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IASB
International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

17 July 2009

Dear Sir,

Thank you for the opportunity to comment on the IASB Discussion Paper: Leases – Preliminary Views. We are pleased to provide you with remarks on the proposed Discussion Paper in response to your Invitation to Comment.

Firstly, we believe that the existing segregation between two different natures of lease contract is economically justified and should be maintained in any future standard on leases. Even if at times drawing the line in practice between two kinds of contract may present difficulties, the distinction should be maintained because it reflects two very different economic transactions: a financing transaction for the acquisition of an asset ("in-substance purchases") on one hand; the purchase of access to a third party's asset for an agreed period of time on the other (rental). We believe that "in-substance purchase" transactions transfer to lessees all economic benefits in the leased asset and that the rights lessors retain in the leased asset are meant to secure the loan they have granted. We therefore support those transactions to be accounted for in compliance with the IAS 17 finance lease model. In operating leases, lessors service lessees in making their assets available on the conditions and for the duration that lessees exactly require or feel able to commit to.

Secondly, structuring opportunities may arise today mainly because of US GAAP bright lines that auditors and some preparers have a tendency to apply instead of focusing on the principle-based approach required by IAS 17. The Board should therefore work on improving the current model to reinforce principles and accounting requirements in order to avoid misrepresenting the substance of the arrangements.

Thirdly, we do not think that developing a new standard on lessee accounting without addressing lessor accounting at the same time is appropriate. Only a simultaneous, comprehensive review of both lessor and lessee accounting can lead to a robust standard. We therefore believe that no fundamental change should be required, before a comprehensive and sound analysis is carried out, as both parts of the project are inter-related and informative of each other. This review should be made consistently with other projects such as Revenue Recognition and Derecognition. We observe that so far preliminary views of the Board on lessee accounting and tentative decisions made by the IASB on lessor accounting conflict with, for example, extracts of the basis for conclusions of the ED Derecognition: only assets and liabilities of the entity should be accounted for (the so-called "single asset and liability approach" conflicts with this basic requirement; one party only can control an asset at a time (so far the IASB has concluded that both lessees and lessors should account for "the right to use" the asset) and there should be accounting symmetry – when considering transfer of control, for example). We agree with the Board that the balance sheet of an entity whose core

THE CONFEDERATION OF EUROPEAN BUSINESS a.i.s.b.l.

AV. DE CORTENBERGH 168
BE-1000 BRUSSELS
BELGIUM
VAT BE 863 418 279

TEL +32(0)2 237 65 11
FAX +32(0)2 231 14 45
E-MAIL: MAIN@BUSINESSEUROPE.EU
WWW.BUSINESSEUROPE.EU

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operations is to rent out assets (for example a car rental company) would not present the economic position of the entity fairly if it does not include the assets under lease/ to be leased and if the flows of income shown in the income statement are more akin to the gains and losses of a broker in rights of use instead of showing the regular stream of periodic rents that the rentals generate.

We have expressed above major concerns that we hope the Board will take into consideration before making any final decision in the area of leases. We believe it to be of the utmost importance to clearly identify what information users really need. We understand that, ideally, users would be interested in core leased assets measured following the whole asset approach. We do not support such an approach because we believe it is not compliant with the IFRS framework. We conclude that the other approaches are unlikely to bring the asset information that users would really find useful. We can understand that there is information value in presenting liabilities *(i.e. minimum lease payments*) that arise from operating leases, if users confirm that it is what they are after. However if it had to be the case:

- we would ask the Board to clarify the rationale for recognising these liabilities but not those arising from other binding service contracts; we would also call for sound criteria to distinguish rentals from other service contracts;
- we would support the linked measurement approach presented in the DP, so that the income statement still portrays the sustainable rent expense that best features the economic burden to the entity. We believe that the related liability is an operating liability. In our view there is no financing component involved in an operating lease;
- we would ask the Board to seriously consider, in developing the procedures for application of the standards that recognition of assets and liabilities arising from rental would generate quite a heavy burden for preparers. As the Board explains in IN23, the final standard should meet an acceptable cost / benefit trade-off considering the costs of running asset registers, physical inventories, etc.

In addition to these main comments, answers to the detailed questions of the invitation for comment are provided in the appendix.

Should you wish any supplementary comment or explanation, please do not hesitate to contact us.

Yours sincerely,

p.p.

Jérôme P. Chauvin
Director
Legal Affairs Department
Internal Market Department

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Appendix to letter on IASB DP "Leases". Answers to the specific questions raised in the invitation for comments

Chapter 2: Scope of lease accounting standard

Question 1
The boards tentatively decided to base the scope of the proposed new lease accounting standard on the scope of the existing lease accounting standards. Do you agree with this proposed approach? If you disagree with the proposed approach, please describe how.

