January 12, 2018

Ms. Susan M. Cosper
Technical Director
File Reference No. 2018-200
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Delivered Electronically

RE: **File Reference No. 2018-200,** Proposed Accounting Standards Update, *Leases (Topic 842) – Targeted Improvements*

Dear Ms. Cosper:

The purpose of this letter is to share our views with respect to the Financial Accounting Standards Board's ("FASB" or the "Board") Exposure Draft of the Proposed ASU, *Leases (Topic 842) – Targeted Improvements* (hereafter the "ED") for the Board's consideration.

Company Background

Branded as Spectrum, we are the second largest cable operator in the United States and a leading broadband communications services company providing video, Internet and voice services to approximately 27 million residential and business customers as of September 30, 2017. We had total pro forma revenues of approximately $40 billion for our most recently reported fiscal year ended December 31, 2016 and are a public registrant whose common stock is listed for trading on the NASDAQ Global Select Market under the symbol: CHTR.

Overall Comments

We applaud the Board's ongoing efforts to proactively address implementation issues raised by stakeholders surrounding the adoption of ASU No. 2016-02 and support the FASB's specific initiative underlying this ED to reduce the cost of implementing the new leases standard by (1) adding a transition option that would permit an entity to apply the transition provisions of the new standard at the date of adoption instead of at the beginning of the earliest comparative period presented in its financial statements and (2) adding a practical expedient to permit lessors to not separate nonlease components from the associated lease components if certain conditions are met (the "Separation PE"). We believe that these amendments, if codified, will indeed meet the Board's stated goal of reducing costs around the implementation of ASC 842 across the system of financial statement preparers without sacrificing the ultimate quality of information provided to investors. With respect to the Separation PE, however, we would like to offer suggestions on the design of the expedient because we believe that the criteria required

to apply the expedient, as currently proposed, are *unnecessarily* restrictive. Further, we believe those restrictions could be removed without any sacrifice to the quality of information provided to financial statements users or additional complexity for preparers in adopting and implementing ASC 842 as compared to the proposed expedient.

Concerns in Design – Separating Components of a Contract

If codified, the Separation PE will provide lessors with a practical expedient, by class of underlying asset, to not separate nonlease components from the related lease components, similar to (1) the practical expedient provided for lessees in paragraph 842-10-15-37 and (2) the ability afforded entities under the new revenue standard to account for distinct goods and services as if they were a single performance obligation if the accounting outcome in terms of the amount and timing of revenue recognition is the same as accounting for the goods and services as individual performance obligations.

In deciding to introduce the Separation PE, the Board questioned why a lessor would be precluded from combining a lease component and a nonlease component solely because one component is within the scope of the new lease guidance and the other component is within the scope of the new revenue guidance. The FASB also highlighted that leasing is considered a revenue-generating activity and, therefore, lessors should not be precluded from combining lease and nonlease components when the timing and pattern of revenue recognition are the *same* for each component (i.e., the only differences between accounting for the lease and the associated nonlease component separately or on a combined basis are with respect to presentation and disclosure).[1]

As currently designed, however, the Separation PE would only be available to lessors in circumstances in which *both*:

1. The timing and pattern of revenue recognition are the same for the nonlease component(s) and the related lease component; and
2. The *combined* single lease component would be classified as an operating lease in accordance with paragraphs 842-10-25-2 through 25-3.

While this current design may prove useful to industries for which the *nonlease* element is a minor component of their multiple-element arrangements, it will likely provide little to no utility to industries for which the *lease* element is a minor component of their customer arrangements. This is because combining significant fixed service payments and minor lease payments all as *lease payments* would likely result in a combined component that would "fail" the present value (i.e., 90%) test in ASC 842-10-25-2(d), thereby causing the combined component to be classified as a sales-type lease and precluding the use of the Separation PE.

We are further concerned that the requirement to present the combined components as *lease* components and make the disclosures required by ASC 842 *in all cases* may prevent some lessors from electing the practical expedient or force them to provide less useful and relevant information to their financial statements users in order to be able to avail themselves of the expedient. For example, an entity for whom the combined component is predominantly a service or a good may feel *compelled*, for the operational reasons the Board has highlighted, to elect the practical expedient (if eligible). However, so long as the

[1] BC19 of the ED.

combined presentation is adequately disclosed, that entity might provide more useful and relevant information to its financial statement users if it were permitted to present and disclose the combined component as revenue from a contract with a customer (i.e., in accordance with ASC 606), rather than required to present and disclose the combined component entirely as a lease.

