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October 25, 2017

Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
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**RE: Proposed Accounting Standards Update, *Land Easement Practical Expedient for Transition to Topic 842* (File Reference No. 2017-290)**

Dear Technical Director:

We appreciate the opportunity to comment on the proposed ASU, *Land Easement Practical Expedient for Transition to Topic 842*.

**Clarifying the guidance applicable to land easements**

We support the Board's proposal to clarify that land easements, as rights to use land (i.e. identified property), are within the scope of Topic 842, and to amend Example 10 in ASC section 350-30-55 to clarify that the entity evaluated the perpetual land easements under Topic 842 and determined that they did not meet the definition of a lease, before the entity accounted for them as intangible assets.

In view of the Board's objectives to have lessees recognize all leases with a term greater than 12 months on the balance sheet, and for all entities to provide enhanced disclosures about their leasing activities, we believe it is important to clarify that *all* rights to use property, plant and equipment are within the scope of Topic 842 and should be evaluated to determine whether they meet the definition of a lease. We do not believe some rights to use property should be excluded from the scope of Topic 842 based solely on how they are labelled (e.g. as an 'easement' or 'right-of-way' versus a 'ground lease' or other similar term).

**Transition practical expedient**

We support the Board's proposed practical expedient related to land easements not previously assessed under (i.e. previously deemed not to be in the scope of) Topic 840. We believe this is a reasonable cost-benefit accommodation.

*Scope of the proposed practical expedient*

As proposed, land easements already deemed to be in the scope of Topic 840 (i.e. those that would have already been assessed under Topic 840) would be subject to the same transition provisions as all other arrangements that were in the scope of Topic 840. This proposed practical expedient being one of scope is understandable given the feedback received about this issue by the staff and Board members as part of the Board's outreach activities, which is that many entities, under current GAAP, have considered land easements to be intangible assets in the scope of Topic 350 or components of other property, plant and equipment (e.g. part of the cost of a pipeline asset) in the scope of Topic 360. Those entities did not, therefore, consider the easements to be in the scope of Topic 840 and evaluate whether they met the Topic 840 definition of a lease. The proposed practical expedient being limited to scope is further

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understandable given that a practical expedient related to the definition of a lease (i.e. lease identification) already exists in ASC paragraph 842-10-65-1(f).

We are aware that the Board has been asked to expand its proposal to allow this practical expedient to apply to all easements that were not *accounted for as leases* under Topic 840, rather than just those that were *assessed* under Topic 840 or to which Topic 840 was *applied* (any may not have met the definition of a lease in that guidance). As proposed, land easements already deemed to be in the scope of Topic 840 would be subject to the same transition provisions as all other arrangements that were in the scope of Topic 840. This would include, for example, assessing whether those easements meet the definition of a lease under Topic 842 (if the package of practical expedients in ASC paragraph 842-10-65-1(f) is not elected), or were appropriately evaluated to determine whether they met the definition of a lease under Topic 840 (as described in paragraph BC393(a) of ASU 2016-02 if the package of practical expedients in ASC paragraph 842-10-65-1(f) is elected). If expanded as requested, the practical expedient would grandfather easements that were deemed to be outside the scope of Topic 840 *and* easements that were deemed to be in the scope of Topic 840 but were determined not to meet the Topic 840 definition of a lease. In other words, for this class of transactions only:

- an entity that does not elect the package of practical expedients in ASC paragraph 842-10-65-1(f) would not be required to reassess whether it would meet the new Topic 842 definition of a lease *even if those easements were deemed to be in the scope of Topic 840*; and
- errors in conclusions about whether land easements that were deemed to be in the scope of Topic 840 met the Topic 840 definition of a lease would be grandfathered (which is otherwise prohibited by paragraph BC393(a) of ASU 2016-02) for an entity that elects the package of practical expedients in ASC paragraph 842-10-65-1(f).

We do not believe the impetus for expansion of the proposal is to create an additional lease definition practical expedient for land easements. Rather, we believe that the requests are driven by concerns about the efforts an entity would have to undertake to identify the population of land easements that were in the scope of Topic 840 – i.e. how will that entity prove what easements were or were not assessed under Topic 840 before the effective date of Topic 842. If the Board wishes to consider other options, we believe there may be an alternative approach to address that concern that would not involve grandfathering Topic 840 lease identification *errors* for land easements only, or permitting entities not electing the package of practical expedients in ASC paragraph 842-10-65-1(f) to avoid lease identification reassessment under Topic 842.