Obviously scope differences between IAS 17 and SFAS 13 exist at present. The proposal does not deal with the outcome of the reconciliation of both standards. Besides, when a completely new accounting model for leases is developed, the scope of the new standard should be carefully scrutinized in order to be consistent. This means the present scope exceptions in IAS 17 especially as far as certain licensing agreements are concerned have to be reassessed. The same applies to the scope of IFRIC4 and SIC 27.

Question 2
Should the proposed new standard exclude non-core asset leases or short-term leases? Please explain why. Please explain how you would define those leases to be excluded from the scope of the proposed new standard.

As we have explained in our cover letter, we do not support this project firstly because we strongly believe that different economic transactions should be accounted differently but also because proposals would lead to a very significant increase in administrative burden without corresponding benefits for financial reporting.

Therefore we would favour scope exclusions to be decided, in addition to the materiality constraint described in the conceptual framework. We agree that criteria as "core vs non core or "short term vs long term" are either subjective or arbitrary and contradict the need for principle-based standards. However, we ask the Board to explore all possible reductions of the administrative impact of the Board's final decisions.

Chapter 3: Approach to lease accounting

Question 3
Do you agree with the boards' analysis of the rights and obligations, and assets and liabilities arising in a simple lease contract? If you disagree, please explain why.

We strongly disagree that in-substance purchases and rentals be analysed in the same away as they encapsulate transactions that are very different in economic substance. In-substance purchases should remain analysed as financing transactions and give rise to the recognition of assets in the same conditions of accounting and presentation as assets that have been purchased.

Actually, one of the major flaws in the analysis by the Board is to assert that the existing intended distinction between finance and operating leases does not reflect any difference in economic substance:

- Rentals are not financing arrangements. Lessees are not purchasing the underlying assets, they are renting them, i.e. they are buying flexibility and the service of being provided with the asset they need, for the period that best serves their needs. Lessors in those circumstances are providers of services.
- Other lease contracts are in-substance financing arrangements for the purchase of an asset and have to be accounted for in accordance with the substance of the purchase of an asset on one hand, the borrowing on the other. Lessors in those circumstances are providers of capital.

Nevertheless, we agree that work needs to be done in order to better determine how to identify in-substance purchases. A principle based approach to those arrangements needs to be defined. Such an improvement does not necessarily trigger a fundamental change in the existing IAS 17 approach.

The Board rejects the existing dividing line between financing and operating leases on the grounds that it is difficult to define and that it results today in structuring opportunities remaining open. This triggers the following comments:

- a key objective of standard setting is to appropriately depict differences in economic substance; whether it is difficult or easy to achieve does not diminish the need for achievement;
- the Board refers to "inappropriate bright lines"; there is no bright line in the existing IFRS; some have tried for both good and bad reasons to import into IFRS practice US GAAP application guidance; practice may be in need for improvement, without many changes in the standard;
- existing practice has benefited in recent years of appropriation by practitioners of IFRS basic principles; principle-based approaches are more and more well understood.

Finally, we believe that identifying that items meet the definition of assets and liabilities is not in itself sufficient to justify those items being reported. Items that meet the definition of assets and liabilities need to be recognised only if such recognition brings valuable information to users. While we have reiterated support for the purpose of the existing IAS 17, we believe the IASB still needs to clearly identify and demonstrate why and how recognition of assets and liabilities arising from operating leases would bring meaningful information.

Question 4
The boards tentatively decided to adopt an approach to lessee accounting that would require the lessee to recognise: (a) an asset representing its right to use the leased item for the lease term (the right-of-use asset) (b) a liability for its obligation to pay rentals. Appendix C describes some possible accounting approaches that were rejected by the boards. Do you support the proposed approach? If you support an alternative approach, please describe the approach and explain why you support it.

As explained in our preliminary comments, we believe that in-substance purchases should remain accounted for as at present (see our answer to question 3)
The question is really how should rentals be accounted for? We reject the Whole Asset Approach for the reasons given in appendix C, i.e. an entity that leases its assets is in a very different economic position from an entity that purchases its assets (or contracts a finance lease). Not only does this approach fail to depict the economy of lease contracts, it also deviates from the framework: neither the asset, nor the liability meets the definitions.

We can understand that the whole asset approach answers some users' desire to see in Financial Statement Position all assets an entity uses to create value. If this information could be relevant, it should be provided in the notes without being reported in the Statement of Financial Position.

