



December 4, 2020

Technical Director
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856-5116

File Reference No. 2020-700

The Accounting Principles Committee of the Illinois CPA Society (“Committee”) appreciates the opportunity to provide its perspective on the *Proposed Accounting Standards Update, Leases (Topic 842) Targeted Improvements* (herein referred to as the “Update”). The Committee is a voluntary group of CPAs from public practice, industry and education. Our comments represent the collective views of the Committee members and not the individual views of the members or the organizations with which they are affiliated. The organization and operating procedures of the Committee are outlined in Appendix A to this letter.

The Committee supports the Board’s efforts to improve Topic 842. Our responses to the questions in the Update are included below.

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We appreciate the opportunity to provide our comments and observations on the proposed Update and would be pleased to discuss them with the Board members or the FASB staff at your convenience.

Sincerely,

William Keirse, CPA
Chair, Accounting Principles Committee

Matt Mitzen, CPA
Vice Chair, Accounting Principles Committee

Issue 1: Sales-Type Leases with Variable Lease Payments

The Committee believes the amendments in the proposed Update will address day-one loss issues for lessors under Topic 842 by requiring lessors to classify and account for leases as operating leases as they did in similar circumstances under Topic 840. However, the Committee believes, as indicated in previous comment letters on proposed accounting standard updates for ASC 606 and ASC 842, a preferable approach would be to require lessors to apply Topic 606 for sale-lease type leases. The Committee believes economically similar arrangements should have similar accounting outcomes. While such an approach would clearly require lessors to estimate all variable lease payments in order to apply the recognition requirements of Topic 606, subject to the constraint, we disagree with the Board's view, as noted in paragraph BC10, that doing so would introduce additional cost and complexity for the lessor's accounting. The Board acknowledges in paragraph BC13 that lessors would have that information available in evaluating expected profitability of a lease arrangement. It is also unclear to the Committee why the inconsistent treatment of variable lease payments by lessees and lessors would be problematic when there is the same issue with asset purchases that include variable consideration (the seller estimates and recognizes variable consideration as part of the selling price, subject to the constraint, but the purchaser does not recognize variable consideration until it is probable it will make a payment and the amount is reasonably estimable). As a result, the Committee believes applying Topic 606 to sales-type leases with variable consideration, which the Board notes in paragraph BC10 is a "conceptually better solution," is a preferable approach.

If the Board decides not to include sales-type leases in the scope of Topic 606, the Committee supports the proposed changes, but believes the "predominant" threshold of a majority of lease payments needing to be variable payments not dependent on a reference index or a rate to be treated as an operating lease should be revised. The proposed majority threshold would still exclude arrangements with variable lease payments that comprise a significant but not majority component of the expected cash flows, which could still result in lessors recognizing an immediate loss on a transaction expected to be profitable. The Committee believes the threshold should include those leases as operating leases where the present value of the fixed lease payments plus unguaranteed residual value interest at the end of the lease is less than the lessor's current net book value and the lessor expects to earn a profit on the contract through expected variable lease payment cash flows.

Issue 2: Option to Remeasure Lease Liability – Lessee Only

The Committee supports the proposed amendments to provide an entity-wide accounting policy election to remeasure lease liabilities for changes in a reference index or rate on which payments are based to further reduce differences between US GAAP and IFRS and increase their comparability. We note the proposed language in paragraph 842-20-35-4A is similar to that in IFRS 16 paragraph 42, whereby the discount rate is not updated at the date of remeasurement unless the change in lease payments results from a change in the floating interest rates, and in that case, a lessee shall use a revised discount rate that "reflects changes in the interest rate." We recommend the Board clarify and provide additional examples to illustrate that is meant by a "revised discount rate that reflects changes in the interest rate". For example, consider a five-year building lease where the first annual payment is fixed and payments for years two through five are adjusted for changes in LIBOR. If LIBOR increases 100bp at the beginning of year 2, is the revised discount rate updated to reflect the 100bp increase only? Alternatively, if the payments in years 2 through 5 are adjusted

for changes in CPI only, presumably the discount rate is not updated. If that is the case, the Board should clarify that point in its example in paragraph 842-10-55-231A.

