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## **Aviation Working Group – Comments on Leases Exposure Draft ED/2013/6**

Dear Mr. Hoogervorst and Mr. Golden:

The Aviation Working Group (**AWG**) is an industry group whose members consist of the leading manufacturers, lessors and financiers of aircraft and aircraft engines. AWG has been closely following and reviewing with interest the leasing project activities of the FASB and IASB (the **Boards**). The Boards' goal to issue a comprehensive leasing standard is commendable and we support the Boards' efforts to develop harmonized accounting standards.

AWG is providing this letter in response to the questions asked by the Boards following the issuance of the Exposure Draft (**ED**), the Illustrative Examples (**IE**) and the Basis for Conclusion (**BC**).

### **Summary**

The accounting for leases is a complex subject. The development of a new accounting model for leases is a difficult challenge as leasing covers a broad spectrum of arrangements, with some arrangements being used to acquire an asset and others being used to gain access to the use of an asset for a limited period of time. Some arrangements involve only the right to use an asset,

while other arrangements embed the right to use an asset in a service arrangement. In our comment letter on the first exposure draft, we referred to this broad spectrum of leasing transactions, and it is this broad range of transactions that makes the development of a new, unified leasing model so difficult to achieve.

The move to a two model approach to leasing is a reasonable way of addressing the spectrum of lease transactions, as a model that is appropriate for one category of transactions is usually inappropriate for others. The feedback the Boards received during outreach following the issuance of the first exposure draft confirmed this view. While some users of financial statements, auditors and preparers may favor a single model for all lease transactions, there is neither agreement as to what that model should be nor whether the goal is attainable. Given this diversity of views, we believe a final leasing standard needs to be both representationally faithful and practical. With the diverse range of views regarding leasing, it is most important that a new lease model be both practical to apply and useful to a plurality of users of financial statements.

The ED incorporates a number of technical improvements to the lease model over that proposed in the first exposure draft, particularly in areas related to the measurement of lease receivables and lease liabilities. We are concerned, however, that the revised ED does not form a consistent, practical and useful system of accounting for leases. In particular, we believe:

- The classification of leases based upon the underlying asset is arbitrary and is not a reasonable approach to leasing. It is not representationally faithful and is not consistent with the manner in which both management and users of lessor financial statements view the economics of lease transactions. If a classification approach is to be retained, the basis should be grounded in the nature of the lease contract and not the underlying asset.
- The classification of aircraft and engine leases as Type A leases in almost all circumstances is not a faithful presentation of many lessor activities and will not provide users of lessor financial statements with the presentation they prefer.
- To be representationally faithful, the lessor model needs to recognize there is a difference between the leases that represent financings and leases that represent the use of an asset regardless of the type of underlying asset.
- The proposed changes to the existing model for finance and sales-type leases do not in total represent an improvement in financial reporting. The changes will require lessors to expend considerable resources and there will be little or no incremental benefit arising from the changes to users of lessor financial statements.

We have been supportive of the lease accounting project, and we support the development of a lease accounting standard that will stand the test of time. ***We believe, however, that our concerns regarding the model proposed in the ED are significant, and we do not support the issuance of a final standard in this form. If it is not possible to develop a recognition and measurement system that is representationally faithful and meets the needs of users of financial statements, we would urge the Boards to pursue an enhanced disclosure regime for leases.*** Improving disclosures has many advantages, especially when there are differing opinions as to the preferred solution to an accounting issue. Improving disclosure keeps the Boards from

having to choose the view of some users of financial statements over the views of others and it should be less costly for preparers to implement. It may be the most effective solution.

### **Lessor accounting**

As stated in our comment letter on the first exposure draft, the Boards embarked on the development of a new lease accounting standard in response to criticism of the existing lease accounting guidance. We believe the criticism is focused principally on lessee accounting and not lessor accounting. We question the need for a new lessor accounting model as the current guidance is well understood by preparers and users, and users of financial statements in the aviation leasing industry generally support the retention of the existing lessor accounting model.