We remain so far unconvinced that the right of use approach proposed by the Board would provide useful information. We believe the Board needs to fully explain and demonstrate, in economic terms, how the information provided would best depict economic phenomena and be useful to users.

Question 5
The boards tentatively decided not to adopt a components approach to lease contracts. Instead, the boards tentatively decided to adopt an approach whereby the lessee recognises: (a) a single right-of-use asset that includes rights acquired under options (b) a single obligation to pay rentals that includes obligations arising under contingent rental arrangements and residual value guarantees. Do you support this proposed approach? If not, why?

We believe that the tentative decision made by the Board to adopt the so-called "single asset and liability" approach conflicts with the framework, as it deviates from the definition of a liability. Only minimum lease payments in an operating lease do meet the definition of a liability. The lease contract grants the lessee the right (but not the obligation) to extend the lease beyond the initial leasing period; this is not a present obligation of the lessee until he exercises the option and therefore should not be recognized.

We agree with the Board that a lessee that can exercise a renewal option is not necessarily in the same economic position as a lessee in the exact same lease contract who has not been granted the option. The supplementary economic benefit should be recognised as a separate asset, unless it cannot be measured reliably. We would agree with the Board that accounting separately for options could be quite complex and not provide useful, understandable information. The Board could valuably look into how to measure those options on a simpler basis: intrinsic value might be a possibility to investigate.

Chapter 4: Initial measurement

Question 6
Do you agree with the boards' tentative decision to measure the lessee's obligation to pay rentals at the present value of the lease payments discounted using the lessee's incremental borrowing rate? If you disagree, please explain why and describe how you would initially measure the lessee's obligation to pay rentals.

As mentioned above, we believe a distinction should be maintained between in-substance purchases and rentals:

- For in-substance purchases, the present value of the minimum lease should be computed by using the implicit interest rate, which is likely to be available as in all other financing arrangements.
- Because rentals are not financing arrangements, we agree that the implicit interest rate would rarely, if ever, be available. In this case, as required in current IAS 17, the lessee's incremental borrowing rate could be a valid substitute.

Question 7
Do you agree with the boards' tentative decision to initially measure the lessee's right-of-use asset at cost? If you disagree, please explain why and describe how you would initially measure the lessee's right-of-use asset.

We approve the boards' tentative decision.

Chapter 5: Subsequent measurement

Question 8
The boards tentatively decided to adopt an amortised cost-based approach to subsequent measurement of both the obligation to pay rentals and the right-of-use asset. Do you agree with this proposed approach? If you disagree with the boards' proposed approach, please describe the approach to subsequent measurement you would favour and why.

Once again, we wish to differentiate treatment depending on the nature of the lease:

- In-substance purchases: we agree with the proposal to adopt an amortised cost-based approach to subsequent measurement of both the obligation to pay rental (as it is required for other borrowings) and the assets (as it is required for others fixed assets).
- Rentals: We would strongly advise in favour of the linked-measurement approach or "the rental expense method", if the Board were to conclude that liabilities arising from rentals need to be recognised on the balance sheet. Such a method brings the liability onto the balance sheet and leaves the income statement unchanged and hence more meaningful. As we have already pointed out, we cannot see any meaningful information content in the asset that would result from the proposed approach.

Question 9
Should a new lease accounting standard permit a lessee to elect to measure its obligation to pay rentals at fair value? Please explain your reasons.

No, it should not. We support amortised cost for debt instruments as we believe that such a method best reflects future cash outflows.

Question 10
Should the lessee be required to revise its obligation to pay rentals to reflect changes in its incremental borrowing rate? Please explain your reasons.
If the boards decide to require the obligation to pay rentals to be revised for changes in the incremental borrowing rate, should revision be made at each reporting date or only when there is a change in the estimated cash flows? Please explain your reasons.

We reject a revision of the incremental borrowing rate during the lease as it is not consistent with subsequent measurement of other financial liabilities and does not bring any additional valuable information to the financial statements. Lease payments are analogous to fixed rate borrowings and, when accounting for fixed rate borrowings, amounts are not remeasured to reflect changes in the incremental borrowing rate.

Finally, were the boards to decide to require reassessment of the incremental borrowing rate, reassessment should only take place when there is a change in the estimated cash flows as periodical reassessment makes lease accounting impracticable.

Question 11
In developing their preliminary views the boards decided to specify the required accounting for the obligation to pay rentals. An alternative approach would have been for the boards to require lessees to account for the obligation to pay rentals in

accordance with existing guidance for financial liabilities. Do you agree with the proposed approach taken by the boards? If you disagree, please explain why.

