

**US Financial Accounting Standards Board  
International Accounting Standards Board  
International Financial Reporting Standards**

**RE: Comments on the Proposed Accounting Standards Update- Leases  
Topic 840, Issued 8/17/2010- Comment Letters # 1850-100**

**Gentlemen;**

Thank you for this opportunity to comment on the proposed accounting standards update regarding lease reporting. My business is the commercial real estate market; I am a small business owner and also an investor. Because of these various of responsibilities, I look upon these proposed modifications with mixed feelings.

As a real estate professional consulting with my clients on leasing activities, investments, buy/sell transactions, sale/lease back arrangements and 1031 exchanges, I see several of these proposed changes opening up challenges to my client's business decisions based on subjective and variable concepts. This would, intern, increase my risk of doing business.

As a small business owner, I see several conflicting issues about valuations of a company, both intermediately and long term, and in addition, the cost of doing that business increasing exponentially.

As an investor, I see several caveats in the requirement that companies provide a substantial amount of financial information that may be "market driven", subjecting themselves to the "whim" of the moment, with the ability to adjust and re-state positions based on improper conclusions made by previous administrations. This would invariably increase the cost of investing and drive down the benefit of these proposed changes.

Even though the generalizations I've listed above appear "negative", I do support the need to refine and update the standards reporting requirements. With a few minor changes (as I've noted in the comments below) I believe a just and beneficial update can be achieved.

Respectfully;

Kevin S. Moffitt  
President  
**SouthEast Commercial Real Estate Services, Inc.**

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**The accounting model**

The exposure draft proposes a new accounting model for leases in which:

- a. a lessee would recognize an asset (the right-of-use asset) representing its right to use an underlying asset during the lease term, and a liability to make lease payments (paragraphs 10 and BC5-BC12). The lessee would amortize the right-of-use asset over the expected lease term or the useful life of the underlying asset if shorter. The lessee would incur interest expense on the liability to make lease payments. *Comment- In the case of real estate (buildings) I don't believe an interest expense is appropriate for commercial leases.*

- b. a lessor would apply either a performance obligation approach or a derecognition approach to account for the assets and liabilities arising from a lease, depending on whether the lessor retains exposure to significant risks or benefits associated with the underlying asset during or after the expected term of the lease (paragraphs 28, 29 and BC23 –BC27). *Comment- I believe this will be interpreted by attorneys many different ways, allowing litigation on purpose or use to determine liability.*

#### 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? *Comment- Yes I agree the ROU asset and a liability to make lease payments for real estate(buildings) should be reported on the Income and Balance sheets, but as a stated contract value, not as a Present Value (PV).*
- 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? *Comment- No, for real estate (buildings) I do not agree with the interest amortization element because the calculation to determine PV of the lease depends on the "incremental borrower's rate" which can change from reporting period to reporting period. I do not believe a PV should be required for a real estate(buildings) lease.*

#### Question 2: Lessors

- a. Do you agree that a lessor should apply (i) the performance obligation approach if the lessor retains exposure to significant risks or benefits associated with the underlying asset during or after the expected lease term and (ii) the derecognition approach otherwise? Why or why not? If not, what alternative approach would you propose and why? *Comment- I believe this needs more review by the legal sector.*
- b. Do you agree with the boards' proposals for the recognition of assets, liabilities, income and expenses for the performance obligation and derecognition approaches to lessor accounting? Why or why not? If not, what alternative model would you propose and why? *Comment- I believe this needs more review by the legal sector.*
- c. Do you agree that there should be no separate approach for lessors with leveraged leases, as is currently provided for under US GAAP (paragraph BC15)? If not, why not? What approach should be applied to those leases and why? *Comment- I believe this needs more review by the legal sector.*
- d.

#### 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: *Comment- If the comments provided herein are adopted, the need for a short-term lease will be substantially diminished or removed.*

- 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?

## Definition of a lease

This exposure draft proposes to define a lease as a contract in which the right to use a specified asset or assets is conveyed, for a period of time, in exchange for consideration (Appendix A, paragraphs B1–B4 and BC29–BC32). This exposure draft also proposes guidance on distinguishing between a lease and a contract that represents a purchase or sale (paragraphs 8, B9, B10 and BC59–BC62) and on distinguishing a lease from a service contract (paragraphs B1–B4 and BC29–BC32).

### Question 4

- a. Do you agree that a lease is defined appropriately? Why or why not? If not, what alternative definition would you propose and why? *Comment- I believe this needs more review by the legal sector.*
- 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? 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? *Comment- I believe this needs more review by the legal sector.*

## Scope

### Question 5: Scope exclusions

This exposure draft proposes that a lessee or a lessor should apply the proposed guidance 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 guidance? Why or why not? If not, what alternative scope would you propose and why? *Comment- I believe this needs more review by the legal sector. Leases of real estate(buildings) are substantively different than leases of plant(furniture, fixtures and equipment) and equipment.*

### Question 6: Contracts that contain service components and lease components

This exposure draft proposes that lessees and lessors should apply the guidance in proposed Accounting Standards Update, *Revenue Recognition* (Topic 605): *Revenue from Contracts with Customers*, to a distinct service component of a contract that contains service components and lease components (paragraphs 6, B5–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 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 guidance in

the exposure draft on revenue from contracts with customers.

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?

### **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 (paragraphs 8, BC63 and BC64).

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 a lessor should account for purchase options and why? *Comment- I believe this needs more review by the legal sector.*

### **Measurement**

This exposure draft proposes that a lessee or a lessor should measure assets and liabilities arising from a lease on a basis that:

- a. assumes 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 (paragraphs 13, 34, 51, B16–B20 and BC114–BC120).
- b. includes in the lease payments contingent rentals and expected payments under term option penalties and residual value guarantees specified by the lease by using an expected outcome technique (paragraphs 14, 35, 36, 52, 53, B21 and BC121–BC131). Lessors should only include those contingent rentals and expected payments under term option penalties and residual value guarantees that can be reliably measured
- c. is updated 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 (paragraphs 17, 39, 56 and BC132–BC135).

