



United States Steel Corporation
600 Grant Street,
Pittsburgh, PA 15219-2800

December 15, 2010

via email: director@fasb.org

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

File Reference No. 1850-100 Proposed Accounting Standards Update – *Leases (Topic 840)* (“the Exposure Draft”)

Technical Director:

United States Steel Corporation (U. S. Steel) appreciates the opportunity to provide comments on the above referenced Exposure Draft. We agree with the goal of providing users with a complete and understandable picture of an entity’s leasing activities. However, we have concerns with some of the proposals contained in the Exposure Draft, as well as the administrative complexity and costs that companies will face if these changes are mandated.

Our total operating lease expense in 2009 was less than one percent of our cost of sales. Since the cost of our leasing transactions is immaterial to our overall financial statements, we do not believe that the costs associated with the implementation of the proposals would be outweighed by the benefits to financial statement users. Under the proposed guidance, we would report an asset and liability on our balance sheet for everything from buildings to copiers to portable toilets. This is not only impractical, but also is of little value to a financial statement user.

We do not believe that lease accounting should be simplified into one model under which all leases are capitalized, as is proposed for lessees. Our concern is supported by the inability to justify a single model for lessors, which has resulted in the proposal to continue a dual model for lessors. As both a preparer and user of financial statements, we recommend retaining the current lease accounting model which provides for operating and capital leases and believe that the current annual disclosure requirements for operating leases provide sufficient information to assess operating lease commitments. However, we have provided our input to the questions in the Exposure Draft as it currently stands.

Question 1 – Lessees

- (a) Do you agree that a lessee should recognize 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 recognize amortization 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?

Our main concern is that the proposed new standard will not reflect the intent of the parties or the substance of the lease transaction. While operating leases under existing standards give the lessee the right to use the leased asset, that right does not convey ownership or control of the asset. For example, a leased asset is not available to the lessee to pledge as security nor does the lessee have the ability to modify a leased asset (for example, to undertake construction on a leased building) without the consent of the lessor. Therefore, we do not feel that operating leases should result in an asset on the balance sheet. Furthermore, companies have several obligations, such as obligations under take or pay contracts, unconditional purchase obligations, and other executory contracts that do not require recognition on the balance sheet. We view operating leases as similar obligations that should not be recorded on the balance sheet. We recommend retaining the current lease accounting model which provides for operating and capital leases.

If the final standard is issued with the guidance as currently written within the Exposure Draft, we agree that the lessee should recognize amortization of the asset and interest on the liability.

Question 3: Short-term leases

This exposure draft proposes that a lessee or a lessor may apply the following simplified requirements to short-term leases, defined in Appendix A as leases for which the maximum possible lease term, including options to renew or extend, is 12 months or less:

- (a) At the date of inception of a lease, a lessee that has a short-term lease may elect on a lease-by-lease basis to measure, both at initial measurement and subsequently, (i) the liability to make lease payments at the undiscounted amount of the lease payments and (ii) the right-of-use asset at the undiscounted amount of lease payments plus initial direct costs. Such lessees would recognize lease payments in the income statement over the lease term (paragraph 64).**
- (b) At the date of inception of a lease, a lessor that has a short-term lease may elect on a lease-by-lease basis not to recognize assets and liabilities arising from a short-term lease in the statement of financial position, nor derecognize any portion of the underlying asset. Such lessors would continue to recognize the underlying asset in accordance with other Topics and would recognize lease payments in the income statement over the lease term (paragraph 65).**

(See also paragraphs BC41–BC46.)

Do you agree that a lessee or a lessor should account for short-term leases in this way? Why or why not? If not, what alternative approach would you propose and why?

