



December 14, 2010

Technical Director
Financial Accounting Standards Board
401 Merritt 7
Norwalk, Connecticut 06856

International Accounting Standards Board
First Floor
30 Cannon Street
London
EC4M 6XH
United Kingdom

RE: File Reference No. 1850-100

Dear Members of the FASB and IASB:

The National Retail Federation (NRF) welcomes the opportunity to comment on the Financial Accounting Standards Board (FASB) and International Accounting Standards Board's (IASB) Proposed Accounting Standards Update, Leases (ASC Topic 840) issued on August 17, 2010. As the world's largest retail trade association and the voice of retail worldwide, the National Retail Federation's global membership includes retailers of all sizes, formats and channels of distribution as well as chain restaurants and industry partners from the U.S. and more than 45 countries abroad. In the U.S., NRF represents the breadth and diversity of an industry with more than 1.6 million American companies that employ nearly 25 million workers and generated 2009 sales of \$2.3 trillion.

NRF supports the FASB and IASB's decision to address lease accounting and agrees with the Boards' decision to recognize the right-of-use asset and the corresponding liability to make lease payments on the balance sheet. However, certain requirements in the proposed model create unnecessary complexity and impose significant administrative burden for retailers, without generating substantial benefits to financial statements users. We ask the Boards to consider the following areas of concern and our suggestions for improvement that we believe will reduce the burden of compliance while achieving the overall objective.

Question 4: Definitions

In the final standard, we ask for more clarity around definition of the terms "commitment date", "initial measurement date", and "commencement date" and their application. Similar to the additional guidance that was issued with FAS 123(R) related to the definition of "grant date" for stock-based compensation, we believe it would be helpful to provide practical examples and workable definitions of each of those terms and their application, and that all dates should be defined such that there is clarity around when each occurs. For example, defining "commitment date" as

“the earlier of the date of the lease agreement and the date of commitment by the parties to the lease agreement” invites unnecessary complexity and documentation, since the date of commitment by the parties is subject to potential interpretation. In addition, we believe that “commencement date” should be defined consistent with the guidance in ASC 840, which clarifies that recognition of rent expense begins when the lessee takes possession of the space.

Question 4: Embedded Leases

We have two areas of concern regarding the notion of embedded leases.

First, we believe executory (or ancillary) costs identified in a lease (real estate taxes, maintenance, landscaping, snow removal, etc.) should be excluded from the Exposure Draft. If these costs are not identified separately in the lease but can be quantified by the landlord, they should similarly be excluded.

Second, retailers may enter into service agreements as part of their business (i.e., alarm systems, logistics providers, delivery trucks, and landscaping). A strict reading of the Exposure Draft might suggest the equipment component of this type of service agreement be treated as an operating lease. We do not agree. We believe the leased equipment is incidental to the service and therefore recommend the costs associated with these types of agreements should be treated as period costs, outside the scope of the Exposure Draft.

Question 8: Lease Term

Existing U.S. GAAP (ASC 840) requires option or renewal periods to be included in the lease term when it is reasonably assured they will be exercised. Retailers have a strong preference that this definition of lease term not change since, in most cases, companies have no legal obligation to exercise renewal periods. When recording a right-of-use asset on its books, a company is essentially accounting for the economic value of the underlying asset. Renewal options, in and of themselves, do not add to the economic value of a leased space. Retailers therefore believe that unless there is a financial penalty for non-renewal, the rental payments associated with renewal options should only be considered in determining the basis of the right-of-use asset when exercise of the renewal option is reasonably assured (i.e., significant capital investment is made in the leased space during the initial term or upon notification to the landlord of the intent to exercise the renewal option). Retail lease agreements also often include “kick-out”, or early-exit clauses, which allow the tenant to exit the lease in certain situations (i.e., the landlord fails to comply with stated conditions of the lease or sales projections are not met). Similar to our recommended treatment of renewal options, kick-out clauses should only serve to reduce the right-of-use asset when exercised or otherwise communicated to the landlord.

