CENTER FOR CAPITAL MARKETS
COMPETITIVENESS

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September 10, 2013

Mr. Russ Golden
Chairman
Financial Accounting Standards Board
301 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-05116

The Honorable Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC 4M 6XH
United Kingdom

Re: Leases (FASB Project 2013-270, Accounting Standards Update Topic 842)

Dear Chairmen Golden and Hoogervorst:

The U.S. Chamber of Commerce (the "Chamber") is the world's largest federation of businesses and associations, representing the interests of more than three million U.S. businesses and professional organizations of every size and in every economic sector. These members are both users and preparers of financial information. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory structure for capital markets to fully function in a 21st century economy. To achieve these goals, the CCMC has supported the development of robust financial reporting systems and encouraged efforts to improve standards and reduce complexity.

The CCMC appreciates the work done by the Financial Accounting Standards Board ("FASB") and International Accounting Standards Board ("IASB") (also collectively as the "standard setters") in developing and releasing **Leases (FASB Project 2013-270, Accounting Standards Update Topic 842),** ("the Proposals") as one of the

convergence projects. The CCMC has several serious issues concerning the proposal specifically:

1. **Continued lack of investor support and failure to transparently identify investor interests that are being addressed;**

2. **Increased footnote disclosure may be as beneficial as balance sheet capitalization;**

3. **Straight line expensing should be used for both equipment and real estate leases;**

4. **Compliance burdens that place costs upon businesses without benefits to investors;**

5. **Driving economic activity rather than reflecting it; and**

6. **Due process and transition issues.**

If these issues are not addressed, the CCMC believes that the finalization of the lease accounting proposal in its current form will increase financial reporting complexity, harm businesses and the investors that provide them with capital. These issues and our concerns are discussed in greater detail below.

Discussion

The CCMC is committed to transparent financial reporting and is a strong supporter of converged accounting standards to facilitate capital formation for businesses. Accordingly, the CCMC has commented extensively on efforts to converge lease accounting[1] and the CCMC is also part of a broad based coalition of trade associations and organizations, representing all forms of businesses and commercial real estate. The coalition on lease accounting has met with FASB, IASB and the Securities

[1] *See* CCMC comment letters of July 17, 2009, December 15, 2010 and February 1, 2011.

and Exchange Commission ("SEC") multiple times and sent numerous correspondences to the standard setters and G-20 Finance Ministers to air our concerns.[2]

The Chamber is also a signatory to the comment letter submitted by the lease accounting coalition filed on September 9, 2013. The CCMC would also like to use this opportunity to address specific concerns and issues related to our membership.

1. **Continued lack of investor support and failure to identify investor interests that are being addressed.**

A primary objective of the lease accounting project is to increase transparency and comparability among companies in the financial reporting for leases. In our comment letters and interactions with the standard setters we have repeatedly asked the standard setters to transparently identify the investor interests and needs they seek to address.[3] We are particularly concerned that this requirement has not been met. On August 27, 2013, FASB's own Investor Advisory Committee ("IAC") raised alarms that the lease accounting proposal is too complex, fails to provide more decision useful information than currently exists and recommended increased footnote disclosure rather than a completely revised standard that capitalizes leases. Similar concerns were raised by IAC in their July 24, 2012 meeting.

Clearly, investors have raised serious concerns regarding the lease accounting proposal and that it does not meet their needs. If investors do not believe that the lease

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[2] *See* lease accounting coalition letters to FASB and IASB of December 8, 2010, March 11, 2011, April 1, 2011, April 28, 2011, May 26, 2011, July 8, 2011, February 17, 2012, April 26, 2012, September 10, 2012, June 6, 2013 and September 9, 2013. See also lease accounting coalition letter of October 21, 2010 to G-20 Finance Ministers.