It is not necessary to formalize a lessor model along with a lessee model as the two sides of the transaction are by their nature different. Lessee accounting is fundamentally concerned with the recognition and measurement of the rights and obligations in a lease contract and the allocation of the cost of that arrangement. Lessor accounting is concerned with the measurement of the lessor's investment and how income on that investment should be recognized. These are different subjects and symmetry is neither necessary nor practical and desirable.

The Boards' effort to change lessor accounting needs more time and due diligence in order to address this complex area. While the Basis for Conclusions states that users of lessor financial statements desire the separate recognition and measurement in all cases of lessor risk into credit and residual components, based upon discussions we have had with investment analysts we do not believe this statement is applicable to the aviation leasing industry. We believe to the extent that further information about lessors is desirable, it can be provided through enhanced disclosures rather than through significant changes to the recognition and measurement model. The Boards should consider carrying out additional research and due diligence before developing an accounting model for lessors. We therefore strongly encourage the Boards to exclude lessor accounting from the scope of any final leasing standard.

### **Alternative Approaches to Lessor Accounting**

The ED's approach to income recognition and cost allocation is based upon the type of asset that is being leased. We do not believe this a reasonable approach and do not believe there is sufficient conceptual support for allocating income and costs in this manner. As further discussed in response to question number four, we further note the basis for the model is not clear. It is difficult to determine if the lease model is concerned with the accounting for the lease contract or the accounting for the underlying asset. Our impression is that: (1) the scope of the proposed standard is based on which party controls the underlying asset; (2) the initial recognition and measurement is based on the contract; (3) the income and expense allocation methods are based upon the underlying asset type; and (4) the accounting for remeasurements is based upon the contract. This is not a unified model. The proposals would be improved if the lease model was based firmly on either the underlying asset or on the contract.

If the Boards decide to include lessor accounting in the new lease accounting standard, the Boards could achieve their goals and have a more consistent model for lessor and lessee accounting if the lease standard focused on the underlying asset. This approach would retain classification, but the basis of the classification test would be whether the lessee has in substance purchased the asset and obtained substantially all of the risks and benefits of the underlying asset. This accounting for the underlying asset could be based upon a simple modification to current accounting guidance rather than a significant change to lessor accounting. The Boards could consider basing this approach on whether substantially all risks and rewards have been transferred, similar to the guidance contained in IAS 17, *Leases*. Leases that do not transfer substantially all of the risks and rewards of ownership could be accounted for in a manner similar to that proposed for Type B leases.

If the Boards did not choose to consider risks and rewards as the basis for this approach to leasing, an approach based upon whether substantial control over the underlying asset has passed to the lessee should be explored. A control based approach would not lead to a significantly different answer than a risks and rewards approach when the lease arrangement is considered in total.

In addition to this suggestion there are other approaches to lessor accounting that could achieve similar results. For example, we have long supported allowing lessors to elect the accounting method that would most faithfully reflect their business model. If the lessor is in the business of managing assets and redeploying them over their useful life – as many aviation lessors do – then an operating lease model should be followed. If, on the other hand, the lessor is financing the sale of an asset, then the approach should be based on a model similar to the derecognition approach to lessor accounting proposed in the ED. This approach would be more faithful to the presentation of the business and how it is managed than what is proposed in the ED.

There are many ways for the Boards to achieve their goals while producing an internally consistent leasing standard that was representationally faithful and useful to both management and investors. These alternatives, along with a rigorous analysis of the cost effectiveness of any proposed changes to lessor accounting, should be reviewed during redeliberation.

### **Cost Versus Benefit Considerations**

The model proposed in the ED will result in lessors and lessees in the aviation industry incurring substantial transition and ongoing compliance costs. If the ED is finalized in its current form, many lessors will be required to change their accounting systems and processes from the current operating lease accounting model to the proposed Type A model. This will represent a significant change in systems, processes, and financial reporting. Based upon the feedback we have received from users of lessor financial statements, we do not believe the proposals represent an improvement in financial reporting and question whether the very significant changes to lessor accounting in the ED meet the cost versus benefit requirements for a new standard. Users of financial statements have many needs, and the recognition and measurement system in the proposed model is not the best way of meeting their needs for additional information. We suggest that enhanced lessor disclosure be considered in place of the proposed model given this diversity of views and the costs related to the proposed model.