Issue 3: Modifications Reducing the Scope of a Lease Contract

The Committee agrees with the Board on the principle that if the economics of the remaining lease components are unaffected by the early termination of one or more separate lease components in a lease contract then the entity should not need to reassess the classification of or adjust its accounting for the remaining lease components and therefore not apply the guidance in paragraph 842-10-29-9 through 25-18 to the entire contract. However, the Committee believes the Board should provide further examples and guidance on the application of paragraph 842-10-25-8B(c) and what payments should be included in the analysis. For instance, using example 18 in ASC 842-10-55-177 on a modification that decreases the scope of a lease from 10,000 square feet of office space to 5,000 square feet, as amended by the Update, it is unclear to us if this example qualifies for the simplified approach proposed in the Update. The total payments for the remaining 5,000 square feet in this example (\$68,000 annually which increases 5% each year thereafter) approximates one-half (53%) of the total payments under the original agreement (\$127,600 at the beginning of year 6 increasing 5% each year thereafter). Would this be “substantially the same” under the Update? What if example 18 was modified to include a termination penalty amount based on the decrease in market rates for leasing up the space the lessee is returning? What impact does operating costs have on the conclusion assuming (a) the lease payment covers all of the cost (gross lease) and (b) the lessee pays operating costs in addition to rent (net lease)?

APPENDIX A
ACCOUNTING PRINCIPLES COMMITTEE
ORGANIZATION AND OPERATING PROCEDURES
2020-2021

The Accounting Principles Committee of the Illinois CPA Society (Committee) is composed of the following technically qualified, experienced members appointed from industry, education and public accounting. These members have Committee service ranging from newly appointed to more than 20 years. The Committee is an appointed senior technical committee of the Society and has been delegated the authority to issue written positions representing the Society on matters regarding the setting of accounting standards. The Committee's comments reflect solely the views of the Committee and do not purport to represent the views of their business affiliations.

The Committee usually operates by assigning Subcommittees of its members to fully study and discuss exposure documents proposing additions to or revisions of accounting standards. The Subcommittee ordinarily develops a proposed response that is considered, discussed and voted on by the full Committee. Support by the full Committee then results in the issuance of a formal response, which at times includes a minority viewpoint. Current members of the Committee and their business affiliations are as follows:

Public Accounting Firms:

Large: (national & regional)

Ryan Brady, CPA	Grant Thornton LLP
Ashley Carboni, CPA	KPMG LLP
Michael Couillard, CPA	Baker Tilly Virchow Krause LLP
Matthew Denton, CPA	Sikich LLP
Jason Eaves, CPA	Crowe LLP
William Keirse, CPA (Chair)	Ernst & Young LLP
Melissa Lynch, CPA	Plante Moran, PLLC
Jason Plourde, CPA	Grant Thornton LLP
Darshana Raigaga, CPA	BKD LLP
David Wentzel, CPA	Crowe LLP

Medium: (more than 40 professionals)

Danielle Martin, CPA	Porte Brown LLC
Jeffery Watson, CPA	Miller Cooper & Company Ltd

Small: (less than 40 professionals)

Peggy Brady, CPA	Selden Fox, Ltd.
Brian Kot, CPA	Cray Kaiser Ltd CPAs
Matthew Mitzen, CPA (Vice Chair)	Bronswick Benjamin P.C.

Educators:

Mollie Adams, CPA	Bradley University
John Hepp, CPA	University of Illinois at Urbana-Champaign

Industry:

John Bercerril, CPA	Elkay Manufacturing
Jeffrey Ellis, CPA	FTI Consulting, Inc.
Michael Maffei, CPA	GATX Corporation
Thomas Masterson, CPA	Medix
Elizabeth Prossnitz, CPA	Consultant
Lisa Sezonov, CPA	Northern Trust
Richard Tarapchak, CPA	Reynolds Group Holdings
William Wang, CPA	Union Tank Car Company
Daniel Wilfong, CPA	Ansira, Inc.

Staff Representative: Rafael Wiesenber, CPA Illinois CPA Society