We believe that the separation and allocation (and faithful economic presentation and disclosure) application issues communicated to the Board by the stakeholders that have influenced the design of the Separation PE (for which leasing activities are the predominant component of the customer arrangement) are no less severe for entities for which service activities represent the predominant component of the customer arrangement (with a minor lease element included). We find it particularly troubling that entities fitting the latter scenario could be precluded from applying the Separation PE because this preclusion could reasonably cause the cost of adopting the lessor provisions of the new lease standard to be *higher* for industries with *minor* leasing activities than for those with *major* leasing activities, which would be counterintuitive. Regardless of whether the lease component is significant or minor, application issues such as difficulties in establishing a suitable method to estimate the standalone selling prices of lease and nonlease components to allocate the consideration in an arrangement on a relative basis, as well as the need for investments in technology modifications to perform such allocations on a transactional basis, prevail. Accordingly, we believe that preparers across a broad cross-section of industries would benefit from the Board altering the design of the Separation PE as described in the section that follows.

Proposed Alternatives

We believe the Board could enact relatively simple changes to the Separation PE to address both issues we highlighted in the preceding section that would not (1) take long to effect (we are aware of the truncated timeline in which the Board seeks to complete these amendments to ASC 842), (2) degrade the usefulness or relevance of the information provided to financial statement users from what has been proposed in the ED or (3) significantly complicate the application of the proposed expedient.

Restriction based on Classification of the Combined Component

Based on the discussion included in the *Background Information, Basis for Conclusions, and Alternative View* section of the ED, we believe that the Board included the second criterion to the Separation PE (regarding a *combined* lease classification test) because the Board was concerned that, absent the second criterion, the Separation PE could otherwise result in a change in lease classification (e.g., from operating to sales-type) solely due to increased amounts attributed to *lease payments* (and, therefore, in a change to the pattern of revenue recognition).[2] However, we believe that there are three alternative designs of the Separation PE that the Board could consider that, if any one of which was introduced, would also allow entities with *minor* leasing activities to apply the proposed expedient that would currently be precluded from doing so, but for whom the *fundamental principal* with respect to the concurrent timing and same pattern of transfer to the customer for the lease and nonlease components holds true.

[2] BC23 of the ED.

Those alternatives we propose be considered are as follows:

- *Alternative #1:* Simply *remove the second criterion* in paragraph 842-10-15-42A regarding lease classification on a *combined* basis. This criterion, as currently designed, adds an incremental layer of complexity to the application of the expedient that is not necessary when the spirit of the Separation PE, derived from BC116 to ASU No. 2014-09, is captured entirely by the first criterion surrounding the timing and pattern of revenue recognition. That is, there are multiple ways an entity could conclude that its timing and recognition of accounting for an arrangement on a combined basis is the same as if the arrangement components were accounted for separately. While demonstrating operating lease classification when conducting the paragraph 842-10-25-2(d) test on a *combined* basis would be one such method to demonstrate that the timing and recognition of a lease and nonlease element are the same, we do not believe it should be the *sole* prescribed method. We note that there is no specified requirement as to how meeting these criteria must be evidenced in the application of the guidance in BC116 (or in BC153 of ASU No. 2016-02, which applies to consideration of multiple lease components). We further make note of the comments of one Board member at the November 29, 2017 FASB meeting that appeared to suggest that at least his view was that the guidance in BC153 should already serve to fulfill the function of the proposed Separation PE (in the same manner as BC116 serves this function for the revenue guidance). BC153 does not contain any classification requirement such as that in proposed paragraph 842-10-15-42A(b), so its inclusion in paragraph 842-10-15-42A(b) serves to narrow the concepts in BC153 rather than codify them.
- *Alternative #2:* Provide *relief from the application of paragraph 842-10-25-2(d)* in situations where the Separation PE is applied and the lease component is reasonably considered to be only a minor component of the overall contract (i.e., the nonlease component is considered to be the predominant element). In proposing this alternative, we note that prior GAAP (Topic 840) included circumstances in which one or more of the lease classification tests were exempted from application, and that Topic 842 also includes such an instance (i.e., when the lease term commences at or near the end of the underlying asset's remaining economic life), when the result would be "illogical"[3] or "would not appropriately reflect the economics of those leases"[4]. Additionally, consistent with the discussion below, we do not believe that use of a qualitative threshold such as "minor" or "predominant" adds measurable complexity to the guidance any more than use of "at or near the same time" or "predominant" added complexity to the lease classification guidance in paragraphs 842-10-25-2 and 25-5, respectively.
- *Alternative #3:* Provide an exception to performing a lease classification test for the *combined* component when it is qualitatively clear that the lease component, if accounted for separately, would be classified as an operating lease. The concept, and language, in this respect could be similar to that in BC120 of ASU No. 2016-02 (or BC69 of ASU No. 2014-09).