## **Lessor Accounting Proposed in ED**

### ***Type A Leases and Lessor Accounting***

While we do not support the classification of most aviation leases as Type A leases, the changes the Boards have made to the lessor models within the ED do represent improvements over what was proposed in the first exposure draft. While the accounting for residual assets is significantly improved in this ED, we do believe that under a derecognition model the residual element of the investment in a lease should be recorded at fair value rather than allocated cost. A fair value approach is consistent with the view that the lessor no longer controls the asset and that the accounting for a loss of control is based upon fair valuing the retained portion of the investment.

The Type A lessor model includes another change from the existing direct finance lease model. Under existing requirements, the lease payments and residual are considered to be one cash flow stream for purposes of income recognition. In the ED this is not the case, as illustrated in IE Example 19. This change to existing accounting principles is not meaningful from a presentation perspective, but will require systems changes to implement. We do not believe this is a change that should be made either from either theoretical or cost versus benefit perspectives.

### ***Rate Implicit in the Lease and Comparability of Financial Statements***

Operating leases may not be priced in a manner that includes the development of a lessor's implicit rate and determining an implicit rate or the rate the lessor is "charging" the lessee will be difficult when this is the case. In the aircraft leasing business, aircraft are often ordered well in advance and leased closer to delivery at then-prevailing market lease rates. While the lessor could estimate an implicit rate after the fact or discount the lease payments at the lessee's borrowing rate, this will likely not produce a meaningful number as lessors do not manage their businesses on this basis. Further, when an implicit rate is not a factor in lease pricing, using a discount rate to value residuals and using this rate to determine accounting gains or losses on releases of assets as if the lessor managed their business on this basis, will create artificial volatility in reported results unrelated to the substance of the lease transactions and not produce a representationally faithful financial presentation.

Today the financial statements of lessors are comparable. Operating lessor financial statements reflect rental income and depreciation based upon what they paid to acquire the asset. If the lease transfers substantially all of the risks of ownership to the lessee, the lease will typically be a direct finance lease that does not include the recognition of a gain at lease inception.

If all aviation leases were to be recast to the Type A model, lessor financial statements would appear to be comparable on the surface, but the financial position and results of operations would be impacted by the newly added assumptions related to the valuation of the receivable and the residual and by the estimation of an implicit rate. These assumptions and related valuations will be developed lessor by lessor. Results of operations will be impacted by newly originated leases or releases. These factors when added to the financial statements will reduce the ability of users of financial statements to compare lease portfolios and results of operations across companies.

We believe this situation further supports our belief that lessors should present their leases based upon one of the alternative methods described under “Alternative Approaches to Lessor Accounting” above.

### ***Reassessment of Lease Term and Lease Payments***

The Boards have concluded that when there is any change in facts and circumstances relating to a lease contract, the lease term and related lease payments should be reassessed. We question the cost and benefit of this requirement. To comply with this requirement, a public company lessor or lessee will be required to review the facts and circumstances relating to every lease contract once a quarter to assess if there were any changes that would require remeasurement. This effort will result in significantly higher personnel and infrastructure operating costs. While we understand the Boards’ desire for reassessments of lease receivables and lease liabilities, we believe language limiting reassessments to situations when the lessor or lessee becomes aware of changes in lease term or payments would be a more cost effective and useful approach.

With regards to changes in the discount rate, we are concerned that the requirement to update the discount rate will be burdensome to lessors and lessees, and these changes are not likely to significantly impact the measurement of lease obligations and assets. Further, this remeasurement requirement is not consistent with other portions of the existing accounting model.

