

22.7/8/1

2 March 2004

Mr Reinhard Biebel
Project Manager
EFRAG
41 Avenue des Arts
1040 Brussels

Dear Mr Biebel,

RE: IFRIC D3 DETERMINING WHETHER AN ARRANGEMENT CONTAINS A LEASE

In response to the draft comment letter published by EFRAG for consultation, we would like to offer the comments set out below.

UNICE is of the opinion that such an interpretation is worth issuing. It should indeed help to clarify situations in which IAS 17 should apply.

However, as a draft, this interpretation raises some issues that need to be resolved before final issuance.

The issues at stake are listed below:

1- Scope

a. Concessions

As IFRIC is developing quite an extensive study on concessions, it appears premature to reach conclusions on this issue within the scope of D3. In our view, IFRIC has to consider the following alternative:

- concessions are included in D3's scope: the definition needs to be reviewed and IFRIC must settle that the concessions contracts dealt with as part of D3 will not be subject to later decisions reaching different conclusions;
- concessions are excluded from D3's scope: IFRIC allows itself more time to define what the appropriate accounting treatment of concessions should be.

b. Components of an asset

The implicit choice that is left to entities should be removed, for the sake of comparability. IFRIC should:

- characterise the differences, if any, between those situations and the situations addressed in IAS 31 paragraphs 13 through 18 (Jointly Controlled Assets),

- refer to IAS 31 for the accounting treatment of those situations that fall under that standard,
- decide either to include in or to exclude from the scope of D3 transactions that have been characterised as being different.

c. Choice of the word “item” instead of “asset”

UNICE believes there is some benefit in using terms that are as precise as possible. Asset remains in our view a large enough concept to encompass the situations in which D3 should apply. The use of the word “item” seems inappropriate since it is too broad and too vague. Is D3 really meant to apply to “items” which would not be characterised as assets? If so what are those items? Should a lease be redefined in IAS 17 since the definition refers to the right of use of an “asset”?

2- Criteria

a. Criteria

The criteria proposed in the interpretation are too close to the characteristics of a lease as defined in IAS 17 to bring sufficient help in assessing the substance of the transaction involved. Except for the mention that the asset can be implicitly identified (§6 a) and that the obligation to make payments may be implicit (§6 b), there is no guidance added in that list of criteria.

Criteria retained in EITF 01-8 are in our view more likely to permit the identification of arrangements that contain a lease. IFRIC should re-work the criteria, while making them adjust to the risk and rewards model set out in IAS 17.

b. Robustness

Also, we believe that criteria should be robust enough to resist changes of circumstances. IFRIC rejects the re-assessment of a transaction whenever the criteria that qualified the arrangement under the scope of D3 would no longer be met because a change in the circumstances would have occurred. Take the example of a railway network whose rights of use are sold to a railway company. At inception of the contract, the railway company enjoys a monopoly of the railway services. Applying D3 criteria could lead to qualifying the contract as a lease. A few years later, when the monopoly is lifted, the criteria would no longer apply.

In UNICE’s view, criteria that help identify the substance of a transaction must resist any change in circumstances independent of the will of the two contracting parties.

3- Valuation

Separating payments is probably the most critical issue after the analysis of the substance of the transaction has been made. And the interpretation is quite short as a source of adequate guidance. Also paragraph 10 implies that the entity will always be in a position to determine the classification of the lease. We believe that the classification might be difficult to assess whenever separating payments is not feasible.

UNICE therefore proposes the following alternative:

- the fair value of the leased asset is identified through observable transactions and the payments are separated as proposed by the draft interpretation,
- the fair value of the leased asset cannot be identified through observable transactions and the minimum contractual payments are appropriately disclosed along with a light description of the whole arrangement.

4- Convergence

In contradiction with § BC 26, we have identified situations whereby EITF 01-08 leads to the identification of a lease while they would not qualify under D3. The opposite situation may also apply. The payment criterion in D3 is not precise enough to provide clear guidance in situations where the “price” criterion is acceptable.

If the desired outcome was to reach convergence, why is there the need to try to invent different criteria?

5- Transitional requirements

UNICE does not believe that D3 should be applied retrospectively:

- a. retrospective application is burdensome because implementation relies on a very thorough and comprehensive identification process of all existing contracts; this identification process is all the more burdensome because the contracts relevant to the issue may be of a seemingly endless variety;
- b. moreover, as we have stressed before, separating payments is one of the key implementation issues. Identifying the fair value of the asset at inception may be even more problematic when carried out retrospectively.

We therefore recommend fully prospective application.

We trust that the above-mentioned remarks will be taken into account in the final EFRAG letter.

We remain at your disposal should you need any further clarification.

Yours sincerely,

(original signed by)
Jérôme P. Chauvin
Director, Company Affairs Department