As we have stated in our response to Question 1 above, we do not feel that operating leases should result in the addition of an asset on the balance sheet. This is particularly true for short-term leases where the substance of the lease transaction is simply providing the lessee with the right to use an asset for a period of time, but does not convey ownership or control of the asset. It is highly likely that we will have one week or one month leases that would need to be tracked under the new model, but which would never appear on our balance sheet since they are so short in nature. At every plant location we have equipment such as small mobile equipment for

maintenance jobs under short-term leases. As stated earlier, under the proposed guidance, we would report an asset and liability on our balance sheet for everything from buildings to copiers to portable toilets. We do not believe that grossing up the balance sheet for these types of leases adds much value to the users of financial statements as these leases are not material enough to impact their economic decisions. It would be administratively burdensome and impractical to identify and track each of these leases. We believe that annual expense disclosures for short-term leases would provide sufficient information to financial statement users regarding the magnitude of short-term leases.

Question 6: Contracts that contain service components and lease components

Do you agree with either approach to accounting for leases that contain service and lease components? Why or why not? If not, how would you account for contracts that contain both service and lease components and why?

We believe that the methodology used to account for embedded leases in service contracts should remain consistent with current methodology formerly contained in EITF 01-08 (now ASC Topic 840).

Question 7: Purchase options

This exposure draft proposes that a lease contract should be considered terminated when an option to purchase the underlying asset is exercised. Thus, a contract would be accounted for as a purchase (by the lessee) and a sale (by the lessor) when the purchase option is exercised. Do you agree that a lessee or a lessor should account for purchase options only when they are exercised? Why or why not? If not, how do you think that a lessee or lessor should account for purchase options and why?

We agree that both a lessee or a lessor should account for purchase options only when they are exercised.

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 do not agree that the lease term should be the longest possible term that is more likely than not to occur taking into account the effect of any new options to extend or terminate the lease. The majority of our leases have options to extend or terminate the lease. The determination of the longest possible lease term that is more likely than not to occur would be highly subjective and could change many times prior to the end of the lease term based on business and economic conditions that exist at the time of reassessment. If we initially predict that we will exercise an option to extend the lease and subsequently do not extend the lease, we will have overstated our assets, liabilities, and expense in the early years of the lease. This will result in a credit being recorded in our income statement at the time that we do not extend the lease and could result in income statement volatility throughout the life of the lease as reassessments are made.

Assessing each lease for the longest possible term that is more likely than not to occur as currently proposed would be administratively burdensome, as we would be adding time and effort to review each lease. Additionally, we believe that the subjectivity involved in the determination of the lease term will lead to diversity in practice and create difficulties from an audit perspective. We recommend that the lease term be the stated term in the contract.

Question 9: Lease payments

Do you agree that contingent rentals and expected payments under term option penalties and residual value guarantees that are specified in the lease should be included in the measurement of assets and liabilities arising from a lease using an expected outcome technique? Why or why not? If not, how do you propose that a lessee or a lessor should account for contingent rentals and expected payments under term option penalties and residual value guarantees and why?

Do you agree that lessors should only include contingent rentals and expected payments under term option penalties and residual value guarantees in the measurement of the right to receive lease payments if they can be reliably measured? Why or why not?

We do not agree that contingent rentals should be included in the measurement of assets and liabilities from a lease using an expected outcome technique. It is not logical to us to recognize an asset and liability based upon a contingency if the amount is not estimable. We also note that there is inconsistent treatment between how lessees and lessors should treat contingent rentals and expected payments under term option penalties and residual value guarantees in the Exposure Draft. We recommend that contingent rentals only be included in the initial measurement of the lease asset and liability if the payments can be reliably measured, as the Exposure Draft suggests for lessors.

Question 10: Reassessment

Do you agree that lessees and lessors should remeasure assets and liabilities arising under a lease when changes in facts or circumstances indicate that there is a significant change in the liability to make lease payments or in the right to receive lease payments arising from changes in the lease term or contingent payments (including expected payments under term option penalties and residual value guarantees) since the previous reporting period? Why or why not? If not, what other basis would you propose for reassessment and why?

