



September 13, 2013

Russell G. Golden
Chairman
File Reference No. 2013-270
Financial Accounting Standards Board
401 Merritt 7
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Hans Hoogervorst
Chairman
Reference ED/2013/6
International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

Re: Exposure Draft *Proposed Accounting Standards Update (Revised)*—*Leases (Topic 842)*

Dear Chairman Golden and Chairman Hoogervorst:

The Commercial Real Estate Finance Council (“CRE Finance Council”) appreciates this opportunity to comment on the revised proposals on lease accounting, *Leases* (the “Proposal”), issued jointly by the Financial Accounting Standards Board (“FASB”) and the International Accounting Standards Board (“IASB”) (together, the “Boards”).

The CRE Finance Council is the collective voice of the entire \$3.1 trillion commercial real estate finance market. Our principal missions include setting market standards, facilitating market information, and providing education at all levels. Because our membership consists of all constituencies across the entire CRE finance markets, the CRE Finance Council has been able to develop comprehensive responses to policy questions that promote increased market efficiency and investor confidence.

First, on behalf of our members, the CRE Finance Council commends the Boards’ collaborative efforts to review and improve upon the accounting standards for leases. The Proposal is a significant improvement over prior guidance on lease accounting for both lessors and lessees. As the Proposal rightly recognizes, real estate accounting is indeed different from other types of accounting and must be treated accordingly. We therefore applaud the progress reflected in the Proposal and appreciate your consideration of the concerns of our members.

We do have some concerns and reservations with the current Proposal, however, and respectfully offer our thoughts and suggestions for your consideration in the comments that follow.

Cost-Benefit Analysis

We are concerned that the proposed leasing standards may result in substantial costs to businesses and lack sufficient meaningful benefits for investors. At a minimum, it is unclear to us whether the potential benefits from this Proposal will ultimately outweigh the significant burdens – in time and money – it will impose on the preparers and users of financial statements and, more broadly, the real estate finance industry.

Moreover, it is difficult to predict what effect the proposed accounting changes might have on leases and lease-ups, in particular. Indeed, making significant shifts to the accounting for lease transactions – including changes to existing recognition, measurement, presentation, and disclosure requirements – could very well have a negative impact on the real estate industry as a whole. That is particularly true today, given the overall instability of the market.

For these reasons, we ask that before finalizing and implementing the Proposal, the Boards specify the benefits expected under the Proposal, and whether those benefits will outweigh the costs created by the proposed changes.

Short-Term Leases

Under the Proposal, both lessees and lessors may elect to use a simplified accounting model under which short-term leases of twelve months or less need not be recognized on the balance sheet. Lessees may elect to recognize short-term lease payments in profit or loss on a straight-line basis, whereas lessors could elect to recognize short-term lease payments in profit or loss on either a straight-line basis or other systemic basis that better represents how income is earned on the particular asset.

Any lease with a possible term of more than twelve months, and any lease that contains a purchase option, would be capitalized.

We support this approach. We agree with the Boards' decision to allow lessors and lessees the option to apply a simplified accounting model to short-term leases. However, due to the amount of work and lack of existing systems to track leases, we believe it would be more appropriate to apply a principle-based approach where the accounting would be dependent on the length of the lease term, the nature of the leased asset and the materiality of the lease payment to the entity. This approach could eliminate the time required under the proposed guidance for leases on business's fax machines and photocopiers, which would require time and system set up for immaterial information.

Lease Reassessments

The Proposal would require that lessees and lessors perform ongoing reassessments of lease assets and liabilities to reflect changes to lease terms and lease payments. Such a requirement would be a dramatic change from today's lease accounting practices, the impact of which is not entirely clear. What is quite clear, however, is that forcing lessees to continually monitor their lease investments for specific changes to the lease term or lease liability, which could trigger reassessment of the leases, is burdensome, unnecessary, and difficult to apply. In practice, mandating such lease term reassessments would present significant and costly operational challenges and complexities.