[3] BC75 of SFAS No. 13.
[4] BC71(d) of ASU No. 2016-02.

Presentation and Disclosure of the Combined Component

Additionally, in order to expand the utility of the Separation PE to industries with multiple-element arrangements that contain a *minor* lease component and to *improve* the quality of information that would be provided to the financial statement users of those preparers electing the Separation PE, we suggest that the Board also permit a reporting entity for which the nonlease component(s) is (are) the predominant element(s) of the combined component to apply the presentation and disclosure requirements of ASC 606 rather than those from ASC 842. We wish to emphasize that this suggestion is *not* a "scoping" provision such as that suggested in BC25 of the ED (i.e., it is *not* a provision that would affect the *availability* of the proposed expedient). Rather, in this circumstance, we believe an entity should be permitted to make a reasonable judgment about which Topic's presentation and disclosure requirements provide *more useful and relevant* information to its financial statement users without having to sacrifice the significant operational benefits that would be afforded by the proposed expedient.

The ability to exercise reasonable judgment (in a transparent and disclosed way, including disclosure of the presence of the lease component within an ASC 606 disclosure) would only improve the financial reporting results achieved by the guidance; with an entity providing the more relevant, yet equally robust, presentation and disclosures. Further, we do not believe that making this determination – i.e., whether the nonlease element(s) of the combined component is (are) the predominant element(s) of the combined component – would be operationally burdensome or significantly judgmental for entities in that we believe in most cases it will be clear whether the nonlease or lease element of the combined component is the primary or predominant element (or if there is a predominant element at all).

In making this suggestion, we respectfully submit that the notion of predominance, if utilized, (1) would not be a new concept in the context of customer arrangement financial reporting as it was recently used in ASU No. 2016-10 with respect to the application of the sales- and usage-based royalties exception for licenses of intellectual property and (2) also already exists in ASC 842 (e.g., paragraph 842-10-25-5 pertaining to lease classification of a single lease component that contains the right to use more than one underlying asset). Additionally, we do not believe that this provision would give rise to diversity in practice in that companies in similar circumstances would be reasonably expected to reach consistent conclusions.

To assist in the Board's consideration of our suggestions, we have included illustrations in ***Appendix A*** to this letter of how we believe each alternative we have proposed might be included in ASC 842.

Conclusion

In this ED, the Board has proposed two amendments to the new leases standard that provide preparers with viable alternatives to cost-effectively adopt and implement the new guidance without sacrificing the quality of information provided to financial statement users. Further, in introducing the Separation PE, the Board has made clear that, based on its view that leasing is fundamentally a revenue-generating activity, the Board's rationale for not requiring the separate presentation of performance obligations that are delivered concurrently and have the same pattern of transfer to the customer (expressed in paragraph BC116 of ASU No. 2014-09) is no less applicable to lease and nonlease revenue, despite the guidance on leases and revenue recognition residing in two different ASC Topics. However, it is our view that the

Separation PE, as currently designed, is *unnecessarily* restrictive and limited in its utility for numerous arrangements that would otherwise meet the fundamental principal for the relief afforded by the proposed expedient. Consequently, we believe that an amendment to the proposed qualification criteria commensurate with what we are proposing would provide greater benefit across industries beyond those of the stakeholders that initially influenced the design of the Separation PE, while still achieving the overall objective of the new leases standard.

* * * * *

We greatly appreciate the time and effort the FASB has devoted, and continues to devote, to assisting with the implementation of ASC 842 and thank the Board for the opportunity to provide input as it relates to the ED.

If useful to the Board or its staff, we would be pleased to discuss these matters in further detail at your convenience.

Respectfully submitted,

/s/ Kevin Howard

Senior Vice President, Chief Accounting Officer and Controller

Charter Communications, Inc.

