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Submission via website

5 November 2010

The Technical Director  
International Accounting Standards Board  
30 Cannon Street  
London  
EC4M 6XH  
England

Joint Submission from:  
Alpine Energy Ltd  
Counties Power Limited  
Eastland Network Ltd  
Horizon Energy Distribution Ltd  
Mainpower NZ Limited  
Marlborough Lines Ltd  
PowerNet Ltd  
Top Energy Ltd  
Unison Networks Ltd  
Wellington Electricity Ltd

Dear Sir / Madam

### **Response to Exposure Draft 2010/9 Leases**

We welcome the opportunity to respond to the above Exposure Draft ('ED').

This submission has been prepared on behalf of 10 of the Electricity Distribution Businesses ("EDBs") of New Zealand, as listed above.

Our responses to the specific questions raised in the ED are attached below in Appendix 1. Before addressing these, we wish to make some observations of a more general nature on the overall direction of the International Accounting Standards Board's (the "IASB's" or "Board's") leases project.

Broadly speaking EDB's have lease agreements for office equipment and property leases.

The submitters vary considerably in size and at the smaller end of the scale turnover is lower than \$10m. All of the submitters prepare full NZ IFRS compliant financial statements and all are audited under the legislative mandate of the New Zealand Auditor-General.

EDB's in New Zealand typically do not have lease arrangements with a significant value, but the quantum in number is significant and therefore compliance with the Exposure Draft is expected to at a significant cost to the preparers of financial statements.

Over the past ten years there has been a growing commitment to technical compliance and to ensuring that financial statements are accurate and all adjustments are made regardless of whether they are material or not. Immaterial adjustments are generally reported to audit committees and if relevant to the wider sector through to the Auditor-General.

We do not support the proposals in the ED which requires lessees to recognise a right-of-use asset and corresponding liability for lease arrangement on the basis that the cost of compliance with the ED outweighs any benefits. The costs include the preparation of the lease calculations, plus the impact on deferred taxation and any consolidation adjustments that will be required.

Further we note:

- We note that the proposed accounting treatment for leases will be inconsistent with the current accounting for non-lease executory contracts, such as supply contracts.
- The ED does not provide an appropriate outcome where the substance of the lease arrangements are simple short term leases of equipment where the risk and rewards of ownership are not transferred to the lessee.

We propose that the exemptions for short term leases are extended to cover a wider range of lease agreements, where the costs of preparation outweigh the benefits.

We would be happy to discuss our concerns with you. Please contact me if you require any further information.

Yours faithfully



Geoff Hoare (on behalf of the 10 submitters)  
Company Secretary  
Marlborough Lines Limited

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### **Question 1 – Lessees**

*(a) Do you agree that a lessee should recognise a right-of-use asset and a liability to make lease payments? Why or why not? If not, what alternative model would you propose and why?*

*(b) Do you agree that a lessee should recognise amortisation of the right-of-use asset and interest on the liability to make lease payments? Why or why not? If not, what alternative model would you propose and why?*

(a) We do not agree with the proposed treatment to recognise a right-of-use asset and liability for all lease agreements for the following reasons:

- The additional cost burden of preparation outweighs any benefits for the submitters. In many cases the submitters have relatively small turnover and limited resources and the cost of compliance on the preparer will be significant as a proportion of the total available resources. The benefit to users will be minimal, if indeed positive at all.
- This proposed treatment may significantly alter the face of the statement of financial position, but will not reflect the substance of these types of transactions, where the risks and rewards are not transferred to the lessees. In many instances, the nature of the payment is not a financing arrangement; rather, it is a payment to use an asset for a specified period of time.
- The recognition of a right-of-use asset and a liability to make lease payments for lease arrangements will be significantly different to the accounting for non-lease executory arrangements. We do not understand why there should be such a difference in the accounting treatment between a lease arrangement and non-lease executory arrangements.
- Our financial statement readers will observe a right-of-use asset and an obligation measured at different values. It is very difficult for users of the financial statements to understand what the net asset or liability represents. In our view the net position does not represent movements in the value of the business, particularly when the nature of the lease arrangements are not in substance financing arrangements.

Our proposal is to extend the definition of short term leases beyond the current definitions within the ED so that it encompasses a wider range of lease agreements to mitigate the costs of compliance. The extension of the accounting treatment applied to short term leases would target lease agreements that are immaterial to the entities financial statements and where the nature of the agreement is not a funding agreement.

### **Question 8: Lease term**

*Do you agree that a lessee or a lessor should determine the lease term as the longest possible term that is more likely than not to occur taking into account the effect of any options to extend or terminate the lease? Why or why not? If not, how do you propose that a lessee or a lessor should determine the lease term and why?*

- We have significant concern regarding whether entities would be able to appropriately estimate lease terms, particularly for renewals in the distant future. The

definition of the lease term is likely to give rise to significant areas of subjectivity that could have significant variable impact on the balance sheet.

- Where it has been determined that the lease arrangement is a financing arrangement we believe that the lease term should be the period in which the lease is non-cancellable by the lessee.

**Question 17 – Benefits and costs**

*Paragraphs BC200-BC205 set out the boards' assessment of the costs and benefits of the proposed requirements. Do you agree with the boards' assessment that the benefits of the proposals would outweigh the costs? Why or why not?*

The above points will require a significant level of attention and time to implement. This is not considered an efficient use of resource where only simple short-term leasing arrangements exist, which do not require such complex accounting.

Similarly, under the changes proposed by the ED, the presentation in the financial statements will be more complex than under the existing guidance. This will require the users of the financial statements to take extra time and attention to interpret the information, which is not considered an efficient use of resource where only simple leasing arrangements exist.

The differences between lessee and lessor accounting give rise to the likelihood that consolidation adjustment will be required and the cost of performing this exercise should not be underestimated.

Further we note that the divergence between accounting and taxation rules on lease accounting will add additional costs to the preparation of income tax computations and deferred tax computations.

We are concerned that the proposals may lead to a change in the way that leases are recognised for taxation purposes in New Zealand in the future, which will cause significant confusion between those that prepare NZ IFRS compliant financial statements and those that apply current NZ GAAP.