



Madrid, 15 December, 2010
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Re: Exposure Draft ED/2010/9 – “Leases”

Dear Sirs,

Repsol is very pleased to provide comments to the International Accounting Standards Board on its request for views on the Exposure Draft ED/2010/9 – “Leases”.

Further information about the Repsol Group and its activities is available on our website: www.repsol.com.

If you would like to discuss any of the points we describe in this letter, please do not hesitate to contact us by e-mail to normativacontable@repsol.com.

Thank you for your attention.

Yours sincerely,

Emilio Linares-Rivas Balius

Accounting Policies and Compliance Manager

SECTION I – GENERAL COMMENTS ABOUT THE PROJECT

The introduction to the Exposure Draft states that the current lease accounting model should be improved to provide better financial reporting for the following reasons:

- existing models have been criticised for failing to meet the needs of users;
- existing models omit relevant information about rights and obligations that meet the definitions of assets and liabilities in the Framework; and
- existing models lead to a lack of comparability and undue complexity because of the bright line distinction between finance leases and operating leases.

Even though we understand the reasons why the IASB has undertaken this project, in general, we consider proposed requirements to be highly complex, asymmetrical and not justified in a cost/benefit basis.

We consider Conceptual Framework project should be finished before amending asset or liability recognition requirements in Standards.

Additional guidance regarding the distinction between service contracts and lease contracts should be provided. According to the proposals in the Exposure Draft, the classification of an agreement as a lease or a service contract would determinate whether it is recognised on the balance sheet or not. Considering the increasing importance of that analysis and current concerns with guidance in IFRIC 4, we consider that additional guidance with robust description would be necessary.

SECTION II – RESPONSES TO QUESTIONS IN DISCUSSION PAPER

Question 1: Lessees

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

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

We agree that the existing model in IAS 17 has application issues (e.g., bright line distinction between finance lease and operating lease). Therefore, we appreciate the IASB's efforts to develop a new approach to address them.

However, in our opinion, a lessee should recognise a right-of-use asset if under the lease contract the lessee *controls* the right to use the item and it meets the definition of asset. Depending on each contract that features would be met or not. This treatment should be also applied to the amounts to be paid by the lessee. The lessee would recognise a liability if the amounts to be paid under the contract meet the liability definition.

We are concerned that the obligation to pay rentals, as currently defined in the Exposure Draft, meets the definition of a liability as defined in the Conceptual Framework. At least for the options and renewals features, there is not a present obligation at inception and therefore this obligation should not be recognized (*Current Conceptual Framework, paragraphs 49, 61 and 83*).

In addition, other features should be analysed. Some lease arrangements are entered into by lessees as an alternative way to finance the acquisition of the underlying asset while in other cases they merely intend to obtain the use of an asset for a limited time.

In our opinion, in those cases in which the lease arrangement is entered into as an alternative way to finance the acquisition of the underlying asset, the lessee would recognise a liability to make lease payments and a right- of- use asset, presented as if it was an item of Property Plant and Equipment. But in those cases in which the lessee merely intends to obtain the use of an asset for a limited time, the lessee would recognise a liability to make lease payments and a right- of- use asset, but presented as if it was an intangible asset.

Question 2: Lessors

Do you agree that a lessor should apply the performance obligation approach when the lease exposes the lessor to significant risks and benefits associated with the underlying asset, and a derecognition approach otherwise? Why or why not? If not, what alternative model would you propose and why?

From our point of view, the lessor accounting model should be symmetrical to the lessee model.

We think that there is a contradiction arising from the performance obligation model. If the lessee controls the right of use from the date of the commencement of the lease, the lessor has completed the execution of part of the transaction at this moment. We consider that in a lease contract the lessor has changed part of an asset for a financial asset, so it makes no sense to duplicate asset accounting (i.e. the underlying asset and the receivable).

We support a single model for all leases based on the derecognition model, instead of a hybrid model from the lessor side.

Question 3: Short-term leases

The exposure draft proposes that a lessee or a lessor should apply simplified requirements to short-term leases, defined in Appendix A as leases for which the maximum possible lease term is twelve 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 recognise lease payments in profit and loss 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 recognise assets and liabilities arising from short-term leases in the statement of financial position, nor derecognise any portion of the right to use the underlying asset. Such lessors would continue to recognise the underlying asset in accordance with other IFRSs and would recognise lease payments in profit and loss 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?