While we understand the rationale for lessees and lessors remeasuring assets and liabilities arising under a lease when changes in facts and circumstances indicate that there has been a significant change from the previous reporting period, this requirement would cause us to incur additional costs that we do not believe would be offset by the benefits to financial statement users. In order to ensure that the reassessment process is consistent throughout the company, we would have to educate and train numerous individuals and develop an information system to capture and track necessary details to support reassessing lease terms and payment estimates as facts and circumstances change across the company, which would result in significant cost.

Question 12: Statement of financial position

- (a) Do you agree that a lessee should present liabilities to make lease payments separately from other financial liabilities and should present right-of-use assets as if they were tangible assets within property, plant and equipment, but separately from assets that the lessee does not lease? Why or why not? If no, do you think that a lessee should disclose this information in the notes instead?**

While we do not agree with the proposed model, if we had to adopt the proposed guidance, we do not believe that a lessee should change the presentation in the balance sheet to present the liability arising from lease payments separately from other financial liabilities and present the right-of-use asset separately from other tangible assets that the lessee does not lease. We believe that the addition of several new line items would confuse financial statement readers. We recommend that the amounts of the lease liability and the right-of-use asset be disclosed in the notes to the financial statements similar to the current disclosure requirement to separately disclose assets under capital lease.

Question 13: Income Statement

Do you think that lessees and lessors should present lease income and lease expense separately from other income and expense in the income statement? Why or why not? If not, do you think that a lessee should disclose that information in the notes instead? Why or why not?

We do not see a benefit from presenting lease income and lease expense separately on the income statement. We recommend that the amounts of lease income or expense be disclosed in the notes to the financial statements.

Question 14: Statement of cash flows

Do you think that cash flows arising from leases should be presented in the statement of cash flows separately from other cash flows? Why or why not? If not, do you think that a lessee or a lessor should disclose this information in the notes instead? Why or why not?

We do not see a benefit from presenting cash flows arising from leases separately on the statement of cash flows. We recommend that the cash flows arising from leases be disclosed in the notes to the financial statements.

Question 15: Disclosure

Do you agree that lessees and lessors should disclose quantitative and qualitative information that:

- (a) identifies and explains the amounts recognized in the financial statements arising from leases; and**
- (b) describes how leases may affect the amount, timing and uncertainty of the entity's future cash flows:**

Why or why not? If not, how would you amend the objectives and why?

We do not believe that the level of detail required in paragraphs 70-86 of the Exposure Draft would provide much practical use to financial statement readers. We have over 8,000 pieces of

equipment on lease with numerous lease commencement dates and lease terms for just our server and networking purposes. The Exposure Draft implies that we should disclose separate information for each lease schedule. However, this would be impractical given the number of leases that we enter into. Although we have a large number of leases, our total operating lease expense in 2009 was less than one percent of our cost of sales and is immaterial to our financial statements.

Aside from being impractical, we also do not feel that the proposed disclosures will provide useful information to financial statement readers. For example, we do not see the benefit of disaggregating by class of underlying asset in the reconciliation of opening and closing balances of our assets and liabilities to make lease payments. Additionally, we do not see a benefit in the narrative disclosures about the options that were recognized as part of the right-of-use asset and those that were not. Overall, we believe that the voluminous disclosures as currently proposed will be overwhelming to financial statement readers. If the proposals in the Exposure Draft as currently written are considered in the final standard, we suggest that the Boards provide further clarity surrounding aggregation of disclosures. We feel that sufficient information regarding the significance of an entity's lease transactions and the related amount, timing and uncertainty of cash flows can be disclosed on an aggregated basis.

In addition, we are concerned that our renegotiations of leases could be harmed if we need to disclose that we intend to renew a material lease at the end of the lease term. The requirement to disclose other terms of individual lease contracts may put us at a competitive disadvantage. We recommend that the disclosure requirements of the current lease accounting guidance, which require a more general disclosure of terms, be maintained.