In-substance purchases being financing transactions, we believe that the obligation to pay "rentals" should be accounted for as a financing liability.

Liabilities that arise from rentals are similar to trade liabilities, except that entities quite rarely, if ever, have to record obligations to suppliers several years in advance of benefiting from the service.

Question 12
Some board members think that for some leases the decrease in value of the right-of-use asset should be described as rental expense rather than amortisation or depreciation in the income statement. Would you support this approach? If so, for which leases? Please explain your reasons.

Please, see our comments on Q8

Chapter 6: Leases with options

Question 13
The boards tentatively decided that the lessee should recognise an obligation to pay rentals for a specified lease term, i.e. in a 10-year lease with an option to extend for five years, the lessee must decide whether its liability is an obligation to pay 10 or 15 years of rentals. The boards tentatively decided that the lease term should be the most likely lease term. Do you support the proposed approach? If you disagree with the proposed approach, please describe what alternative approach you would support and why.

In answer to question 5, we have explained why we reject the decision made by the Board. Were the Board to decide to deviate from the conceptual framework, we would be in favour of the most likely outcome being used for recognition purposes. We also believe that management's expectations should be taken into account, while they should be fully documented taking into account all factors, contractual, non-contractual and business factors as identified in par 6.39.

Question 14
The boards tentatively decided to require reassessment of the lease term at each reporting date on the basis of any new facts or circumstances. Changes in the obligation to pay rentals arising from a reassessment of the lease term should be recognised as an adjustment to the carrying amount of the right-of-use asset. Do you support the proposed approach? If you disagree with the proposed approach, please describe what alternative approach you would support and why. Would requiring

reassessment of the lease term provide users of financial statements with more relevant information? Please explain why.

In the context of the Board's proposals for rentals (which we do not support), we would agree with the Board's position.

Question 15
The boards tentatively concluded that purchase options should be accounted for in the same way as options to extend or terminate the lease. Do you agree with the proposed approach? If you disagree with the proposed approach, please describe what alternative approach you would support and why.

In the context of the Board's proposals for rentals (which we do not support), we would agree with the Board's position.

Chapter 7: Contingent rentals and residual value guarantees

Contingent rentals

Question 16
The boards propose that the lessee's obligation to pay rentals should include amounts payable under contingent rental arrangements. Do you support the proposed approach? If you disagree with the proposed approach, what alternative approach would you recommend and why?

We are of the opinion that this item requires a deeper analysis that should take into account the different kinds of "contingent rentals" that might exist because all contingent payments do not correspond to an irrevocable obligation to make future payments.

Actually, we believe that a distinction should be made between unconditional liabilities of which the amount will vary depending on some form of index (inflation, change rate …) and other forms of contingent rent that generate conditional liabilities that should not be reported in the balance sheet (when conditions are dependent on the entity and when the entity can avoid payment by acting differently).

Question 17
The IASB tentatively decided that the measurement of the lessee's obligation to pay rentals should include a probability-weighted estimate of contingent rentals payable. The FASB tentatively decided that a lessee should measure contingent rentals on the basis of the most likely rental payment. A lessee would determine the most likely amount by considering the range of possible outcomes. However, this measure would not necessarily equal the probability-weighted sum of the possible outcomes. Which of

these approaches to measuring the lessee's obligation to pay rentals do you support? Please explain your reasons.

In the context of the Board's proposals and of our answer to question 16 in mind, we agree with the FASB's position.

Question 18
The FASB tentatively decided that if lease rentals are contingent on changes in an index or rate, such as the consumer price index or the prime interest rate, the lessee should measure the obligation to pay rentals using the index or rate existing at the inception of the lease. Do you support the proposed approach? Please explain your reasons.

We believe that the FASB's position should be supported on pragmatic grounds. Actually, if the Board requires reassessing both obligation and asset values at each reporting date, the standard is going to grow in complexity. In the Board's model it should be kept in mind that any change in the value of the asset triggers new computation of the depreciation plan.

Question 19
The boards tentatively decided to require remeasurement of the lessee's obligation to pay rentals for changes in estimated contingent rental payments. Do you support the proposed approach? If not, please explain why.

We disagree for the reason we support the FASB's position in question 18 above.

Question 20
The boards discussed two possible approaches to recognising all changes in the lessee's obligation to pay rentals arising from changes in estimated contingent rental payments:
(a) recognise any change in the liability in profit or loss
(b) recognise any change in the liability as an adjustment to the carrying amount of the right-of-use asset.
Which of these two approaches do you support? Please explain your reasons. If you support neither approach, please describe any alternative approach you would prefer and why.

