



Letter of Comment No: 13
File Reference: FSPFAS13-B
Date Received:

August 18, 2005

Lawrence W. Smith
Director, TA&I--FSP
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

RE: FSP FAS 13-b—Accounting for Rental Costs Incurred During a Construction Period

Dear Mr. Smith:

The National Retail Federation (NRF) and its Financial Executives Council (Council) welcome the opportunity to share its views on the Proposed FSP FAS 13-b—Accounting for Rental Costs Incurred During a Construction Period (FAS 13-b). NRF is the world's largest retail trade association, with membership that comprises all retail formats and channels of distribution including department, specialty, discount, grocery, chain restaurants, catalog, Internet, and independent stores, as well as the industry's key trading partners of retail goods and services. The Council is comprised of senior financial executives from the nation's leading retailers who are experts in retail industry accounting practices.

NRF submitted comments to the EITF on Issue No. 05-3, *Accounting for Rental Costs Incurred During the Construction Period* in advance of their meeting on June 16, 2005. In that letter, dated June 10, 2005, we detailed our position as to why capitalization of rental costs during the construction period is supported under existing GAAP literature. In the interest of brevity, we will not repeat the points made in that letter. Rather, we will focus our comments on a few additional pragmatic points, which are outlined below.

The SEC Has Signaled Their Acceptance of Existing Practice

We understand that the Securities and Exchange Commission (SEC) has signaled its acceptance of capitalizing rental costs incurred during a construction period under certain circumstances. They did so in recognition of current practice and interpretations of existing guidance. We ask the FASB to follow the SEC's lead for the reasons stated by the SEC staff in addition to the following considerations.

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Frequent Accounting Changes Lead to Confusion in the Marketplace

NRF understands and supports the need for evolving guidance that responds to emerging business models and financial transactions. We also understand the need to modify or append existing guidance in order to clarify accounting treatment. However, we also believe this must be balanced with the practical implications of changing practices. How much value does the change add? Will it lead to more transparent financial statements? Does it raise more questions than answers? It is well known that the retail industry, among others, issued a significant number of restatements earlier this year as a result of more refined interpretations of existing GAAP, including interpretations on capitalizing rent in the build out period. To change that interpretation, yet again, could lead to even more restatements adding to the confusion, and possibly leading to a loss of credibility in our financial reporting process. Those affected by these changes include shareholders and other users of the financial statements, as well as management, software developers and other service providers.

Those affected also include a wide variety of industries, including retail, restaurant, hotel, and building owners, all of whom express concern and confusion over the FASB's differing opinion from that of the EITF and SEC.

Control of the Store Does Not Necessarily Mean it Can Open for Business

The FASB has said that the recognition period should begin when the lessee gains control of the property; the notion being that at that point the lessee has full control over when to open for business. But that is not always the case. The construction period can last several months to several years for reasons beyond the control of the retailer. For example, it is possible that a store is structurally ready to open but the mall is not yet completed. In that case the retailer cannot open for business. To treat the lease cost as a period cost in this example does not make economic sense to us. We believe the more appropriate treatment would be to capitalize the cost as you would other development costs.

Inconsistent Treatment of the Same Economic Transaction

Another complication with FAS 13-b exists due to accounting inconsistencies that may arise from two leases being structured differently.

Gross Lease. In a gross lease agreement, the insurance, real estate taxes, maintenance, and utilities are rolled into the fixed lease cost. Under FSP FAS 13-b, the entire cost would be treated as lease costs and expensed during the construction period.

Triple Net Lease. In a triple net lease agreement, insurance, real estate taxes, maintenance, and utilities are the direct responsibility of the lessee and thus not rolled into

the fixed lease cost. Under current GAAP, the lessee would capitalize the real estate taxes incurred during construction as allowed under GAAP.

While the economic model is the same for the two facilities, the P&L will reflect very different treatment. NRF feels that these inconsistencies are an undesirable effect of FAS 13-b and will lead to further comparability difficulties in the marketplace.

FASB Plans to Address Lease Accounting as a Whole in the Future

FASB Chairman Robert Herz has stated that lease accounting is a priority and will be addressed in the near future. Accounting for rental costs incurred during a construction period will certainly be addressed as part of the larger discussion. NRF recommends that the SEC's guidance on rental costs stands until lease accounting as a whole is addressed by the FASB. Issuing new guidance now in the form of FAS 13-b, only to make changes in the future, just adds to the confusion and is an inefficient use of resources.

Transition Date

FSP FAS 13-b is scheduled to become effective for the first reporting period beginning after September 15, 2005. FSP FAS 13-b was released on July 19, 2005. Such a quick turnaround does not provide adequate time for our members to assess the impact of the change on its leasing strategies, systems development, and other financial metrics. If FAS 13-b is issued as written, NRF feels that the effective date should be no earlier than the beginning of the next fiscal retail year, as most other guidance stipulates.

NRF thanks the FASB for its consideration of the retail industry's concern about this important issue and welcomes any opportunity to further explain the rationale behind our position.

Sincerely,



Carleen C. Kohut
SVP and Chief Financial Officer