We consider simplified requirements proposed for lessees should be consistent with the simplified requirements proposed for lessors. There is no conceptual basis for providing different simplifications for lessees and lessors, considering that both are counterparties in the same contracts. Therefore, we think lessees should be also permitted not to recognise additional assets and liabilities arising from short-term leases.

Anyway, and in order to provide consistent information, we consider that the simplified requirements should be an accounting policy choice and, consequently, should not be applied on a lease-by-lease basis.

Question 4: Definition of a lease

(a) Do you agree that a lease is defined appropriately? Why or why not? If not, what alternative definition would you propose and why?

(b) Do you agree with the criteria in paragraphs B9 and B10 for distinguishing a lease from a contract that represents a purchase or sale? Why or why not? If not, what alternative criteria would you propose and why?

(c) Do you think that the guidance in paragraphs B1–B4 for distinguishing leases from service contracts is sufficient? Why or why not? If not, what additional guidance do you think is necessary and why?

Lease definition

We consider lease definition in Appendix A is correct. However, we consider that robust principles that distinguish a lease from a sale or a service contract are critical.

Difference between a lease and a sale

We think principles included in paragraphs B9 and B10 are not consistent with proposals in Exposure Draft “*Revenue from Contracts with Customers*”. While the Exposure Draft “*Revenue from Contracts with Customers*” focuses on the transfer of control over a good or service (or over an PPE in the consequential amendment to IAS 16) as the condition to generate revenue from a sale or service contract, the proposals in paragraphs B9 not only are based on the transfer of control but also on “*the transfer of all but a trivial amount of risks and benefits associated with the entire underlying asset*”.

Difference between a lease and a service contracts

We feel preparers have shown concerns about the applicability of IFRIC 4. In fact, IFRIC 4 has been considered to be difficult to apply when evaluating some contracts. Considering the importance of the difference between a service and a lease contract as a consequence of the proposals in the Exposure Draft, we think existing guidance in IFRIC 4 should have been reconsidered. We are not convinced that the proposed criteria carried over from IFRIC 4 provide the necessary robust and operational distinction required to determine which accounting treatment is appropriate for the specific transaction.

Question 5: Scope exclusions

The exposure draft proposes that a lessee or a lessor should apply the proposed IFRS to all leases, including leases of right-of-use assets in a sublease, except leases of intangible assets, leases of biological assets and leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources (paragraphs 5 and BC33–BC46).

Do you agree with the proposed scope of the proposed IFRS? Why or why not?

If not, what alternative scope would you propose and why?

We think the exclusion of intangible assets should be justified, including a conceptual basis for such exclusion.

Additionally, we miss the reference to cancellable and non-cancellable contracts. We believe some cancellable contracts could be scoped out of the proposed requirements. In this sense, we would like to point out that the Exposure Draft “*Revenue from Contracts with Customers*” includes a scope exclusion for some contracts that could be terminated by either party without the payment of a penalty.

Question 6: Contracts that contain both service and lease components

The exposure draft proposes that lessees and lessors should apply the proposals in Revenue from Contracts with Customers to a distinct service component of a contract that contains service components and lease components (paragraphs 6, B6-B8 and BC47-BC54). If the service component in a contract that contains service components and lease components is not distinct:

a) The FASB proposes that the lessee and lessor should apply the lease accounting requirements to the combined contract.

b) The IASB proposes that (i) a lessee should apply the lease accounting requirements to the combined contract; (ii) a lessor that applies the performance obligation approach should apply the lease accounting requirements to the combined contract; (iii) a lessor that applies the derecognition approach should account for the lease component in accordance with the lease requirements and the service component in accordance with the proposals in Revenue from Contracts with Customers.

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

In our opinion, the proposed approach is too complex and therefore, we would advocate for a simplification, subject to a materiality assessment.

Regarding this issue, we believe that unbundling of service and lease components in order to assess whether a service is distinct should be based on an entity’s own business practices.

In addition, we agree that the mandatory separation into different components for a lessee would not be appropriate in those cases in which a reliable allocation of payments could not be available.

