixed payments" due the wide range of possible types of variable payments that may qualify as "in-substance fixed payments".

Variable consideration is being discussed in the Revenue Recognition Project and it is also included in the Agenda of the IFRS Interpretation Committee in regards of contingent payments on the acquisition of tangible and intangible assets. We consider that this is a relevant issue and the final conclusions about the initial recognition and subsequent measurement across all these projects should be consistent.

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?

Subject to our views stated above in our 'General Comments', if the IASB issues a new Lease Standard based on the proposals in the ED, the IASB should not underestimate the difficulty in gathering all historical data required to apply not only a full retrospective approach, but also the proposed modified retrospective approach, and consider granting additional practical reliefs as well as providing a reasonable period when setting the effective date.

Question 8: disclosure

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?

The ED proposes a number of new and detailed disclosures, some of which are a direct consequence of excessively complex accounting model (as an example, the reconciliations of balances for Type-B leases). The fulfilment of these new disclosure requirements shall entail incurring high costs and a major effort in terms of time and resources. We fail to see the consistency in proposing the implementation of a fundamental change in the lessee accounting model and increase the disclosure burden at the same time. In this sense, we believe it would be appropriate the IASB consider the alternative of refocusing the Lease Project to a revision and improvement of the current disclosures in notes to the financial statements in order to eliminate those proposed disclosures directly motivated by the proposed accounting model and to enable the improvement of those disclosures which are required by users of financial statements as well as to achieve a substantial and cost-effective improvement of the financial reporting in relation to lease arrangements.

Question 9 (FASB-only): nonpublic entities

To strive for a reasonable balance between the costs and benefits of information, the FASB decided to provide the following specified reliefs for non-public entities:

- (a) To permit a non-public entity to make an accounting policy election to use a risk-free discount rate to measure the lease liability. If an entity elects to use a risk-free discount rate, that fact should be disclosed.*
- (b) To exempt a non-public entity from the requirement to provide a reconciliation of the opening and closing balance of the lease liability.*

Will these specified reliefs for non-public 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?

N/A

Question 10 (FASB-only): related party leases

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?

N/A

Question 11 (FASB-only): related party leases

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?

N/A

Question 12 (IASB-only): 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?

Although we do not account for investment property using the fair value model in IAS40, we believe that the application of this model to right-of-use assets may raise cross-cutting issues.