### ***Sale and Leaseback Transactions***

If a sale and leaseback does not represent a sale by the transferor/lessee, the ED proposes that the transferee/lessor not recognize the transferred asset and account for the amount paid by the transferee as a receivable. We do not regard this as faithful representation of the lessor’s position in the transaction. In a sale and leaseback a lessor will generally pay fair value for the asset and have a residual position in the asset. Including the residual in the financing receivable will misrepresent the lessor’s investment in the lease under either a Type A or Type B lease model. The lessor should account for its investment according to the nature of the transaction and this presentation should not be ignored in order to provide symmetrical presentation.

## **Transition**

### ***Leveraged leases***

The Boards have proposed that accounting for certain leases as leveraged leases would not be allowed. As also stated in our comment letter on the first exposure draft, we recommend that the Boards revisit their conclusion. Leveraged leases are based on unique circumstances, including tax treatment, and continue to be used as a viable and efficient means to finance long-lived assets in our industry. Should the Boards elect to eliminate leveraged lease accounting, we recommend that leveraged leases in existence at the implementation date for the new lease accounting guidance be grandfathered and allowed to run their course with no adjustment due to the new lease accounting guidance.

### ***Implementation***

We provide a comment later in this paper on the implementation of the new lease accounting standard. We believe that the modified retrospective approach will not appropriately reflect proper accounting for lease contracts, since the accounting commencement date for a lease contract will be the implementation date. We support providing lessors with the option of applying the new lease accounting guidance on a prospective basis, with appropriate disclosure about the effect of such adoption method, or on a full retrospective basis. A full retrospective implementation would involve a higher level of costs for a lessor as a result of personnel, operational and information system resources needed for compliance. If a full retrospective implementation is selected by the Boards, lessors should have an adequate amount of time for implementation so that they may properly account for lease contracts during the time between issuance of the new standard and the year in which the new standard is adopted. We also recommend the Boards explicitly consider the SEC five year reporting requirements when selecting the amount of time provided for implementation of the new lease accounting standard.

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In addition to these summary comments, we provide answers and comments to the Boards' questions, below.

#### **Question 1: Identifying a Lease**

This revised Exposure Draft defines a lease as a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration. An entity would determine whether a contract contains a lease by assessing whether:

1. Fulfillment of the contract depends on the use of an identified asset.
2. The contract conveys the right to control the use of the identified asset for a period of time in exchange for consideration.

A contract conveys the right to control the use of an asset if the customer has the ability to direct the use and receive the benefits from use of the identified asset.

Do you agree with the definition of a lease and the proposed requirements in paragraphs 842-10-15-2 through 15-16 for how an entity would determine whether a contract contains a lease? Why or why not? If not, how would you define a lease? Please supply specific fact patterns, if any, to which you think the proposed definition of a lease is difficult to apply or leads to a conclusion that does not reflect the economics of the transaction.

#### ***Answer***

We agree with the definition of a lease as proposed in the ED, but we suggest the Boards provide additional guidance and examples with regards to the critical terms included in the definition.

## **Question 2: Lessee Accounting**

Do you agree that the recognition, measurement, and presentation of expenses and cash flows arising from a lease should differ for different leases, depending on whether the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset? Why or why not? If not, what alternative approach would you propose and why?

### *Answer*

Once the decision has been made to recognize lease assets and obligations on a lessee's balance sheet, the allocation of the cost arising from a lease transaction becomes the central question of the lease accounting project. The approach to expense allocation is somewhat dependent upon what the basis is for recognition of the lease contract. If that basis is that leasing is merely the integration of an asset acquisition with a financing component – a view we do not agree with – then the asset and liability should be accounted for separately after recognition. If, on the other hand, leasing represents a separate class of transactions, then a model that is representationally faithful to the transaction should be developed. Otherwise, making leases the “same as” or “equivalent to” the acquisition of an asset with a financing component will be distortive to the financial statements.

As stated in our detailed response to Question 4, below, we support a categorization approach to lease accounting, but we do not believe a consumption based concept is a reasonable basis for the allocation of income or costs arising from lease contracts. We believe the separation should be based upon the nature of the contract – whether the contract does or does not represent an in substance purchase of an asset -- rather than the characteristics of the asset being leased.