### **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? *Comment- In the realm of real estate(buildings) the lease document is a contract with time and consideration as essential elements. I feel those elements are the only elements to be reported in the Financial Statements. Any options, right to terminations, etc, could be listed in the foot notes. The term "significant change..." is subjective, leading to confusion and mistaken assumptions, thereby creating more risk and adding more liability.*

### **Question 9: Lease payments**

- a. 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? *Comment- In real estate(buildings) leases, I do not agree contingent rentals and expected payments under term options penalties should be included in the Financial statements. However, they could be included as part of*

*the foot notes.*

- b. 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? *Comment- In real estate(buildings) leases, I do not agree contingent rentals and expected payments under term options penalties should be included in the Financial statements. However, they could be included as part of the foot notes.*

#### **Question 10: Reassessment**

Do you agree that lessees and lessors should re-measure 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? *Comment- In real estate(buildings) the term "significant change....." is subjective, leading to confusion and mistaken assumptions, thereby increasing risk.*

#### **Sale and leaseback**

This exposure draft proposes that a transaction should be treated as a sale and leaseback transaction only if the transfer meets the conditions for a sale of the underlying asset and proposes to use the same criteria for a sale as those used to distinguish between purchases or sales and leases. If the contract represents a sale of the underlying asset, the leaseback also would meet the definition of a lease, rather than a repurchase of the underlying asset by the lessee (paragraphs 66–67, B31 and BC160–BC167).

#### **Question 11**

Do you agree with the criteria for classification as a sale and leaseback transaction? Why or why not? If not, what alternative criteria would you propose and why? *Comment- I believe this needs more review by the legal sector.*

#### **Presentation**

This exposure draft proposes that lessees and lessors should present the assets, liabilities, income (or revenue), expenses and cash flows arising from leases separately from other assets, liabilities, income, expenses and cash flows (paragraphs 25–27, 42–45, 60–63 and BC142–BC159).

#### **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 (paragraphs 25 and BC143–BC145)? Why or why not? If not, do you think that a lessee should disclose this information in the notes instead? What alternative presentation do you propose and why? *Comment- In real estate(building), I agree these elements should be presented, but only as contract values.*
- b. Do you agree that a lessor applying the performance obligation approach should present underlying assets, rights to receive lease payments and lease liabilities gross in the statement of financial position, totaling to a net lease asset or lease liability (paragraphs 42, BC148 and BC149)? Why or why not? If not, do you think that a lessor should disclose this information in the notes instead? What alternative presentation do you propose and why? *Comment- In real estate(building), I agree these elements should be presented, but only as contract values.*

- c. Do you agree that a lessor applying the derecognition approach should present rights to receive lease payments separately from other financial assets and should present residual assets separately within property, plant and equipment (paragraphs 60, BC154 and BC155)? Why or why not? Do you think that a lessor should disclose this information in the notes instead? What alternative presentation do you propose and why? *Comment- In real estate(building), I agree these elements should be presented, but only as contract values.*
- d. Do you agree that lessors should distinguish assets and liabilities that arise under a sublease in the statement of financial position (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? *Comment- In real estate(building), I agree these elements should be presented in a sublease, but only as contract values.*

### **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 (paragraphs 26, 44, 61, 62, BC146, BC151, BC152, BC157 and BC158)? Why or why not? If not, do you think that a lessee should disclose that information in the notes instead? Why or why not? *Comment- In real estate(building) I agree these elements should be separately reported.*

### **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 (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? *Comment- In real estate(buildings) I agree these elements should be separately reported.*

## **Disclosure**

### **Question 15**

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 *Comment- In real estate(buildings) I agree these elements should be included in the foot notes.*
- b. describes how leases 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? *Comment- In real estate(buildings) I agree these elements should be included in the foot notes.*

## **Transition**

### **Question 16**

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 (paragraphs 88-96 and (BC186–BC199).

- a. Are these proposals appropriate? Why or why not? If not, what transitional requirements do you propose and why? *No comment*
- b. Do you think full retrospective application of lease accounting requirements should be permitted? Why or why not? *Comment- In real estate(buildings) I believe a retrospective application would be cost prohibitive.*
- c. Are there any additional transitional issues the boards need to consider? If yes, which ones and why?

## Benefits and costs

### Question 17

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? *Comment- In real estate(buildings) I believe the costs for the proposed changes would outweigh the benefits. However, if a refined proposal (as noted herein) is adopted, the benefits would far outweigh the incremental costs of adoption.*

## Other comments

### Question 18

Do you have any other comments on the proposals?

- 1. The Present Value computation, even though introducing a "now" financial picture, also introduces uncontrollable "market" forces that could create confusion, cause mistaken conclusions resulting in a more "volatile" financial report (quarter to quarter, year to year) and wide variations in company value. I believe this to be contrary to the intent of FASB and IASB.*

## Non-public entities

### Question 19

Should any of the proposed guidance be different for non-public entities (private companies and not-for-profit organizations)? If so, which requirement(s) and why? *Comment- I believe the proposed lease accounting changes (as amended by comments herein) should be adopted for "public" companies only, where users of financial reports do not have the resources to conduct their own "due diligence" of the investment quality of the subject company. The cost of accounting services to non-public entities for adopting these proposed changes for real estate(buildings) (as amended by comments herein) would be marginally increased, but not cost prohibitive.*