



November 30, 2010

Mr. Russell G. Golden
Technical Director
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, Connecticut 06856-5116

Re: File Reference 1850-100 – Proposed ASU Leases (Topic 840)

The Accounting and Auditing Committee (the Committee) of the Pennsylvania Institute of CPAs (PICPA) appreciates the opportunity to comment on the Proposed Accounting Standards Update, Leases (Topic 840). In general, the Committee supports the FASB’s goal of establishing a principles-based approach to lease accounting and agrees that the standards should minimize the potential for off-balance sheet abuses. However, the Committee has the following specific comments:

Lease period – The proposed ASU uses an estimated probability distribution of various outcomes to determine the lease period that is “more likely than not” to occur. This methodology, which is similar in concept to the withdrawn FIN 46R Appendix A, introduces unnecessary complexity into the standards and results in a contrived lease term that is likely not to occur. Furthermore, adjusting the amounts based on revisions to this lease term creates fabricated income statement adjustments that have no meaning. We believe that the lease period should not incorporate a renewal option until it is probable that the option will be exercised. Once renewal is probable, the entire renewal period should be incorporated into the determination of the lease term.

To minimize the opportunities for transaction structuring, management’s intent could be disclosed and the likelihood of renewing the lease could be qualitatively evaluated based on the nature of lease and the company’s history of performing in accordance with their stated intentions. This provides for a more principles-based approach. Once renewal is probable, the lease period would include the renewal period. There would then be no need for partial weighing of potential outcomes. Also, the “significant assumptions and judgments” referred to in paragraph 83 would not be needed, further reducing complexity. We request that FASB revise the guidance for the lease term to reduce unneeded complexity and provide greater clarity to financial statement users.

Dissenting View – Several members of the Committee believe that the renewal periods should not be incorporated into the lease term until they are exercised. Instead, the contract terms should



dictate the accounting treatment. They believe that the accounting treatment should recognize that there is a substantive difference between a multi-year lease and a one year lease with renewal rights.

Leases with Uncertain Terms – The Committee noted that the proposed ASU does not take into consideration leases with unspecified terms; for example, leases that are billed based on the number of hours of use. As the production hours, or hours of use, are not known until after the fact, using the probable term and payments as proposed by the ASU would be equivalent to booking a budgeted number, which is completely subjective and impossible to audit.

Contingent rentals, term option penalties, and residual value guarantees – The proposed ASU requires the inclusion of contingent rentals, expected payments under term option penalties, and residual value guarantees in the lease. We agree that residual value guarantees should be incorporated into the amount of the capitalized asset and liability. However, we believe that contingent rentals should be accounted for in accordance with their substance. In addition, expected payments under term option penalties should not be incorporated into the capitalized amount until they are more likely than not to occur.

Proposed method for lessor’s accounting – The proposed ASU outlines two revenue recognition methods, a performance obligation approach and a derecognition approach, that vary depending on whether the lessor “retains significant risks or benefits associated with the underlying asset.” It is unclear why revenue recognition for a lessor would have to diverge from the revenue recognition methodology outlined in the proposed ASU on Revenue Recognition which uses a control model similar to the performance obligation approach. We support standardizing the accounting for revenue recognition to the extent possible. Lessor accounting does not appear to warrant an exception from the proposed revenue recognition standard. Furthermore, the proposed de-recognition approach adds unnecessary complexity to the standards and is too subjective. Finally, recognizing a residual asset under the proposed derecognition approach appears conceptually inconsistent.

Paragraph 27 – The Committee requests that the FASB clarify this paragraph to note whether the cash payments referenced relates to the total cash payment or only the principal portion.

Implementation Method and Timing – We agree that the transition to the new guidance should include an opening balance adjustment for the earliest prior period presented in order to make the financial statement presentation meaningful. We also agree with the simplified retrospective approach outlined in paragraph 90. However, due to the significance of the proposed changes, we request a significant lead time to implement. In addition, the required timing for implementation should take into account the potential impact of the new guidance on business



and the overall economic environment. Specifically, as a result of implementing the new standards, entities may experience a decline in credit ratings, an increase in the cost of credit, significant costs in renegotiating debt covenants, or difficulty continuing credit arrangements due to their change in financial position.

Threshold for application – The Committee recommends that the proposed ASU be applied only to an entity’s core assets so that so that basic office equipment, etc. would not be required to be capitalized. We believe that principles based guidance could be developed to assist in identifying an entity’s core assets (e.g. whether the asset is crucial to the business operations, etc.). If this threshold is not permitted for publically-held entities, we request that such a threshold be established for privately-held entities and not-for-profit organizations. We believe that privately-held companies, and not-for-profit organizations are less able to incur the implementation costs for this proposed standards update and that any effort and cost should be concentrated on the entity’s core business assets.

Exception for Privately-Held Entities and Not-for-Profit Organizations - The Committee also requests an exemption for privately-held entities and not-for-profit organizations from the following disclosures:

- Paragraph 70 (b) - Quantitative and qualitative financial information describes how leases may affect the amount, timing and uncertainty of the entity’s future cash flows.
- Paragraph 77 - “Reconciliation of opening and closing balances of right-of-use assets and liabilities”...for lessees
- Paragraph 80 - Reconciliation of the opening and closing balances for lease payments receivable, lease liabilities, and residual assets for lessors.
- Paragraph 83- “Significant assumptions and judgments and any changes in assumptions and judgments relating to renewal options, contingent rentals, term option penalties, residual value guarantees and the discount rate used when determining the present value of lease payments.”

We appreciate your consideration of our comments. We are available to discuss any of these comments with you at your convenience.

Sincerely,

A handwritten signature in black ink, appearing to read "Richard E. Wortmann".

Richard E. Wortmann, CPA
Chairman, PICPA A&A Committee