To arrive at the estimated lease term, the Exposure Draft suggests performing a probability analysis. We are concerned this approach will yield improbable results since the calculated value could be a number that is unrealistic in retail leasing (i.e., a ten year lease with consecutive five year renewal options produces an estimate of 17.5 years). In these instances, the Exposure Draft allows rounding up or down to a “normal lease term” but we question how this drives a better result than the current allowed language. We believe the current GAAP approach to defining a lease term would be significantly easier to execute and provide a more accurate result. This is particularly true for retailers, some of whom manage more than 2,000 leases. Performing a probability analysis based on future expectations is neither productive nor cost-justified in this instance. An alternative to including the incremental lease payments associated with renewal options in determining the basis of the right-of-use asset would be to disclose the cost of the renewal options alongside the 5-year

minimum rent disclosure. In the event that the Boards insist on including renewal options in the lease term, NRF recommends using a “more likely than not” approach or a best estimate of lease term.

When negotiating a lease, both parties recognize economic conditions may change, which could result in either non-acceptance of optional lease term or a full renegotiation of the existing lease. Retailers structure their lease agreements to provide flexibility to react to operating results (i.e. kick-out clauses, terms, etc.). Therefore, current GAAP, which provides that renewal options be considered only if reasonably assured, is most representative of the true underlying economic value of the lease. In addition, this approach will ease many adoption concerns for retailers who otherwise believe it will be necessary to evaluate real estate leases on a case-by-case basis since very few leases are structured the same.

In some instances, retailers will want to change or renegotiate certain terms of a lease, occasionally resulting in an entirely new lease. NRF asks for clarification in the final standard on how a renegotiation resulting in a new lease would be accounted for, similar to current ASC 840 guidance on what constitutes a new lease versus a new agreement on an existing facility.

Question 9: Contingent Rent

Contingent rent is typically based on sales productivity and is often due in addition to base rent. For these reasons, NRF believes contingent rent is a period cost and should not be considered in determining the basis of the right-of-use asset, since a retailer’s sales productivity in a leased space is not relevant to the economic value of the space. In addition, projecting sales is very difficult, particularly over the entire period covered by a lease, due to factors both within (i.e., product, merchandise assortment, marketing, etc.) and outside of (economic, demographic changes, etc.) a retailer’s control. Because of the high-level of judgment required, sales projections that underlie contingent rent estimates could result in comparability issues between retailers, will result in continuous changes in the value of the right-of-use asset, and may result in misleading financial statements. In addition, we believe this leads to a financial statement disconnect since retailers would be required to record a liability for a revenue stream that cannot yet be recognized. As an alternative, at inception, the present value of the right-of-use asset should be established based upon the stated minimum rent in the lease. Any contingent rent paid would be recognized in the income statement in the period incurred and disclosed in the footnotes.

If contingent rent must be included, only the initial term should be considered, and the underlying sales estimates should be based on a retailer’s best judgment, rather than a weighted average probability-based calculation. A probability-based approach is overly burdensome for retailers who by nature manage a multitude of leases and does not necessarily yield a more accurate result. The Exposure Draft requires periodic updates if material changes occur. Therefore, the best approach is to allow companies to use their best estimate and adjust if material changes in estimates occur.

In addition, the guidance is not clear regarding the types of contingent rent included in the scope of the Exposure Draft. For example, many retailers pay in-lieu contingent rent, which is defined as an alternate rent amount in lieu of the stated minimum rent plus ancillary costs. In-lieu contingent rent is generally lower than minimum rent and is usually the result of a negotiated rent reduction for a specified period of time. Some leases also provide for overage contingent rent, which is defined as additional rent above the stated minimum rent, and is due when sales exceed a specified threshold defined in the lease agreement. In any case, NRF believes all contingent rent should be excluded from consideration in determining the right-of-use asset. If, however, it is to be included we ask for further clarification.

Question 10: Ongoing Reassessment

The proposed guidance states reassessments would be necessary if significant changes in facts or circumstances have occurred. The term “significant” should be better defined in the final standard. If renewal options and contingent rent are not considered at inception, as we suggest above, compliance with the reassessment requirement will be considerably less difficult. If not, the inclusion of these items and the related probability weighted average analyses will result in a higher likelihood of revisions/reassessments. This would impose a major burden for retail companies due to the volume of leases they manage. If our suggested changes to renewal options and contingent rent are not included in the final standard, we believe reassessments should only be required annually or when material changes occur, with material changes defined.

Question 15: Disclosures

The amount of required disclosure is excessive, and is indicative of the problems this standard presents for comparability among retailers, given the inherent difficulty involved with projecting future sales for contingent rent and the probability analysis suggested for determining lease term as related to renewal periods. This problem could be remedied if some of the suggestions recommended above are addressed in the final standard.