Stakeholders raised similar concerns about the Board’s proposed use of the ‘portfolio approach’ in the application of Topic 606 and Topic 842. In response to the portfolio approach proposal in the 2011 Exposure Draft of the new revenue recognition standard, stakeholders expressed concerns that the portfolio approach would be of little expedient value because entities would be required to prove quantitatively that the result of applying a portfolio approach did not differ materially from applying the standard on a contract-by-contract basis. In response to that concern, the Board included language in ASU 2014-09 (and again in ASU 2016-02 on leases) that has generally resulted in acceptance that use of the portfolio approach under either standard does *not* require a quantitative “with and without” type analysis.

*BC69. ...In their discussions, the Boards indicated that they did not intend for an entity to quantitatively evaluate each outcome and, instead, the entity should be able*

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*to take a reasonable approach to determine the portfolios that would be appropriate for its types of contracts.*

We believe the Board could similarly clarify in a final land easements ASU that, in identifying land easements that were previously assessed under Topic 840, it does *not* intend for the presumption to be that an easement was assessed under Topic 840 unless the entity can prove otherwise. However, an entity would not be permitted to disregard ‘readily available’ (or similar) evidence that an easement was subject to assessment under Topic 840. Such evidence may include, for example, financial statement disclosures, accounting policy documents, accounting process narratives and controls related to the accounting for easements, or other clear evidence of the entity performing lease identification assessments for those easements.

We believe this alternative approach would resolve the potential issue that we believe is the reason for the request to expand the proposed practical expedient, while not either (1) creating a “special” class of transactions that obtains a second lease definition practical expedient, or (2) grandfathering actual errors in the application of Topic 840 by entities to arrangements within its scope.

*Application of consistent accounting policies until the Topic 842 effective date*

We support the Board’s position, as expressed in paragraphs BC13 and BC15 of the proposal, that an entity should maintain its current accounting policies for land easements up to the effective date of Topic 842. These paragraphs clarify the Board’s intent for the practical expedient to apply to only those easements that commence before the effective date of Topic 842 and for which the entity has maintained a consistent accounting policy that they are not in the scope of Topic 840.

We believe it would be useful for the Board to clarify that the discussion in paragraphs BC13 and BC15 precludes an entity from ‘re-characterizing’ arrangements as easements. Consider an entity that has easements to place a telecommunications cable or a pipeline beneath landowners’ property and has an accounting policy before the effective date of Topic 842 that those easements are intangible assets in the scope of Topic 350. We do not believe that the Board intends for that entity to be permitted to apply that policy to additional classes of existing or new arrangements before the effective date of Topic 842 by referring to (or re-characterizing) those arrangements as easements. For example, if that entity had ground leases on which it had constructed storage sheds or integral equipment, it would not be appropriate to re-characterize them as easements before the effective date of Topic 842 in order to apply its accounting policy for the telecommunications cable or pipeline easements to those arrangements.

#### **Additional guidance on applying the definition of a lease to land easements**

We suggest that the Board consider providing additional guidance in the Codification about how to apply the definition of a lease to land easements (regardless of how the practical expedient is designed). Addressing the fact patterns outlined in paragraphs BC3 and BC4 of the proposed ASU would help address the risk of significant diversity in practice in applying the definition of a lease to those scenarios. Paragraph BC10(a) of the proposal states that many land easements – e.g. perpetual land easements – would not meet the Topic 842 definition of a lease. We believe that view would be better expressed in the amendments to the Codification section of the final ASU than in the Basis for Conclusions. Clarifying the Board’s position with respect to perpetual easements could likely be accomplished by adding a few more

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words to Example 10 in ASC Section 350-30-55 beyond what is suggested in the proposal. Our suggested edits to Example 10 are:

