management and users of financial statements. This has been noted by other commentators. The American Accounting Association comment letter #396 states, "If future standards make it more difficult to distinguish between these two types of leases because both are capitalized, lenders may consider themselves ill served."

In a similar vein, the AIPCPA Private Companies Practice Section comment letter #614 says their Technical Issues Committee (TIC) discussed the proposal with lenders in their communities and did not find support for putting operating leases on the balance sheet. These lenders would ignore a right-to-use asset because such assets cannot serve as collateral on loans. They are able to derive information about the lease obligation from the commitments note in the financial statements and from direct interaction with management, and analyze cash flow sensitivity without considering the lease commitment a liability.

The SBAC/FASB meeting discussion regarding the lease project was very revealing as one speaker said small businesses may not follow the proposed new lease accounting rules and will accept a qualified opinion so that their lenders would get the balance sheet "right" for debt limit covenants (operating/executory lease obligations are not debt in bankruptcy) and for tangible net worth covenants (operating/executory leases create intangible assets and the liability is not debt). If small businesses will not follow the requirement to capitalize leases so that their lenders best understand the substance of leases reported in their financial statements that has to be saying the proposed accounting in the Exposure Draft (ED) is not providing the most relevant information to suit lenders' needs.

In my opinion the Boards should also refine the "official" stated definition of debt in your glossary of terms to help lenders in their analysis. Merely defining debt as what is owed does not help users understand how a lease liability will be treated in a bankruptcy. It seems that the Boards and lenders do not have the same definition of the word "debt". The Boards should be concerned with the impact on debt limit and tangible net worth covenants as they are common in lease and loan agreements. Small and medium sized companies are heavy users of leases and are more prone to bankruptcy so it is most important to properly classify and label the executory lease ROU asset and liability for the benefit of their lenders.

- Small ticket/immaterial lease portfolio solution – A portfolio approach to small ticket leases will still be complex. Not all master leases have homogeneous assets with one delivery date and one lease term. Also the leases in the immaterial portfolio group may have reassessment issues such as variable rents, residual guarantees and renewal/purchase options. The individual leases will have different incremental borrowing or implicit rates and lessees will have to establish a convention with regards to the discount rate used versus the portfolio. The portfolio will need continual adjustment when the leases in the portfolio are added, drop out, or change. I suggest the elimination of the need to reassess those leases considered to be immaterial. I also suggest field testing of the portfolio concept prior to further review.

As an alternative for small ticket/immaterial operating lease accounting simplifications I suggest using the accounting method for ***all*** operating leases recommended by comment letters from me, the ELFA and FEI which may be called the "Display" method. In that case one can use an Excel spread sheet to

capture future lease payments of each lease, material or not, and, using the unique discount rate for each lease, discount them to calculate the amount/value of the lease asset and liability to be reported on balance sheet. The lease cost recognized would be the accrued average rent which is easily calculated in the Excel spread sheet. Using this "Display" method is very simple and would use an Excel file as most preparers currently use to capture future operating lease obligations for footnote reporting. Merely "displaying" the value of the assets and liabilities on the balance sheet would achieve the goal of capitalizing operating lease assets and obligations while preserving the lease accounting regime in current GAAP. More importantly the "Display" method handles initial direct costs, landlord concessions, rent free periods, impairment, variable payments and changes in assessment of the lease term easily compared to both Type A & B accounting where complex recalculations of the asset, liability and future amortization are required. The Boards should understand that it is very common to have CPI variable adjustments in leases that will result in high costs to adjust under both Type A and B methods often occurring on an annual basis for ***each*** lease.

- Lessor Selling Profit – I ask the Boards to view when a lessor can record a sale from the lessor's perspective rather than the lessee perspective as is proposed. In my opinion, a lessor can sell /give up control of the various rights inherent in an asset (an asset is a bundle of rights – rights of use and rights of ownership) to more than one entity. I suggest that you consider third party residual buy back agreements, third party guarantees and residual insurance as factors in lessor revenue/sale recognition as they are a factor in whether a lessor has sold the ownership rights in the asset. As proposed only residual guarantees from the lessee are considered in determining lessor revenue/sale recognition.

- Complexity – Complexity depends on what your definition of complexity is and what the amount of work/cost that results from the complexity is. I think the issue is to analyze and weigh complexity in lease classification vs. complexity in ongoing accounting. Current GAAP lease classification may be complex (until you learn the tests) but it is well understood, has been in effect and working well since 1976 and it is in line with the legal and tax view of leases. I do not view that as being bad or complex - rather the approaches in ED1 or ED2 add complexity for users in ongoing compliance (reclassifying leases based on current GAAP for tax compliance and user/lender questions (see the AAA comment letter #396)) as well as the P&L accounting for Type A accounting and ED2 Type B when you have a variable rent or reassessment adjustment. CPI adjustments alone will mean complex adjustments will be an annual event for many leases. Also the ED2 classification tests are more complex than current GAAP as they differ by asset type, one needs to define what assets are property versus equipment and there are leases with both property and equipment components that have to be dealt with. All things considered, in my opinion, using current leases GAAP lease classification methods plus the "Display" method for accounting for former operating leases as a framework would reduce complexity in classification and ongoing accounting for preparers and users compared to the ED1 and ED2 choices.

I value the relationship built over the years with the FASB and IASB. The Boards and staff have always given me access and allowed me to provide my views on various accounting and financial reporting matters. In the past, members of the Boards and staff have given my input consideration, which I appreciate. In some cases, the decisions and outcome have reflected this consideration. I hope that my input here is valuable to furthering the mission of the Boards to help improve transparency in financial reporting. I look forward to continuing to work with the Boards and staff on this matter and stand ready to assist in any way I can.

Sincerely,

William Bosco
Leasing 101