In our comment letter on the first exposure draft, we stated that we did not believe that the Boards' guidance relating to amortization of a lessee's right-of-use asset or recognizing interest on a lessee's liability to make lease payments reflects the true economic intent of a lease that is not a purchase, such as where title transfers or a bargain purchase option exist. We also did not believe the proposed separation of assets and liabilities is consistent with other areas of the accounting literature, since the lessee may not separately settle the separate components of the transaction. When viewed from a lessor-customer perspective, the asset and obligation component of a lease transaction are not distinct.

We continue to urge the Boards to consider linking the amortization of a lessee's right-of-use asset and lease obligation such that the balances remain equal during the term of a lease for the bulk of lease transaction. In addition, we believe that a lessee should record lease expense on a level basis over the term of a lease.

## **Question 3: Lessor Accounting**

Do you agree that a lessor should apply a different accounting approach to different leases, depending on whether the lessee is expected to consume more than an insignificant portion of the



economic benefits embedded in the underlying asset? Why or why not? If not, what alternative approach would you propose and why?

*Answer*

We believe there is no need to make changes to lessor accounting. The existing lessor accounting models are well understood by users of financial statements and preparers and, based upon the information we have received to date from users, provide financial information that is useful to investors.

If the Boards continue to include lessor accounting within the lease accounting project, we support a categorization approach to lease accounting, but we do not believe a consumption based concept is a reasonable basis for the allocation of income or costs arising from lease contracts. The separation should be based upon the nature of the contract rather than the characteristics of the asset being leased. This would provide a better basis for the presentation of lessor financial information and would recognize the difference between long term leases that are substantially similar to asset purchases and medium term rentals that are not substantially similar to asset purchases.

We do not believe the classification of aircraft leases as Type A leases in almost all circumstances will improve financial reporting. Most lessors in the aviation industry are in the business of managing their pool of asset over the long term, which will typically involve several leases of an aircraft over its useful life. The essential element of this business approach is the management of the hard asset. Separating that asset into credit and residual components will in most cases not present a faithful depiction of the lessor's financial position when a lessor enters into, for example, a seven year lease of an asset with a twenty-five year useful life. We have participated in discussions with users of aviation lessor financial statements and has participated in outreach meetings with the Boards on lessor accounting. The feedback we have received from users of financial statements is that the existing lessor models meet the needs of investors and that the proposed changes do not represent an improvement in financial reporting for lessors. If users of financial statements require additional information on credit and residual risk, it is best provided through additional disclosures rather than through a recognition and measurement system that will mask the performance of the lease over time.

If the Boards continue with the classification approach to lessee accounting outlined in the ED, then lessors should be allowed to determine which lease accounting model best reflects their business model and follow that approach in their financial statements. While this might lead to accounting that is not symmetrical between the lessee and the lessor, we do not believe that symmetry should be a goal of the project at the expense of other financial accounting elements. Lessor accounting is concerned with the presentation of the investment in a lease and the recognition of income. Lessee accounting is about the recognition and measurement of lease rights and obligations and expense recognition or cost allocation. These are different topics and symmetry should not be pursued to the exclusion of concerns regarding the usefulness of the financial information.

#### **Question 4: Classification of Leases**

Do you agree that the principle on the lessee's expected consumption of the economic benefits embedded in the underlying asset should be applied using the requirements set out in paragraphs 842-10-25-5 through 25-8, which differ depending on whether the underlying asset is property? Why or why not? If not, what alternative approach would you propose and why?

#### *Answer*

As stated in the opening section of this comment letter, we believe that leasing encompasses a broad spectrum of transactions and the development of one general model for all lease transaction is not possible without producing a result that is potentially distortive to whole classes of transactions. While it is necessary to separate leases into two or more categories, based upon the characteristics that are central to the transaction and that require a specific accounting treatment, we do not support a separation of leases based upon whether the lessee is expected to consume more than an insignificant portion of the economic benefits embedded in the underlying asset. We do not believe there is a similar concept elsewhere in the accounting literature, in the conceptual framework or in corporate finance literature.