Here again we need to differentiate our answer, whether dealing with in-substance purchases or rentals.

In-substance purchases: we believe that the financing liability that arises from such a lease should be accounted for as a variable financial liability consistently with IAS 39 present requirements.

Rentals: for the reasons given in answer to question 18 (and 19), we do not believe that reassessments should be carried out at all, for cost/ benefit trade-off. Furthermore, we observe that contingent rentals in operating leases are not liabilities that are contracted upon variable terms. They are generally intended to make the lessee pay for a current price in each period in which it benefits from the leased asset. Therefore changes in the liability to pay rentals should be reflected in the cost of providing the asset to the entity, and the cost of the leased item in each period should be reflected in the income statement. This requirement is also more in line with the "rental expense" method that we have favoured.

Residual value guarantees

Question 21
The boards tentatively decided that the recognition and measurement requirements for contingent rentals and residual value guarantees should be the same. In particular, the boards tentatively decided not to require residual value guarantees to be separated from the lease contract and accounted for as derivatives. Do you agree with the proposed approach? If not, what alternative approach would you recommend and why?

We have argued in favour of the component approach. We therefore cannot support the proposed approach.

Chapter 8: Presentation

Question 22
Should the lessee's obligation to pay rentals be presented separately in the statement of financial position? Please explain your reasons. What additional information would separate presentation provide?

Since the proposed accounting for obligations to pay lease rentals described in the DP differs from the way most other financial liabilities are accounted for, we agree that such liabilities should be presented separately from other liabilities in the statement of financial position.

Question 23
This chapter describes three approaches to presentation of the right-of-use asset in the statement of financial position. How should the right-of-use asset be presented in the statement of financial position? Please explain your reasons. What additional disclosures (if any) do you think are necessary under each of the approaches?

Even though the proposal to present the right-of-use asset as an intangible asset is theoretically consistent with the new approach to lease accounting proposed in the

Discussion Paper, we think that it seems more useful to present the right of use of the leased asset together with owned assets but clearly separated from them

Chapter 9: Other lessee issues

Question 24
Are there any lessee issues not described in this discussion paper that should be addressed in this project? Please describe those issues.

The following issues should be addressed in this project:
- Guidance on impairment of the right-of-use asset should be provided.
- First-time adoption guidance including guidance on how to deal with existing lease contracts when the new lease standard becomes effective, should be provided. We would like to stress the need for a practical and cost-effective solution

Lessor Accounting

Generally, we think that a conceptual change of lease accounting must include lessor accounting. There is a close link between lessee and lessor accounting which must be reflected in developing a new model for lease accounting. Therefore, we would appreciate a more thorough analysis of the issues concerning lessor accounting which has not taken place so far.

Having said that, the comments you will find below reflect only our preliminary view to the questions 25 to 29 concerning lessor accounting.

Question 25:
Do you think that a lessor's right to receive rentals under a lease meets the definition of an asset? Please explain your reasons.

In-substance sales are already acknowledged as giving rise to a receivable in the lessor's accounts today under IAS 17. We agree with that assessment.

We have acknowledged that minimum lease payments arising from rentals met the definition of a liability. This liability is an asset of the lessor.

Nonetheless, as we have indicated in our answer to question 3, the mere fact that items meet the definition of assets and liabilities does not justify in itself that they be recognised. Whether they should depends on the usefulness of the information that such recognition would provide

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Question 26:
This chapter describes two possible approaches to lessor accounting under a right-of-use model:
(a) derecognition of the leased item by the lessor or
(b) recognition of a performance obligation by the lessor.
Which of these two approaches do you support? Please explain your reasons.

In-substance sales trigger derecognition of the leased asset in the books of the lessor under IAS 17 today. We believe that this is a sensible outcome that should not be changed.

Assets leased by lessors in rentals remain assets of the lessor in our view. Lessors use those assets to provide rental services to their customers. Therefore a rental should not trigger derecognition of leased assets by lessors.

Question 27:
Should the boards explore when it would be appropriate for a lessor to recognise income at the inception of the lease? Please explain your reasons.

We believe that the existing principle and guidance on the gain that a lessor should recognise at inception of an in-substance purchase is fully appropriate, including guidance on leaseback transactions.

We do not think that any income should be recognised at inception of a rental. All our reasons have been explained in our earlier comments in this letter.

The boards may also find it useful to consider derecognition in the context of non-financial instruments to see if the principles should be consistent with financial instruments.
