March 14, 2014

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Submitted via electronic mail to director@fasb.org

Subject: Lease Accounting Project

Dear Sirs:

The Committee on Corporate Reporting ("CCR") of Financial Executives International ("FEI") has been following the Leasing project with great interest. We understand that the Boards will be making key decisions related to the leasing project at their joint meeting on March 18-19, 2014. The issue of how to account for operating leases in the new standard is a pivotal issue that likely will determine the success or failure of the standard in becoming generally accepted worldwide. In our letter dated September 17, 2013, we proposed an approach that would display operating lease obligations on the balance sheet in a manner that is simple, transparent and cost-effective to apply (the display approach). At this critical juncture in the process, we believe that it is important to explain, in our own words, why that is the best approach.

FEI is a leading international organization of 15,000 members, including Chief Financial Officers, Controllers, Treasurers, tax executives and other senior financial executives. CCR is a technical committee of FEI that reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations. This document represents the views of CCR and not necessarily the views of our members individually.

In judging whether an accounting standard is of high quality, one must assess: (1) whether it faithfully reflects the economics of the underlying transactions, (2) whether it provides useful

information to financial statement users in making credit and investment decisions, and (3) whether its benefits exceed associated costs. FEI believes that our proposal meets all of those requirements and we have significant concerns as to whether the same can be said of Approach 1 as characterized in the current Board materials.

Economics of the Underlying Leasing Transactions

The concept underlying our approach is that an operating lease agreement embodies both a right to use and an obligation to pay for such use, each of which exist within the confines of a single contract. These rights and obligations are inextricably linked to, and are inseparable from, the economics of the contract as a whole. The best reflection of the economics of the contract is the level benefit that is received by the lessee from the right to use the asset over the term of the lease. FEI believes that operating lease arrangements are essentially rentals which are conceptually and legally different from "in-substance purchases" and that financial statement users clearly understand the difference between the two and would expect them to be treated differently in financial statements.

Applying Type A accounting to operating leases, as contemplated in Approach 1, will require the lease assets and liabilities to be accounted for independent of one another as though they represent separate free-standing assets and liabilities. In reality, they are not free-standing nor do they have separate economic substance. Although it should be self-evident, we would observe that lease assets cannot be sold, pledged or otherwise encumbered. Nor does the lessee have complete freedom to use or misuse that asset as it would if it owned it outright. Assuming a lease remains at market subsequent to lease inception, Type A accounting will produce non-economic gains and losses upon early termination that can only be explained by the disconnect between the accounting for the asset and liability. Type A accounting also causes the expense pattern to diverge from the actual cash flows, which we believe will be problematic for financial analysis performed by investors and creditors.

Another important aspect of the economic relevance of a high quality accounting standard is how it embraces the concept of comparability: that is, ensuring that the accounting principles do not cause transactions that are substantively different to appear to be the same. Type A accounting obscures the important differences between operating leases and in-substance purchases. Tax law and bankruptcy law acknowledge these economic differences and provide different treatments for them in many jurisdictions around the world. Adoption of Type A accounting will therefore introduce new book-tax differences, adding unnecessary and avoidable complexity to corporate reporting.

Decision-Useful Information for Investors

Much has been written about the views of financial statement users regarding the usefulness of the various approaches considered by the Boards. We believe that the diversity among user views is much greater than what is being portrayed in the summaries of the outreach performed. For example, we are troubled by the characterization of the views of the airline industry analysts in the Board materials. The Board memo for the March meeting includes the following statement: "*Almost all airline and transport analysts agree with the proposal to recognize and present amortization separately from interest for most leases of assets other than property because, in their view, there should be consistency in the treatment of owned and leased assets*." However, we note that in its letter dated March 5, 2014, the Aviation Working Group provides a markedly different view of airline industry analysts on their preferences compared to what is in the latest Board memo. That letter indicates that a strong

majority of the group's analysts prefer the current model to any of the approaches proposed by the Boards. This development raises questions about the overall findings from the outreach.

