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The European Federation of Financial Services Users
Fédération Européenne des Usagers des Services Financiers

Revised IASB Exposure Draft Leases

Better Finance Response to the Additional Consultation Questionnaire for users of financial statements

8 August 2014

ID number in Transparency Registry: 24633926420-79

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- Please indicate how you use financial statements:

  Credit analyst

  Sell-side equity analyst

  Buy-side equity analyst

  Retail investor X

  Other (please specify)

PART 1 - DESCRIPTION OF THE IASB AND FASB APPROACHES TO LESSEE ACCOUNTING

Common features

9. Including the tentative decisions made at the June 2014 meeting, the two Boards are converged on the following aspects in relation to lessee accounting:

(a) A lessee should recognise a right-of-use asset and a liability on its balance sheet for all leases (other than short-term leases);

(b) The criteria and guidance to identify if an arrangement contains a lease;

(c) When a contract includes both a lease and service components (such as maintenance), a lessee shall separate the contract and allocate the total payments to the different components, A lessee recognises an asset and a liability only for the lease component;

(d) Right-of-use assets and lease liabilities shall be presented or disclosed separately from other assets or liabilities;

(e) A lessee shall initially measure the lease liability as the present value of the future lease payments and the right-of-use asset at the amount of the lease liability plus initial direct costs; and

(f) The guidance on discount rates, options and variable lease payments.

Differing features

10. The approaches of the two Boards differ in relation to:

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(a) The subsequent measurement of the right-of-use asset for those leases that, in the FASB model, are not in substance purchases of the underlying asset;

(b) The presentation of the lease expense in the income statement;

(c) The presentation of the lease payments in the statement of cash flows; and

(d) In the IASB approach, an exemption for 'small' assets (eg laptops and office furniture).

IASB approach

11. The IASB approach requires a lessee to recognise a right-of-use asset and a lease liability at the commencement date of each lease. A lessee may elect not to recognise assets and liabilities in relation to:

(a) Short-term leases; and

(b) Leases of 'small' assets.

12. After commencement, a lessee shall measure the lease liability at the present value of future lease payments and amortise the right-of-use asset over the lease term in accordance with the requirements in IAS 16. This results generally in a straight-line amortisation of the right-of-use asset and a declining interest expense on the lease liability.

FASB approach

13. The FASB model distinguishes between leases that are in substance purchases of the underlying asset (written as leases) and leases that are not in substance purchases of the underlying asset. The distinction is based on the principle used in IAS 17 to distinguish finance leases from operating leases.

14. A lessee shall recognise a right-of-use asset and a liability for all leases, whether they are in substance purchases or not. A lessee may elect not to recognise assets and liabilities for short-term leases.

15. For leases that are in substance purchases, a lessee shall account for the transaction in the same manner as any other financed purchase. After commencement, this results generally in a straight-line depreciation of the asset and a declining interest expense on the liability.

16. After commencement, leases that are not in substance purchases are accounted for using a single approach that recognises a single lease expense measured generally on a straight-line basis over the lease term. The lease liability is measured at each reporting date at the present value of future lease payments, while the right-of-use asset equals the lease liability (as adjusted for any prepaid/accrued rent).

How the approaches depict leases

17. In substance, the IASB approach considers all leases as finance leases. The IASB approach views a lease as providing a lessee with a non-financial asset that it typically uses over time and for which it pays over time. Accordingly, the IASB approach requires a lessee to account for the right-of-use assets consistently with other non-financial assets and lease liabilities consistently with other similar financial liabilities.

18. Compared to the current requirements and the FASB approach, the IASB approach removes the need for a classification of leases, which some may consider as improving comparability. However, others may disagree that all leases should be treated in the same way.

19. Concerning presentation, under the IASB approach, a lessee shall present the interest expense on the lease liability within finance (interest) costs and the amortisation of the right-of-use asset typically within the same line item as depreciation on items of property, plant and equipment (ie within operating expenses).

20. The IASB does not specify how a lease liability is presented. However, the IASB staff noted that under the general requirements of IAS 1, a lessee would either present these liabilities in a separate line or include them with other financial liabilities.

21. The FASB approach maintains the view that some leases are in substance purchases of the underlying asset, and some leases are not. For the latter the lease expense is recognised generally on a straight-line basis because it represents the generally equal benefit the lessee receives each period throughout the lease term, as well as the periodic cost of the access to that benefit. Compared to the IASB approach, in most cases the FASB approach maintains the same profile of recognition of lease expenses and reduces the extent of change imposed on preparers.

22. Concerning presentation, for leases that are not in substance purchases the single expense is shown as an operating cost in its entirety and is not broken down between amortisation and interest.

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23. The FASB does not specify how a lease liability is presented, but has indicated that a lessee cannot present the total liabilities as a single separate line or include them in the same line, but it has to separate the liabilities arising from leases that are in substance purchases and other leases.

24. The FASB staff noted that this would generally allow lessees on the US to present lease liabilities from leases that are not in-substance purchases as operating liabilities (e.g., akin to a restructuring liability that is still financial in nature, but not 'debt-like'); given the different legal treatment of these liabilities in case of a bankruptcy procedure.

Questions

25. Assume that the Boards maintain the current scope of application of the proposals, do you prefer:

The IASB approach, that recognises all leases on the balance sheet and in substance treats all leases as finance leases **NO**

The FASB approach, that recognises all leases on the balance sheet but, after commencement as follows:

- ✓ for leases that are in substance purchases: separate finance and amortisation costs in the income statement and right-of-use assets and liabilities in the balance sheet **YES**

- ✓ for leases that are not in substance purchases: a single lease expense in the income statement and right-of-use assets and lease liabilities, separately presenting these liabilities from the liabilities for leases that are in substance purchases, in the balance sheet **YES**

26. Please provide your reasons for supporting one or the other approach:

It provides more relevant information **YES**
It is easier to understand **YES**
It improves comparability of similar transactions **YES**
Other reasons (please explain):

The distinction between financial leases and operating leases is convincing. Both types of leases should not be treated the same. Also, this is fully in consistency with IAS 17.

Please explain the basis of your conclusion:

35. Based on the proposals, the Customer will need to separate the total contract payments between the lease and the consumables and services. Payments related to consumables and services are recognised as a cost during the lease term and do not give rise to an asset and liability at the beginning of the lease.

Assessing if there is an identified asset – Portion of capacity

36. Customer enters into a contract to transport gas with the Supplier. The Supplier owns a pipeline. The volume of gas transported on behalf of the Customer is equal to 50% of the total capacity of the pipeline.

37. Based on the proposal, the contract does not contain a lease because the 50% capacity occupied is not physically distinct.

38. However, if the volume transported equals to 100% of the total capacity of the pipeline, the Customer would need to assess which party has the right to control the use of the pipeline. If the Customer concludes that it has the right to control the use of the pipeline, the contract is a lease.

Question

39. The current definition and criteria to identify a lease are explained above in paragraphs 27 to 30. Based on your knowledge, do you think that some transactions should be excluded from the scope of the Standard and treated as service contracts (i.e., no asset and liability are recognised by the lessee)? If so, please describe the transaction and provide your reasons.

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