Question 7: Purchase options

The exposure draft proposes that a contract should be considered as terminated when an option to purchase the underlying asset is exercised. Thus a contract is accounted for as a purchase (by the lessee) and a sale (by the lessor) when the purchase option is exercised (paragraph 8 and BC63 and BC64).

Do you agree that a lessee or a lessor should account for purchase options when they are exercised? Why or why not? If not, when do you think that a lessee or a lessor should account for a purchase option and why?

In this regard we believe options to extend and purchase options should be accounted consistently.

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 consider this approach could lead to constant adjustments to the carrying amount of assets and liabilities and to high volatility in financial statements.

We believe management should assess and determine the lease term according to available information and evidences, considering contractually unavoidable rental payments, instead of considering payments that are likely but not certain.

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 contract should be included in the measurement of lease assets and lease liabilities 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 can only include contingent rentals and expected payments under term option penalties and residual value guarantees in the measurement of the lease receivable if they can be measured reliably? Why or why not?

We think contingent rentals and expected payments under term option penalties and residual value guarantees that are specified in the lease contract should not be included in the measurement of lease assets and lease liabilities using an expected outcome technique.

Their inclusion would increase complexity of lease accounting, judgements and estimates on inception and throughout the term of lease, and volatility in reported assets and liabilities. Otherwise, in our opinion, the proposal would not increased comparability of information.

As mentioned in our response to Question 8, lease assets and liabilities should be measured including contractually unavoidable rental payments, instead of considering payments that are likely but not certain.

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 obligation or receivable arising from changes in the lease term or contingent payments since the previous reporting period? Why or why not? If not, what other basis would you propose for reassessment and why?

In this sense, as we have pointed in our response to Question 9, we think that contingent rentals and expected payments under term option penalties and residual value guarantees that are specified in the lease contract should not be included in the measurement of lease assets and lease liabilities using an expected outcome technique.

Anyway, we feel that a continuous reassessment of the lease term and of the contingent rentals on a lease-by-lease basis could not be justified in a cost/benefit basis. We note that the IASB has included some restrictions on the frequency of the remeasurement (i.e. when facts or circumstances indicate that there is a significant change in the obligation or receivable), however we think a greater emphasis on the materiality should be considered.

Question 11: Sale and lease back

Do you agree with the criteria for classification as a sale and leaseback transaction? Why or not? If not, what alternative criteria would you propose and why?

As we have mentioned in our response to Question 2, we support a single model for all leases based on the derecognition model, so we disagree with the requirement that a lessor in a sale and leaseback transaction shall use a performance obligation approach.

Question 12: Statement of financial position

(a) Do you agree that a lessee should present its liability to make lease payments separately from other financial liabilities and present right-of-use assets as if they were tangible assets within property, plant and equipment, or investment property as appropriate, but separately from other assets that the lessee does not lease (paragraphs 25-27, 42-45, 60-63 and BC142-159)? Why or why not? What alternative presentation do you propose and why?

(b) Do you agree that a lessor applying the performance obligation approach should present its underlying assets, rights to receive lease payments and lease liabilities gross in the statement of financial position, totalling to a net lease asset or lease liability (paragraphs 42, BC148 and BC149)? Why or why not? What alternative presentation do you propose and why?

(c) Do you agree that a lessor applying the derecognition approach should present rights to receive lease payments separately from other financial assets and residual assets separately within property, plant and equipment (paragraphs 60, BC154 and BC155)? Why or why not? What alternative presentation do you propose and why?

(d) Do you agree that lessors should distinguish assets and liabilities that arise under a sublease separately (paragraphs 43, 60, BC150 and BC156)? Why or why not? If not, do you think that an intermediate lessor should disclose this information in the notes instead?

Lessee

As we have mentioned in Question 1, we consider lessees should present assets held under a lease, in that cases in which the lessee merely intends to obtain the use of an asset for a limited time, as if they were intangible assets, instead of as an item of Property, Plant and Equipment.