The central premise behind the Type A lease model is the notion that a lease is the "same as" or "equivalent to" the acquisition of an asset and the incurrence of debt. The consumption concept is the basis for determining which leases are "as if" purchases and which leases are not. We believe that consumption is not an indicator of an asset acquisition and financing. In a Type A lease, there are two units of account: the asset and the lease liability. It is not clear to us how consumption can be used as the basis for the bifurcation of a contract into two units of account and how this concept relates to other accounting literature related to bifurcation of a contract. Bifurcation is generally a concept that is applied to economically different elements of a contract that influence how that contract is settled. Consumption is not related to this concept.

An accounting model that is based upon equating one series of transactions to another should be based upon whether or not the transactions are in fact the same or very similar. Therefore, for leases that are to be accounted for as if they were separate purchase and financing transactions, the accounting model should be based upon what transactions are equivalent to this occurrence. We believe that either a risk and rewards criteria, based upon IAS 17, or a control criteria should therefore be employed to classify leases as it would be these transactions that are most similar to or equivalent to purchase and financing transactions. Using an IAS 17 based approach, leases that transfer substantially all of the risks and rewards of ownership would be accounted for as Type A leases and all other leases would be accounted for as Type B leases by lessors and lessees. The IAS 17 criteria are well understood and this approach would be cost effective to apply.

If the Boards find it is not possible to work with a classification approaches to leases, we believe the best alternative would be the development of general model for lessees based upon the contract --- which might involve recognition of an asset and liability and cost allocation based upon rent expense – and elimination of lessor accounting from the project. Lessor accounting could then continue to follow the well tested methods that are used today.

If a classification approach to recognizing the differences between leases proves to be unworkable and if the Boards determine that additional information is required, we recommend the Boards pursue improved lessor and lessee disclosures. Given the wide spectrum of leasing arrangement and the divergent views of users, a disclosure based approach to lease accounting is preferable to the development of a model that does not represent a meaningful improvement over the existing lease accounting standards.

### **Question 5: Lease Term**

Do you agree with the proposals on lease term, including the reassessment of the lease term if there is a change in relevant factors? Why or why not? If not, how do you propose that a lessee and a lessor should determine the lease term and why?

*Answer:*

The proposed definition of lease term appears to result in the recognition of lease liabilities and lease receivables that are closer to the accounting definitions of assets and liabilities than what was proposed in the first exposure draft. We do believe, however, that there needs to be greater clarity as to the factors that preparers should consider when evaluating the term of a lease, as we are not certain there is agreement as to what is meant by the terms contractual, entity and market based factors that should be evaluated when determining lease term. Of the three terms, it is entity and market factors that require the most explanation. We understand this approach was adopted as it was designed to mimic the analysis of lease term that is done under existing standards, but we are concerned the new wording may lead to interpretations that result in a different application to transactions in the future. Since the intent of the Boards is for lease term to be determined in a manner consistent with existing requirements, we suggest that existing concepts be employed to minimize the effort and cost related to transition. We believe this approach is more cost effective than the proposals included in the ED.

We do not agree with the Boards' proposal that lease assets and liabilities should be remeasured when there are significant changes arising from the lease term since the last reporting period. Options to extend or terminate a lease do not give rise to contractual rights and obligations until the options are exercised or until the contingent events occur. As a result, lessors and lessees should not recognize assets and liabilities until the exercise of the options or the occurrence of the contingent events. The Boards have not provided substantial theoretical support for the inclusion of lease options assets and liabilities in recognized lease assets or liabilities.

We also question whether the Boards have appropriately balanced the costs and benefits associated with the reassessment requirements included in the proposal. Lessees and lessors will need to invest significant resources of personnel, process and systems in order to meet this requirement. It is not clear that the proposed requirement will provide decision-useful information to users of an entity's financial statements. We recommend that the Boards use input from roundtable discussions and comment letters and give appropriate consideration to the costs and benefits of this proposal.