[3] For instance see the principles for an effective leasing standard set forth by the lease accounting coalition:

1) New lease accounting standards must reflect economic activity, not drive it;
2) New lease accounting standards must permit financial statements to represent the true effect of lease transactions;
3) New lease accounting standards should not raise the cost of capital or unnecessarily create adverse impacts upon financial statements;
4) FASB and IASB should ensure that the benefits of revised rules outweigh the costs;
5) New lease accounting standards must take into account non-accounting issues, such as contractual obligations, industry related practices, and potential regulatory environments, to truly represent lease transactions;
6) To ensure accuracy, lease accounting standards should be consistent for the lessor and lessee; and
7) Standard-setters should transparently identify the investor interests and needs they seek to address.

accounting proposal meets their needs, then the project itself should not move forward and this highlights the concerns raised by the CCMC in the context of this project and others regarding the transparency, disclosure and outreach to the investment community. It further illustrates the need for a real and transparent economic analysis for standard setting.

A transparent disclosure of investor outreach and clear articulation of investor interests would have highlighted concerns early in the process and taken this project, in our view, down a different and more productive path. Indeed, significant differences within the investor community, particularly investors' concerns that the lease accounting proposal does not provide more decision useful information than currently exists, calls into question the utility of the current proposal itself.

2. **Increased footnote disclosure may be as beneficial as balance sheet capitalization.**

Reacting to some of these concerns, some investors have publicly questioned the need for capitalizing leases onto the balance sheet and instead have requested maintaining extant lease accounting standards with increased footnote disclosure. A recent study, *Evidence that Market Participants Assess Recognized and Disclosed Items Similarly when Reliability is Not an Issue,*[4] which specifically focused on lease accounting, put forth that footnote disclosure is as effective as balance sheet capitalization when recognizing payments required through contractual obligations. Therefore, increased footnote disclosure, as also supported by IAC members, is a viable and more cost-effective alternative to the lease accounting proposal.

Furthermore, balance sheet capitalization of executory contracts raises issues on the nature of assets and liabilities. It would be appropriate if the definition of assets and liabilities in the lease accounting proposal is consistent with the definitions in the conceptual framework. Furthermore, right of use assets are not ones that meet the definitions of assets and liabilities under bankruptcy law. Therefore, the lease accounting proposals may undermine the usefulness of the financial statements for users including credit analysis.

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[4]The study was authored by Professor Brian Bratten, University of Kentucky, Professor Preeti Choudhary, Georgetown University and Professor and former FASB member Katherine Schipper, Duke University. The study was published in the July, 2013 edition of the *Accounting Review*, Volume 88, No. 4.

3. Straight line expensing for equipment and real estate.

Setting aside the recommendation for enhanced disclosure rather than balance sheet capitalization, if the FASB and IASB decide to proceed with balance sheet capitalization, the CCMC believes that straight line expensing should be used for both real estate and equipment leases. Essentially, the Proposals have straight line expensing for real estate but not equipment leases.

The accelerated recognition of expenses for equipment does not reflect the true financial costs incurred by a business in the appropriate time frame. This will skew profit and losses, imposing costs on and ultimately harming investors. Through the current bi-furcated proposal companies will have to encounter complexity by recognizing expenses in two different manners.

Further, investors will be saddled with additional complexity in analyzing financial information. As proposed the system will not show investors a true recognition of expenses (or cash flows) obfuscating financial reporting. Again, it is noteworthy that these concerns were expressed during the discussion at last month's IAC meeting with IAC members raising concerns and declining to support accelerated recognition, also known as "front-end loading," of expenses.

4. Compliance burdens that place costs upon businesses without benefits to investors.

The lease accounting proposal requires the disclosure of individual leases by businesses. This creates complexity, costs, and enormous compliance burdens on businesses that may have tens of thousands of leases. Individual reporting and disclosure of leases multiple times a year will require costly new systems. Furthermore, there is no articulation as to the benefit for investors to this type of disclosure, while the costs will harm potential return for investors.

Clearly, the individual disclosure of leases places enormous costs upon businesses without any benefits to investors. The failure to conduct and publish a transparent cost-benefit analysis has again yielded a serious flaw in the proposed lease accounting standard.