In addition to being impractical and administratively burdensome, requiring reassessment of the lease term based on certain new facts or circumstances is unlikely to yield useful information to users. Rather, the proposed requirement would be likely to confuse lessees and increase volatility, because lessees would be required to make more judgment calls about uncertain future events. Indeed, in deciding whether to exercise options to extend, lessees would be required to project the extent to which a variety of factors might be important several years down the road. It is, for example, difficult to determine at the beginning of a ten-year lease whether there would be an economic benefit to extend the lease term at that time. Additionally, it would be burdensome to continue to assess whether an economic benefit exists. We believe that the continued monitoring is not productive time spent by preparers or beneficial information for the users of the financial statements. We would suggest that the lease should be set up on the initial term only and adjusted when actual extension is exercised.

Moreover, given that most commercial property leases contain a Consumer Price Index ("CPI") or other inflation factor to help protect lessors from inflation on multi-year leases, this reassessment requirement based on a CPI or other escalation clause would be time-consuming and expensive for lessees – particularly commercial lessees that lease hundreds or thousands of properties compounding the administrative effort further.

We ask that this proposed requirement be removed from the Proposal and that differences from the assumptions used at set up be recorded as period expenses.

Fair Value Accounting

Large amounts of real estate are managed through insurance company separate accounts, open-end commingled funds or single investor pension funds that report net assets value at fair value under current guidance. These real estate entities report lease income on an accrual or as-earned basis rather than on a straight-line basis, because the value associated with the lease is imbedded in the fair value of the leased real estate asset. The bifurcation of the fair value of the real estate asset resulting from a straight-lined requirement would be time consuming and confusing for the financial statement users. We believe the Boards did not intend for lessors of fair value real estate to change their current method of accounting under the proposed guidance and we ask for additional clarifying language.

Comparability Concerns

Discount rates in a lease would be used to determine the present value of the lease payments and the related liability. The Proposal would result in measurement inconsistencies among different companies' borrowing rates, because if the lessee cannot determine or does not know the rate the lessor charges, the lessee must use its own incremental borrowing rate. Because lessees often may not know the rate the lessor charges and thus use their own incremental borrowing rate, there will be inconsistencies among the borrowing rates of different companies. For many property leases, for example, a high creditworthy company may end up reporting a larger right-of-use asset than a less creditworthy company for the same lease asset with the same annual lease expense. In analyzing peer companies' balance sheets, this puts higher creditworthy borrowers at a disadvantage in a comparison situation.

Disclosures

The Proposal would impose a number of new disclosure requirements on both lessors and lessees that we believe are unnecessary. Lease disclosure requirements are already quite extensive and detailed, and the new proposed rules would go much further. Although we appreciate the importance and effectiveness of good disclosure, we do not believe that imposing additional disclosure requirements is necessarily good for investors, nor is it the same as *improving* the disclosures that are currently required.

Because the Proposal treats leases as debt instruments, lessor and lessee disclosures should be treated the same as any other debt instrument. That is, they should be geared toward describing the investment or property, its value, and any changes in value or liabilities for mortgages, capitalized leases, and other long-term debt. The new proposed disclosure requirements, however, go well beyond what the Boards require for other instruments, and we believe they would fail to provide any added practical or useful information for investors related to an entity's lease-related cash flow, financial condition, or overall activities.

Moreover, the complexity of the proposed disclosure requirements would pose a real burden of time and resources on businesses, particularly smaller entities, without any added clarity to investors or benefits to users of financial statements.

Transition Period

The Boards have not yet proposed a date on which the Proposal would take effect. Because the Proposal includes significant changes regarding the accounting for leases that could have broad implications for entities' finances and overall operations, however, we believe a transition period of at least a few years is essential. Many of the proposed changes, for instance, would require businesses, users, and preparers of financial statements to undertake internal overhauls of their real estate accounting systems, as well as force many companies to create accounting systems for tracking leases other than real estate leases.

Accordingly, we recommend a transition period of at least three years for public entities and four years for private entities before any new rules take effect.

Conclusion

The CRE Finance Council and our members applaud your efforts and the improvements contemplated in the current Proposal. We appreciate your consideration of our views on the issues of concern to us, as described above.

Please do not hesitate to contact us at your convenience if you have questions or if any additional information would be helpful.

Sincerely,

A handwritten signature in black ink, appearing to read "S.M. Renna", with a long horizontal flourish extending to the right.

Steven M. Renna
President and CEO