If the Boards conclude that lease options should be included in the measurement of lease assets and liabilities and periodically reassessed, we believe that reassessment should only be carried out when a material change to the contract has occurred. We also believe that the Boards' guidance on reassessment of lease term and lease payments should also address commonly occurring events for lease contracts, including novation, amendments, restructuring and business combinations

### **Question 6: Variable Lease Payments**

Do you agree with the proposals on the measurement of variable lease payments, including reassessment if there is a change in an index or a rate used to determine lease payments? Why or why not? If not, how do you propose that a lessee and a lessor should account for variable lease payments and why?

*Answer*

We believe the proposals on the initial measurement of variable lease payments are reasonable. With regards to the reassessment requirements, we believe they – like the reassessment requirements for lease term -- will be burdensome to preparers and are unlikely to result in a significant change in the lease liability. We also question the need to reassess lease liabilities and assets when similar requirements do not exist for other financial assets and liabilities.

### **Question 7: Transition**

Subparagraphs 842-10-65-1(b) through (h) and (k) through (y) state that a lessee and a lessor would recognize and measure leases at the beginning of the earliest period presented using either a modified retrospective approach or a full retrospective approach. Do you agree with those proposals? Why or why not? If not, what transition requirements do you propose and why?

*Answer*

We believe that a fundamental tenet of any new standard is that its application results in decision-useful information for investors, which can only be achieved if stakeholders are offered the necessary time to thoughtfully contemplate each new proposal and provide the Boards with meaningful feedback to ensure the final standards are of the highest quality and result in improvements to our existing financial reporting model. We also recognize that each new standard will have a different magnitude of impact to different industries; however, we believe there are concerns that would likely be shared by all industries, including:

- The ability to manage, educate, and communicate to senior management, boards of directors, audit committees, investors, and analysts regarding the changes and related impact resulting from the adoption of new standards;
- The availability of external resources, including consultants and auditors, similar to the resource constraints that occurred during the implementation of Sarbanes Oxley;

- The availability and time required by companies' auditors to plan, understand, and test new processes, controls and data resulting from the changes in accounting standards;
- The premiums associated with the accelerated audits performed by auditors necessary for them to render an audit opinion;
- The impact to companies' business models and strategies; and
- Entity-wide training.

Given the importance of convergence topics, particularly the lease and the revenue recognition standards, and the broad potential impact of the proposed standards, we believe that field-testing is necessary to ensure that the final standards are both operational and provide an improvement over existing financial reporting.

The transition methods within the proposed standards require retrospective application and presentation. We believe retrospective application for the proposed new lease accounting and revenue recognition standards is impractical and cost-prohibitive. We recommend the proposed standards include implementation guidance that considers when retrospective treatment may be impractical, such as that in FASB Accounting Standards Codification 250, Accounting Changes and Error Corrections (ASC 250), which states that this is the case when:

- An entity is unable to apply the requirement after making every reasonable effort to do so;
- An entity is required to make assumptions about management's intent in a prior period that cannot be substantiated; and/or
- An entity is required to make estimates of amounts for which it is impossible to distinguish objective information about those estimates at the time they were made.

We suggest that, if adopted, the proposed guidance be applied prospectively for lease contracts entered into with customers on or after the effective date of the standard. To address the Boards' concern regarding the preservation of trend information about leasing transactions, we suggest that entities be required to disclose information, where practicable, that enables financial statement users to understand the effects of the change in accounting principles, in the spirit of ASC 250.

If the Boards decide that the new lease accounting standard should be implemented with modified or full retrospective reporting, companies would need a sufficiently long lead-time to assess the substantial system, process, and policy implementation challenges which would result. It will take significant resources to implement this standard on a retrospective basis, given the long-term nature of our contracts. We recommend that if retrospective application is required, the adoption date be at least five years from the date of final standard issuance.

Are there any additional transition issues the Boards should consider? If yes, what are they and why?

*Answer*

It is not clear from the ED which date a lessor or lessee should use to perform lease classification at transition. The date should be made explicit in a final standard. We recommend that the classification date should be an election based upon the information available to individual lessors and lessees.

