



European Financial Reporting Advisory
Group (EFRAG)
35 Square de Meeûs
B-1000 Bruxelles
Belgium

9 September 2014

Dear Chairman,

Re: Lessee Accounting

We would like to express our appreciation for the additional public consultation on lessee accounting organised by EFRAG. Although some BUSINESSEUROPE members consider that too much time and effort has been dedicated to this project already without tangible progress, they acknowledge that the level of attention should not be diminished now.

BUSINESSEUROPE wrote a letter to Mr. Didier Millerot, Head Financial Reporting and Accounting Unit, DG Internal Market and Services at the European Commission, on May 15 2014. In this letter, we expressed the view that - for the time being - the IASB should limit any changes to the lease accounting literature to the improving of the disclosures on operating leases that are currently required by IAS 17, with the overall aim of providing users with the information that is believed to be missing. This would allow time for the IASB (and the FASB, as we strongly support convergence in this matter) to:

- Provide an appropriate distinction between leases and services and other executory contracts, as suggested by EFRAG, in order to ensure that only lease contracts will appear on the balance sheet;
- Further analyse and acknowledge the fundamental economic difference between leases which are essentially financed purchases of an asset and contracts which represent the purchase of flexibility for access to an asset or a purchase of services; and
- Ensure that there is a minimum level of consistency between accounting by lessees and lessors.

In our view, these are fundamental pre-requisites for a high-quality, understandable and enforceable standard on leasing.

We will call this view, which is clearly BUSINESSEUROPE's preferred solution, the "IAS 17 + additional disclosures" approach in the remaining part of this letter.



We understand that the question asked in EFRAG's additional outreach on Lessee accounting is for respondents to express a preference between the IASB approach and the FASB approach.

This question has resulted in much debate at BUSINESSEUROPE:

- There is an overwhelming view that non-convergence on such an important topic between US GAAP and IFRS is not acceptable. As leases impact nearly all companies to a varying degree, comparability between US GAAP and IFRS financial statements is absolutely paramount to ensure that users of the financial statements can perform a robust peer analysis without having to perform complex or short-cut adjustments between different companies to achieve some sort of comparability. Such an outcome, we believe, would represent no improvement whatsoever compared to the current situation.
- Also, many members fear that the IASB model as it stands today will not be endorsed by Europe, and non-endorsement would entail costly reconciliation between "IFRS as published by IASB" and "IFRS as adopted by Europe" for companies listed in the US.

BUSINESSEUROPE members have held different views at the time various EDs were published:

- Some members expressed their preference for one single model for leases, on the assumption that the IASB and FASB models would be the same and that the IASB standard would be endorsed by Europe.
- Other members expressed their preference for the "IAS 17 + additional disclosures", as they believe that IAS 17 depicts correctly two different types of contracts: "in substance acquisitions" and "assets rented for reasons of flexibility".

As stated above, all BUSINESSEUROPE members are very concerned about the recent developments and the apparent risk of non-convergence. Most members continue to believe that the "IAS 17 + additional disclosures" approach is the appropriate solution to reach a consensus among different views supported by constituents.

However, BUSINESSEUROPE is realistic enough to acknowledge that in the Boards' view too much time and effort has been spent on this topic to allow the Boards to revert to such a solution, without a perceived loss of credibility. Consequently, BUSINESSEUROPE members, in an attempt to provide constructive feedback and allow progress on this topic, have considered whether they could possibly accept a solution of the kind that the FASB is now proposing. In considering the FASB approach, members that support a single approach point out that they have such serious concerns about the economic and political risks of non-convergence and non-endorsement that they would settle for the FASB model for practical reasons, assuming this model would be endorsed.

Members that hold the second view described above could be willing to accept a FASB type model, as it retains the principle-based distinction between finance leases and operating leases as defined in IAS 17. Although it retains a full balance sheet



approach, they consider that this model is more practical and simpler to implement than any other model proposed by the IASB.

When discussing the theoretical foundation of a model that would develop into the FASB's proposed direction, BUSINESSEUROPE members noted that some believe that the FASB model is not conceptually sound, particularly the recognition of a financial liability without any financial expense. Others noted that the IASB model also raises fundamental theoretical concerns that were pointed out in a number of comment letters.

As we stated in our letter to the European Commission, "in adopting the classification principles of IAS 17, the FASB appears to have confirmed that there is a fundamental distinction between the two principal different types of lease contracts and accepted the inherent quality of the existing IAS 17's principles", which many members believe is preferable to the IASB model, which focuses on the financing element of the lease contracts and removes from the Financial Statements the important distinction between the different nature of leased assets and the underlying economic drivers for the transactions.

Taking into account the above considerations as background information to our answer, you will find below the answers to questions 3 and 4. BUSINESSEUROPE will not answer questions 1 and 2 but did encourage its constituents to answer these questions on an individual basis.

Q3 - Assuming that the Boards confirm the scope of application and the guidance to identify a lease, which of the approaches described above in paragraphs 14 to 21 do you prefer? Please explain the reasons for your views.

For the reasons explained above, most BUSINESSEUROPE members would support an approach that is based on the FASB model, as described in the EFRAG paper, if that ensures convergence and endorsement.

If there was a risk of non-endorsement of the FASB approach, BUSINESSEUROPE would recommend the "IAS 17 + additional disclosures" approach, as most members believe it is the most conceptually sound approach of the three approaches and allows users easily to perform the reconciliation with the FASB model. Assuming that the additional disclosures of the "IAS 17 + additional disclosures" approach include the discounted future operating leases payments, an operating lease liability comparable with the FASB model could easily be derived from these new disclosures.

Q4 Based on the description above, which of the two approaches you believe to be less complex and costly to implement? Please explain the reasons for your views.

Based on what is explained in the EFRAG document in paragraphs 25 and 26, most members believe that an approach based on the FASB proposal would likely be less complex and costly to implement than any other full balance sheet model.

Having said this, most of our members have not spent sufficient time in fully analyzing the FASB proposal and they have currently no view on how the liability/asset would be



measured in detail, i.e. what are the lease payment components, what is the lease term, how are options treated, what discount rate would be applied etc. They have also not investigated how such a model would work in practice and how users of financial statements would deal with the liability of operating leases. Due to that, and as many companies will often have limited information on current operating leases readily available, any proposal that would require gathering additional information compared to the current situation will result in potentially significant implementation costs, even for the FASB proposal.

We remain at your disposal should you wish to discuss this subject further.

Yours sincerely,

Jérôme P. Chauvin
Deputy Director General