In relation to the liability to make payments, we are not opposed to the disaggregation proposed in the Exposure Draft. However, there are several financial liabilities such as "long-term payables for the acquisition of PPE", that are not required to be presented separately from other financial liabilities. In this sense, we think the proposal is not consistent with other presentation requirements contained in other Standards. Additionally, we feel it may be preferable to maintain current level of disaggregation in the statement of financial position (IAS 1 - paragraphs 54 and 55) and consider these issues in the context of Financial Statements Presentation Project, despite the fact that paragraph 77 on the ED already requires disclosing detailed information in notes about assets and liabilities arising from lease contracts.

Lessor performance obligation approach

Considering paragraph 42 a lessor shall present the following items together in the statement of financial position: (a) underlying assets; (b) rights to receive lease payments; (c) lease liabilities; (d) the total of (a)–(c) as a net lease asset or a net lease liability.

Consistently with our response to Question 2, we are not persuaded by the presentation requirements for lessors applying a performance obligation approach. We think that the proposal could reflect the ambiguity of the approach (i.e. duplicate asset accounting), considering that paragraph BC148 points out that such a presentation has the following advantage: *"It alleviates the concern that presenting separately the underlying asset, a right to receive lease payments and an offsetting lease liability inappropriately overstates both total assets and total liabilities in the statement of financial position"*.

Question 13: Statement of comprehensive income

Do you think that lessees and lessors should present lease income and expense separately from other income and expenses in the statement of comprehensive income (paragraphs 26, 44, 61, 62, BC146, BC151, BC152, BC157 and BC158)? 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?

Lease income and lease expense are significant from a qualitative point of view and, sometimes, also quantitatively. However, there are several types of income and expense that are at least as quite significant as those arising from leases and are not required to be separately presented in the statement of comprehensive income.

We think it may be preferable to consider this issue in the context of the Financial Statements Presentation Project and maintain the current level of disaggregation in the statement of comprehensive income until this Project is finished. Meanwhile, detailed information about income and expenses arising from leases could be provided in the notes.

Question 14: Statement of cash flows

Do you think that cash flows arising from lease contracts should be presented on the statement of cash flows separately from other cash flows (paragraphs 27, 45, 63, BC147, BC153 and BC159)? 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 are not opposed to the proposed requirements.

However we wonder whether a lessee should present lease payments separately from other financial cash flows, considering paragraph 77 already requires disclosing in the notes the amount of lease payments paid during the period. A similar redundancy would arise for lessors that applies the derecognition approach (paragraph 80 requires to disclose in the notes a reconciliation of the rights to receive lease payments). In this sense, and consistently with our responses to Questions 12 and 13, we think it may be preferable to deal with the level of disaggregation of the statement of cash flows in the context of the Financial Statements Presentation Project.

Question 15: Disclosures

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

(a) identifies and explains the amounts recognised in the financial statements arising from lease contracts; and

(b) describes how lease contracts may affect the amount, timing, and uncertainty of the entity's future cash flows?

(paragraphs 70-86 and BC168-BC183) Why or why not? If not, how would you amend the objectives and why?

We are not against the proposed requirements, however we think that more emphasis should have been done in paragraph 71, in order to make clear that entities may not provide each disclosure included in paragraphs 72-86 if the effect of some transaction is not material (for example lease back, paragraph 76).

Question 16: Transition

The exposure draft proposes that lessees and lessors should recognise and measure all outstanding leases as of the date of initial application using a simplified retrospective approach (paragraphs 88-96 and BC186-BC199). Are these proposals appropriate? Why or why not? If not, what transitional requirements do you propose and why?

Do you think that full retrospective application of lease accounting should be permitted? Why or why not?

Are there any additional transitional issues the boards need to consider? If yes, which ones and why?

We agree with the simplified retrospective approach proposed in the Exposure Draft because a full retrospective application would be too onerous for preparers.

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 outweigh the cost? Why or why not?

We believe that there are quite significant concerns about the proposals that are not considered in paragraph BC 203. For example:

- Changes in IT systems.
- Tax implications in some jurisdictions.
- Impacts on financial ratios, etc.

These concerns are widespread among preparers and we think that should be considered when analysing the proposals on a cost/benefit basis.

This proposed IFRS does not specify a possible effective date. In our opinion, in order to provide enough time to implement the proposed changes, the effective date should be established taking into account the feedback provided by preparers during the outreach activities.