Appendix A – Illustration of proposed alternatives

The following examples illustrate how the Board might develop each of our proposed alternatives outlined above in the body of this letter. Changes from ASC 842 are marked (new text added is underlined), while text added to or different from that proposed in the ED is highlighted in **bold** to distinguish it from the proposed guidance.

Classification Alternatives

Alternative #1 – Eliminate the criterion that the combined lease component be classified as an operating lease

> **842-10-15-42A** As a practical expedient, a lessor may, as an accounting policy election, by class of underlying asset, choose to not separate nonlease components from lease components and, instead, to account for each separate lease component and the nonlease components associated with that lease component as a single lease component if **they will be provided over the same period of time and have the same pattern of revenue recognition.**

We believe the Basis for Conclusions to the final ASU could further explain that it is not the Board's intent to prescribe how an entity must prove that the requirements in the proposed paragraph 842-10-15-42A above are met and highlight that there has been no such requirement when applying this principle to two ASC 606 performance obligations.

Alternative #2 – Provide an exception to the application of paragraph 842-10-25-2(d)

> **842-10-15-42A** As a practical expedient, a lessor may, as an accounting policy election, by class of underlying asset, choose to not separate nonlease components from lease components and, instead, to account for each separate lease component and the nonlease components associated with that lease component as a single lease component if both of the following are met:
>
> a. The timing and pattern of revenue recognition for the lease component and nonlease components associated with that lease component are the same.
> b. The combined single lease component is classified as an operating lease in accordance with paragraphs 842-10-25-2 through 25-3. **However, the criterion in paragraph 842-10-25-2(d) shall not be used for purposes of classifying the combined lease component in accordance with this paragraph if the lease is only a minor element of the combined component (for example, the lease may be only a minor element when the lessor has a reasonable expectation that the lessee would ascribe significantly more value to the nonlease element(s) than to the lease element)**.
>
> or
>
> **842-10-15-42A** As a practical expedient, a lessor may, as an accounting policy election, by class of underlying asset, choose to not separate nonlease components from lease components and, instead, to account for each separate lease component and the nonlease components associated with that lease component as a single lease component if both of the following are met:
>
> a. The timing and pattern of revenue recognition for the lease component and nonlease components associated with that lease component are the same.

b. The combined single lease component is classified as an operating lease in accordance with paragraphs 842-10-25-2 through 25-3. **However, the criterion in paragraph 842-10-25-2(d) shall not be used for purposes of classifying the combined component in accordance with this paragraph if the nonlease element(s) is (are) the predominant element(s) of the combined component (for example, the nonlease element(s) may be predominant when the lessor has a reasonable expectation that the lessee would ascribe significantly more value to the nonlease element(s) than to the lease element)**.

Alternative #3 – Qualitative evaluation of the classification of the separate lease component

842-10-15-42A As a practical expedient, a lessor may, as an accounting policy election, by class of underlying asset, choose to not separate nonlease components from lease components and, instead, to account for each separate lease component and the nonlease components associated with that lease component as a single lease component if both of the following are met:

a. The timing and pattern of revenue recognition for the lease component and nonlease components associated with that lease component are the same.

b. There is a reasonable expectation that the application of the lease classification criteria in paragraphs 842-10-25-2 through 25-3 to the lease component on a separate basis would not result in that separate lease component being classified as a sales-type or direct financing lease.

We believe the Basis for Conclusions to the final ASU could explain, similar to the guidance in BC120 of ASU No. 2016-02 and BC69 of ASU No. 2014-09, that the Board does not intend for an entity to quantitatively prove the lease, if accounted for separately, would not be classified as a sales-type or direct financing lease because having to do so would obviate the cost and operational benefit of the separation PE.

Presentation and Disclosure of the Combined Component

The following addition (in **bold**) (presented here as an additional paragraph 842-10-15-42B but which could also simply be added as additional text to paragraph 842-10-15-42A) could be combined with any of the above classification alternatives.

842-10-15-42B For those arrangements to which the practical expedient applies, if a nonlease component(s) is (are) the predominant item(s) in the combined component, the lessor shall present and provide disclosures for the combined component in accordance with the Topic that would govern the nonlease component if it was accounted for separately (for example, Topic 606). Otherwise, including if neither the lease component nor the nonlease component(s) that comprise the combined component are predominant (for example, the lessor does not reasonably expect the lessee would ascribe significantly more value to either the lease or the nonlease component(s)), the lessor shall apply the presentation and disclosure requirements of this Topic.