**Question 8: Disclosure**

Paragraphs 842-10-50-1, 842-20-50-1 through 50-10, and 842-30-50-1 through 50-13 set out the disclosure requirements for a lessee and a lessor. Those proposals include maturity analyses of undiscounted lease payments, reconciliations of amounts recognized in the statement of financial position, and narrative disclosures about leases (including information about variable lease payments and options). Do you agree with those proposals? Why or why not? If not, what changes do you propose and why?

*Answer*

We agree that lessors and lessees should provide quantitative and qualitative information about amounts recognized in their financial statements relating to lease contracts. We also believe the proposed disclosures are excessive and will not provide decision useful information. The costs associated with providing the proposed disclosures will outweigh any perceived benefit.

Due to the complexity of applying the ED for Type A leases, the Boards have proposed disclosures for Type A lease which are numerous and complex. The proposed disclosures are vastly different for Type A leases versus Type B as follows:

<b>Type A Discloses</b>	<b>Type B Disclosures</b>
Reconciliation of the opening and closing balances of the lease receivable	Maturity analysis of lease payments
Reconciliations of the opening and closing balances of the residual asset	
Maturity analysis of the lease receivable	
Disclose how the lessor manage its risk associated with residuals	

We believe that lessors should include in their qualitative disclosure an explanation of the nature of leases, information about significant assumptions and judgments made in applying the requirements of this ED and how the lessors manage the risk associated with residuals. We agree that a quantitative disclosure in the notes to the financial statements for the maturity of the lease receivable and additional disclosure of the future net book value of assets under leases maturing in five years, for example, would be appropriate. We do not believe that additional disclosures reconciling the opening and closing balances of the lease receivable and residual asset are necessary.

We interpret the disclosure requirements as being mandatory in quarterly filings. Quarterly disclosure will be excessive and should be more limited in scope. Whatever approach is finally adopted, additional disclosure requirements would be more acceptable if they were only required annually when there is more time to accumulate, summarize and report the data. Large U.S. SEC filers have 40 days to file their Form 10Qs. With the processes involved in quarterly filings, including auditor reviews, audit committee clearance and XBRL, there would not be enough time for extensive quarterly disclosure. Disclosures for larger companies would not be expected to change materially on a quarterly basis. Given that quarterly disclosures would be similar to annual disclosures, we do not believe users would benefit from such quarterly disclosure. Quarterly disclosures should focus on any significant changes that occurred since the year-end disclosure.

**Question 9: Nonpublic Entities (FASB Only)**

To strive for a reasonable balance between the costs and benefits of information, the FASB decided to provide the following specified reliefs for nonpublic entities:

1. To permit a nonpublic entity to make an accounting policy election to use a risk-free discount rate to measure the lease liability. If an entity elects to use a risk-free discount rate, that fact should be disclosed.
2. To exempt a nonpublic entity from the requirement to provide a reconciliation of the opening and closing balance of the lease liability.

Will these specified reliefs for nonpublic entities help reduce the cost of implementing the new lease accounting requirements without unduly sacrificing information necessary for users of their financial statements? If not, what changes do you propose and why?

*Answer*

We have not provided a response to this question as we represent public entities.

**Question 10: (FASB Only)**

Do you agree that it is not necessary to provide different recognition and measurement requirements for related party leases (for example, to require the lease to be accounted for based on the economic substance of the lease rather than the legally enforceable terms and conditions)? If not, what different recognition and measurement requirements do you propose and why?

*Answer*

We believe this is a reasonable decision as the prior guidance was difficult to implement.

**Question 11: (FASB Only)**

Do you agree that it is not necessary to provide additional disclosures (beyond those required by Topic 850) for related party leases? If not, what additional disclosure requirements would you propose and why?

*Answer*

We believe this is a reasonable decision.

**Question 12: Consequential Amendments to IAS 40 (IASB Only)**

Do you agree that a right-of-use asset should be within the scope of IAS 40 if the leased property meets the definition of investment property? If not, what alternative would you propose and why?

*Answer*

We have not provided a response to this question as we are not aware of our members having investment property as defined under existing IFRS requirements.

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We would be pleased to discuss these comments further with the Boards and their staff.

Sincerely yours,



Jeffrey Wool  
Secretary General  
Aviation Working Group