What also concerns us is the perception that a majority of users support a particular model. While it may be fair to say that a majority of users support capitalization of leases, we observe that there remains significant diversity among users about the following important follow-on decisions: (1) how to measure the separately recognized asset and liability, (2) whether the standard recognizes one or two types of leases, (3) how to determine the classification for the two types, and (4) presentation of lease expense in the Statements of Earnings and Cash Flows (i.e., whether bifurcation of interest and depreciation is appropriate). These follow-on decisions have as much bearing on the relevance of the resulting financial reporting as the decision on whether or not to capitalize operating leases.

Finally, given that recognition and measurement can only portray one set of decisions, we are concerned about the utility of the results for those investors who disagree with the Boards' conclusions. This point is highlighted in a recent article on the leasing project, where the views of two members of the FASB's Investor Advisory Committee are referenced, as follows.[1]

> "Having to unwind an accounting construct put on the balance sheet and then having to do my own analysis is not very desirable," Trainer said. "I'd rather just have the data there, and let me do with it what I think I ought to do with it." In the Spring, Moody's Investors Service Managing Director Mark LaMonte expressed a similar view, saying the proposal would force investors and analysts to deconstruct the information placed on the balance sheet before performing their own calculations to determine lease liabilities."

In that regard, FEI observes that of the three alternatives under consideration, Approach 3 is the easiest of the models for users to unwind in order to reflect the effects of leases as they see fit in their respective models. That is a significant benefit that should not be overlooked.

Cost-Benefit Considerations

The proposed FEI solution is simpler and less costly for companies to implement than the proposed accounting under Type A because it does not require the development of a new integrated system solution that links lease assets and liabilities at a specified unit of account level (e.g., individual leased asset, master lease, etc.). Because both the asset and liability under the display approach are measured based on the present value of the remaining future lease payments, the company can determine the carrying amount of the assets and liabilities at an aggregate level and can continue to account for the operating lease itself using existing systems that produce the straight line results required by current GAAP (as amended). That approach is not feasible for accounting under Type A because the company would need to account for each lease (or group of leases under a master agreement) by vintage in order to appropriately determine the carrying amount of the asset. When implementing compliant systems involving tens of thousands of leases, the level of effort and cost are much lower under the display approach we recommend. We also would observe that the costs and complexity associated with classification decisions under Approach 3 are not significant in comparison to Approach 1. We have decades of experience in making these decisions

[1] "FASB's Investor Advisory Committee opposes leases proposal", Journal of Accountancy, September 3, 2013.

under existing GAAP and interpretive guidance is well developed and understood. The operational costs and complexity associated with implementing Approach 1, including the book-tax complexities referenced above, are far more significant in considering the overall impact of these alternative approaches.

Given the level of uncertainty regarding the degree to which financial statement users find these proposed changes to be an improvement in financial reporting, coupled with resource demands that will be placed on preparers, auditors and investors, it seems logical to ask whether the benefits derived from any of these models are commensurate with the level of resource commitment that will be required. Based on the concerns expressed above and the significant and intrusive nature of the systemic and process changes that will be required to implement any of the approaches under consideration, we do not believe the finalization of the proposed standard, under any model other than Approach 3, will meet a reasonably performed cost-benefit analysis.

We therefore urge the Boards to adopt the display approach we recommended in our comment letter response to the Revised Exposure Draft. In so doing, the Boards will accomplish the goal of improving financial reporting in the simplest and most cost-effective way possible.

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At our most recent meeting, the Committee was asked to consider the question of whether it is more important for the Boards to reach a converged solution than it is for the FASB to adopt FEI's recommended approach. Our response to that question is to observe that today's leasing models are substantially converged and could move closer together with removal of the quantitative thresholds present in US GAAP. We believe that the Boards should consider that alternative before embarking on a path that would apply Type A accounting to all lease contracts. We have doubts as to whether the latter approach is capable of becoming generally accepted.

We appreciate the opportunity to share our views with the Boards. Please contact Lorraine Malonza at (973) 765-1047 with any questions.

Sincerely,

Stephen J. Cosgrove
Chairman, Committee on Corporate Reporting
Financial Executives International

cc: Paul Beswick, Chief Accountant, US Securities and Exchange Commission
FASB Board Members
IASB Board Members