**> Example 10: Easements**

**350-30-55-30** Entity A is a distributor of natural gas. Entity A has two self-constructed pipelines, the Northern pipeline and the Southern pipeline. Each pipeline was constructed on land for which Entity A ~~owns~~has perpetual easements. Those easements were evaluated under Topic 842 but did not meet the definition of a lease because they are perpetual and, therefore, do not convey the right to use the underlying land for a period of time. The Northern pipeline was constructed on 50 easements acquired in 50 separate transactions. The Southern pipeline was constructed on 100 separate easements that were acquired in a business combination and were recorded as a single asset. Although each pipeline functions independently of the other, they are contained in the same reporting unit. Operation of each pipeline is directed by a different manager. There are discrete, identifiable cash flows for each pipeline; thus, each pipeline and its related easements represent a separate asset group under the Impairment or Disposal of Long-Lived Assets Subsections of Subtopic 360-10. While Entity A has no current plans to sell or otherwise dispose of any of its easements, Entity A believes that if either pipeline was sold, it would most likely convey all rights under the easements with the related pipeline.

With respect to time-based land easements, there is ongoing debate about whether surface land use rights can or should be separated from subsurface use rights. While we believe Topic 842 is clear that any parcel of land can be an identified asset and, therefore the subject of a lease – e.g. any parcel of land on which a structure is or can be built or a piece of integral equipment such as a cellular tower or wind turbine is or can be installed (even if only *implicitly* specified) – there is ongoing debate about whether the subsurface land in which a pipeline or telecommunications cable is buried can be an identified asset separate from the land surface above it. We believe the Board should provide guidance on this distinction to help ensure consistency in practice.

We understand that the Board may be reluctant to provide additional guidance on the definition of a lease because the Topic 842 definition is converged with the definition in IFRS 16. However, we believe that the need for guidance on the accounting for land easements in the United States, as evidenced by the need for this proposed ASU, outweighs potential convergence considerations. We also believe this could be accomplished without amending the guidance on the core definition of a lease. For example, the Board could provide this additional guidance through an example demonstrating application of the definition of a lease to land easement scenarios.

While we recommend that the Board provide additional authoritative guidance about applying the definition of a lease to land easements, if the Board decides not to do so, we believe the Board should expand on the views expressed in paragraph BC10 of the proposal to address time-based easements. We would be happy to meet with the Board or its staff or otherwise offer our assistance if that would be helpful.

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**Additional guidance on identified assets**

There is currently ongoing discussion in practice about some Board members' comments at the July 12, 2017 easements roundtable. Specifically, comments about identifying the unit of account in some lease scenarios requiring judgment (including, but not limited to, land use scenarios), and therefore some diversity in application naturally being expected. We interpreted those comments as recognition by those Board members that facts and circumstances often differ (even for arrangements involving the right to use similar underlying assets), rather than an intent to communicate that they expect diversity to exist when accounting for substantially the same facts and circumstances (regardless of the underlying asset), or that Board members' expectations of some diversity equates to permitting a policy election in the application of the identified asset guidance. If our understanding of those Board members' comments is correct, we agree and support them, and do not think the Board needs to provide additional guidance related to those comments or on identified assets more broadly. However, if our interpretation of those Board members' comments is not correct, we suggest that the Board clarify what it views to be acceptable diversity with respect to the identified asset guidance either in this final ASU or in some other formal manner.

\* \* \* \* \*

Our responses to the Questions for Respondents are included in the Appendix to this letter.

If you have questions about our comments or wish to discuss the matters addressed in this comment letter, please contact Kimber Bascom at (212) 909-5664 or [kbacom@kpmg.com](mailto:kbacom@kpmg.com), or Scott Muir at (212) 909-5073 or [smuir@kpmg.com](mailto:smuir@kpmg.com).

Sincerely,



KPMG LLP

## Appendix – Responses to Selected Questions for Respondents

### Question 1:

**Would the land easement practical expedient in this proposed Update reduce the cost and complexity to implement Topic 842? If not, please explain why.**

Yes. We believe permitting entities not to revisit earlier decisions about whether land easements are in the scope of Topic 840 will ease the transition to Topic 842.

### Question 2:

**Would the proposed amendments require transition provisions or an effective date that is different from those for Topic 842? If yes, please explain what transition requirements and/or effective date you would recommend and why.**

No. Because the transition practical expedient eases the transition to Topic 842, we do not believe there is a need for a different effective date.

Because the clarification that land easements are in the scope of Topic 842 relates to guidance (Topic 842) that entities should already be preparing to apply, we do not think there is a reason for the Board to provide different transition guidance or a different effective date for that clarification.