As an alternative, which could also apply to increased lease disclosures through enhanced footnotes, the disclosure of lease obligations on a portfolio basis will reduce some of these burdens and costs and prevent irrelevant information from being disclosed to investors.

5. Driving economic activity rather than reflecting it.

Throughout its consideration, the CCMC has raised concerns that the lease accounting proposal would not accurately reflect economic activity, but rather, drive it. This is in some ways exemplified through the treatment of debt covenants. While some debt covenants will take into account changes in U.S. Generally Accepted Accounting Principles ("US-GAAP"), others will not, either forcing the debt to be called in or to be renegotiated. Thus, the lease accounting proposal will increase costs for companies that have debt financing that doesn't take into account US-GAAP changes.

In addition, the recognition of additional assets and liabilities under the Proposals could affect the capital sufficiency ratios of financial institutions. It is unclear how regulators will respond to these changes and, therefore, the ensuring operational implications. With the changes in capital standards, leverage ratios, and risk tolerance, as mandated in various initiatives including the Dodd-Frank Wall Street Reform and Consumer Protection Act and Basel III capital standards, it is unclear how violating debt covenants will impact regulated financial entities thereby harming capital formation for businesses.

Similarly, signatories to the lease accounting coalition comment letter have heard from members that they have already suspended providing long-term leases pending the completion of a proposed leasing standard. Further, if a certain portion of a building is owned and a certain portion leased, the entire building is being converted to ownership to avoid the complexities of a proposed lease accounting standard.

These are just a few illustrations of the economic implications of the Proposals, as additional economic consequences are also expected to occur. For example, changes to the financial statements in accordance with the Proposals could have implications for state and local tax apportionment and, in foreign jurisdictions, impact cash taxes.

6. Due process and transition issues.

The broad implications and ramifications of the Proposals go beyond accounting and will impact many different industries and business models. This will require a thorough vetting process, specifically the identification of investor interests the proposal seeks to address, a robust cost-benefit analysis published for review and comment and a comprehensive pre-implementation review through field testing.

These issues go to the core of the lease accounting project and remain unanswered for some industries years into the project. In accord with the lease accounting coalition comment letter, we believe that these process concerns must be met before stakeholders can provide informed commentary on the Proposals, and before a lease standard is finalized by the FASB and IASB. Recent statements by investors that the Proposals do not provide any additional useful information over what exists under current standards highlights the potential lack of understanding of investor needs and the absence of a benefit.

Thus, we respectfully request that FASB and IASB adhere to their own norms by providing the following assurances of adequate due process and cost benefit analysis:

I. Clearly identify the specific investor groups and users of financial statements that FASB and IASB believes it is serving in the current lease accounting proposal;

II. Provide the opportunity for investor groups and users of financial statements to participate in at least two rounds of public roundtables devoted to substantive discussion of the recently released Exposure Drafts;

III. Conduct and publish a robust cost-benefit analysis of the proposals; and

IV. Commit to field testing of the proposal prior to its finalization, to ensure that the cost-benefit analysis is rooted in reality.

Conclusion

Once again, the CCMC thanks you for the work done by the staffs of FASB and IASB, as well as the continuous dialogue the standard setters have engaged in with us and other concerned associations during the consideration of this project. However, we have substantial concerns regarding the need for the Proposals, the process used to develop the Proposals, as well as concerns about the Proposals themselves.

In order to improve the Proposals, we believe that increased footnote disclosure rather than capitalization would meet the needs of investors and businesses. If capitalization moves forward, straight line expensing should be the norm for both equipment and real estate leases, issues such as debt covenants must be better understood and resolved to avoid driving economic activity and, as we have stated before, FASB and IASB must address the due process and transition concerns that we have continually raised.

We look forward to discussing our concerns with you further.

Sincerely,

Tom Quaadman

Cc: Mr. Paul Beswick , Securities and Exchange Commission