If renewal options, contingent rent and probability analyses are eliminated, disclosure should be less burdensome; however, specific disclosure areas that require clarification are:

- 1) Initial direct cost (IDC) disclosure requirement: are dollar amounts required or the business' policy on treating IDC?
- 2) 12 month lease term disclosure: are dollar amounts required or something else?

Reducing the disclosure requirements for quarterly reporting would make compliance with the final standard less burdensome. We do not feel it is necessary to complete a full reconciliation each quarter, particularly since systems are not yet developed to assist with the reconciliation. In place of the full reconciliation, companies could report any material changes since the last 10K filing, consistent with existing quarterly disclosure rules.

Question 16: Timing and Adoption

Retailers manage a vast number of leases. The complexity of managing these leases and complying with the final standard will require a sophisticated software system. While major service providers for our industry are working to develop a software solution, these products will not be available until the final standard is issued. In turn, until the software is available, retailers will have a difficult time complying with the complexities of the standard. We therefore ask that adequate time be given between issuance of the final standard and the adoption date. A date before 2014 should not be considered.

Question 16: Impairment

The current Exposure Draft does not explain how previous impairments of assets should be treated in the transition. Retailers believe the most appropriate treatment is to capture previous impairments as a cumulative effect upon adoption.

The Exposure Draft states that the leased asset is to be part of the total carrying value of the store subject to impairment in accordance with Topic 350 and it would be based on the undiscounted cash flows of the store. We ask FASB to provide clarity on whether assets and liabilities would be netted as is current practice for goodwill under Topic 350.

Further, we question how leases which have been accrued for under the cease-use criteria would be treated in transition. For example, assume a lease was accrued for under the current restructuring guidance 1 year prior to effective date of new lease rules. We believe the cease-use date should be the basis for the calculation rather than making the adjustment to the earlier period for ease of transition.

Question 18: Other Comments Deferred Rent Credits and Construction Allowances

There is confusion on the adoption, transition and ongoing accounting for deferred rent credits and construction allowances. Retailers agree with the proposed guidance of netting the existing deferred rent credits with the asset at transition, since existing leases would use the simplified retrospective approach to determine the asset and liability value.

In addition, we believe construction allowances should be netted against the minimum rental payments due during the initial term of the lease when determining the basis of the right-of-use asset, so the combined value of the lease-related assets (comprised of the right-of-use asset and the cash/receivable related to the construction allowance) equals the liability recognized on day one. This would be consistent with the current view that construction allowances represent a reduction of rent expense/payments due under the lease.

We ask the Boards to provide clear guidance in the final standard with regard to whether changes need to be made to current accounting for construction allowances and how this should be handled in the transition.

Separately, payments made from lessees to lessors for certain improvements need to be addressed as to how to include in the cash flow model (e.g. are such payments a reduction of the lease liability and related asset, or are such payments a separate prepaid asset).

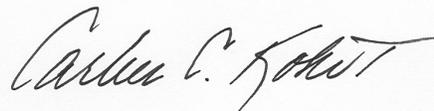
Incremental Borrowing Rate

Clarification is needed on the calculation of the incremental borrowing rate. Specifically, we request clear guidance on the date the rate should be determined. Retailers believe it makes sense to use the possession date as the date the rate is locked in. This is consistent with current practice – rent is recognized on the date retailers are given access to the leased space.

Another area of confusion is how the incremental borrowing rate should be determined if companies face a tight credit market where financing is not available. The current Exposure Draft requires quotes on issuing financing with the same terms, size, risk exposure, etc. In the current tight credit market, some retailers are concerned they could not obtain financing with the same terms as in the lease. In the absence of such data, we recommend using a company's internal cost of capital.

As previously stated, NRF agrees with the Boards' decision to recognize the right-of-use asset and the corresponding liability to make lease payments on the balance sheet. While we agree with this overall objective, we feel the discussed modifications and clarifications are needed to ease the burden of compliance. NRF thanks the FASB and IASB for their consideration of our comments and suggestions and welcomes any further discussion on the topic.

Sincerely,

A handwritten signature in black ink, reading "Carleen C. Kohut". The signature is written in a cursive style with a large initial "C" and a long horizontal stroke at the end.

Carleen C. Kohut
SVP and Chief Financial Officer