Question 16: Transition

- (a) This exposure draft proposes that lessees and lessors should recognize and measure all outstanding leases as of the date of initial application using a simplified retrospective approach. Are these proposals appropriate? Why or why not? If not, what transitional requirements do you propose and why?**

We do not agree with the proposed guidance, but if mandated, we agree that using a simplified retrospective approach would be appropriate.

- (c) Are there any other transitional issues the Boards need to consider? If yes, which ones and why?**

We would like to stress again the administrative complexity that companies will face if this guidance is adopted. We are not aware of any software on the market today that can capture the information required by this Exposure Draft. We believe that due to the time and effort required to implement a new system and train personnel, implementation should be delayed to permit companies to have sufficient time to transition to the new methodology.

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?

We do not agree with the Boards' assessment that the benefits of the proposals would outweigh the costs. It is common to have a master lease that covers hundreds of different items that are placed on lease on varying dates with varying terms over the period of lease commitment. It would be very difficult to track each individual lease and reassess the lease each reporting period without a system change. As we stated in our answer to Question 16, we are not aware of any software on the market today to make this an easy transition. Also, for capital leases that have a defined lease period of 1, 3 or 5 years, it is relatively simple to obtain a relevant interest rate to use for capitalization purposes. However, mandating the capitalization of all operating leases will add a variety of unique lease terms for which it will be more difficult to obtain relevant interest rates.

Additionally, we believe that the information required to be disclosed in the footnotes to the financial statements under current lease accounting guidance is sufficient to enable financial statement users to make informed economic decisions. If additional disclosures would further benefit financial statement users, we would not be opposed to including them in our interim or annual financial statements. However, in order to comply with the proposals in the Exposure Draft, we would likely incur substantial costs to develop an information system to capture and track necessary details to support quarterly reassessment requirements. Additionally, we would need to educate and train employees at each of our locations to ensure that they have the necessary skills to determine if they are recording every lease in the appropriate manner, including assumptions made to measure the right-of-use asset and lease liability that will be added to the balance sheet, assessments related to term and contingent rentals (including reassessments) and calculations for expense recognition. We would like to reiterate that we do not agree that short-term leases should be included in the scope of this proposal. The cost and effort that would be involved in identifying and tracking these leases would not be offset by any benefit to financial statement users, since the majority of short-term leases would be expensed within an annual period. In addition to our above concerns, we have several credit agreements that contain cross-default clauses which include capital leases in the definition of debt. If we failed to make a payment on a capital lease, it could be seen as a default. We would therefore likely amend the credit agreements to modify the definition to exclude capital leases. However, this again would take significant time and effort and result in further costs to the company. Additionally, for many companies, covenants would need to be renegotiated, again leading to time and effort and further costs to companies.

Additionally, we have many concerns from a tax and tax accounting standpoint. It is currently uncertain how the Internal Revenue Service (IRS) will respond to the proposed lease accounting and how tax reporting requirements will change. If leases that were formerly operating leases for book and tax purposes continue to be treated as operating leases for tax purposes but are now subject to the new lease accounting rules, extensive reconciling of tax versus book treatment will be necessary, possibly for each and every asset acquisition and disposition. These changes will impose a significant cost and burden on reporting entities. There will also likely be changes in

apportionment factors for state income taxes since rent expense would be replaced by a capitalized lease asset. Furthermore, personal property taxes in various locations may increase as a result of this accounting change since many tax jurisdictions begin with book value and new "fixed assets" will be added on the books.

In addition to the comments that we have provided in direct response to the questions in the Exposure Draft, we would also like to add that we believe the proposed changes are a disincentive for business growth since renewal terms are likely to diminish. We suggest enhancements to the current lease footnote disclosures in order for financial statement users to have a better understanding of leasing activity and address the issues identified under the current lease accounting model.

We appreciate the opportunity to express our views and concerns regarding the Exposure Draft. If you have any questions with respect to our comments, please call Kim Fast, Director – External Reporting, at 412-433-5572.

Sincerely,

/s/ Gregory A. Zovko
Gregory A. Zovko
Vice President & Controller