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2018-200  
Comment Letter No. 41

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

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

Dear Ms. Cospers:

We appreciate the opportunity to comment on the Proposed Accounting Standards Update (ASU), *Leases (Topic 842) – Targeted Improvements*, issued by the Financial Accounting Standards Board (FASB or Board).

We support the FASB's objective to reduce the cost and complexity of applying the transition guidance in Accounting Standards Codification (ASC) 842. We believe the proposal would contribute to that objective by allowing entities to continue to apply the guidance in ASC 840, including its disclosure requirements, in the comparative periods presented in the year that they adopt the new leases standard. However, as noted in our response to question 1, we believe additional relief could be provided.

We also support the FASB's objective to address stakeholders' concerns about the requirement for lessors to separate components of a contract by providing lessors with a practical expedient, by class of underlying assets, to not separate non-lease components from the associated lease components, similar to the practical expedient provided for lessees. However, as noted in our response to question 3, we are concerned that the proposed criteria for use of the practical expedient do not accomplish that objective.

\* \* \* \* \*

Our responses to the questions in the proposed ASU are included in Appendix A. We have included other editorial suggestions in Appendix B.

We would be pleased to discuss our comments with the Board or its staff at your convenience.

Very truly yours,

## Appendix A – Responses to questions in the proposed ASU

**Question 1:** Would the proposed optional transition method to apply the new lease requirements through a cumulative-effect adjustment in the period of adoption reduce the costs and complexity associated with implementing Topic 842? If not, please explain why.

We believe the proposal would reduce the costs and complexity of applying the transition guidance in ASC 842. However, we believe the Board could provide additional relief by giving entities the option to use an alternative transition method that would allow them to apply the recognition and subsequent measurement guidance in ASC 842 to existing leases at the date of initial application.

Paragraph BC10 states that the proposed transition method would require entities to apply the transition provisions in ASC 842 to initially recognize and measure existing leases, regardless of the transition method elected. However, many of the complexities of applying the new leases standard result from the application of its transition provisions. We believe that a transition method that would permit an entity to apply the recognition and subsequent measurement guidance in ASC 842 to existing leases at the date of initial application would be less costly and complex to apply than the current transition provisions. The proposed alternative transition method would allow an entity to “grandfather” its classification under ASC 840, determine its remaining lease term under ASC 842, and apply the subsequent measurement guidance in ASC 842 as if the lease were a new lease. This transition method would simplify the accounting for existing leases in transition and eliminate the need for entities to maintain records of amounts accounted for under both ASC 840 and ASC 842 for existing leases after the effective date.

**Question 2:** Is the proposed transition method, as written in this proposed Update, operable? If not, please explain why.

We believe the proposed transition method is operable, but certain aspects of the proposal should be clarified.

The proposed transition method would require entities to continue to apply ASC 840, including its disclosure requirements, during the comparative periods presented in an entity’s financial statements. Paragraph BC9 states that the Board’s decision to provide the proposed transition method was supported by the fact that “the comparative periods would include disclosures required under current GAAP, including the operating lease obligations disclosure, such that information about the comparative period would not be completely removed.” However, the operating lease obligations disclosure required by ASC 840-20-50-2(a) is required only as of the latest balance sheet date and it is unclear whether the Board intends to amend paragraph 50-2(a) to require entities to include the required disclosure in the comparative periods. Further, ASC 840 does not require specific disclosures on an interim basis. We recommend that the Board clarify what disclosures, if any, are required in an entity’s interim financial statements that include comparative periods presented in accordance with ASC 840.

**Question 3:** Would the practical expedient in this proposed Update for lessors to not separate nonlease components from the related lease components and, instead, to account for those components as a single lease component reduce the costs and complexity associated with applying Topic 842 by lessors? If not, please explain why.

We believe that the proposed amendments would reduce the costs and complexity of applying ASC 842 for lessors. However, we believe that, as drafted, the criteria for using the practical expedient would significantly limit the population of leases to which the practical expedient could be applied.

Paragraph BC19 states that the Board's intent is for lessors to apply the practical expedient when the only difference between accounting for a lease and the associated non-lease component separately is presentation and disclosure. However, we do not believe the proposed criterion in ASC 842-10-15-42A(a) accomplishes this objective. We believe the "pattern" of revenue recognition for the lease and non-lease components will often differ, but the amount of revenue recognized in each reporting period will be the same, regardless of whether the lease and non-lease components are combined.

For example, a lessor that receives a fixed payment for leased space and variable payments for common area maintenance (CAM) accounts for the fixed lease payment as income on a straight-line basis. The variable CAM payments are recognized in the period when the changes in facts and circumstances on which the variable payments are based occur and when earned. In this example, the only difference between accounting for the lease and the associated non-lease component separately is are presentation and disclosure (i.e., the amount of revenue recognized in each reporting period would be the same, regardless of whether the lease and non-lease component are combined). However, the lease and non-lease component do not have the same pattern of recognition and, therefore, the lessor would not be able to use the proposed expedient.

We recommend that the Board simplify and clarify the criteria that must be met to elect the practical expedient. We suggest the Board amend proposed paragraph ASC 842-10-15-42A to align conceptually with paragraph BC 153 in ASU 2016-02 as follows:

As a practical expedient, a lessor may, as an accounting policy election, by class of underlying assets, choose to not separate non-lease components from lease components and, instead, to account for each separate lease component and the non-lease components associated with that lease component as a single lease component if accounting for multiple components of a contract as a single component would be similar in each reporting period as accounting for the components separately.

We suggest that the Board include examples in ASC 842-10-55 to illustrate how an entity would apply proposed paragraph ASC 842-10-15-42A. For example, the Board could include examples illustrating how a real estate operating company would apply the expedient to a contract that includes a lease of a building and a related non-lease common area maintenance services component. The Board also could include an example illustrating how the expedient would be applied to a drilling contract that includes a lease of a drilling rig and a related non-lease service component. Alternatively, the Board could discuss examples illustrating application of the proposed practical expedient at a public education session.

**Question 4:** Is the proposed practical expedient, as written in this proposed Update, operable? If not, please explain why.

We believe the proposed practical expedient is operable. We recommend that the Board clarify to which leases the practical expedient can be applied in order to improve its operability.

We believe it was the intent of the Board to allow entities to apply the practical expedient to some, but not all, lease and non-lease components in a contract that contains at least one lease component and one related non-lease component that do not meet the requirements in proposed paragraph ASC 842-10-15-42A. As drafted, we believe the proposed update is unclear on this point.

For example, assume that Lessor elects the practical expedient and enters into a contract that includes a lease of space in a building, non-lease common area maintenance services and other related non-lease services. Lessor determines that the other related non-lease services do not meet the requirements in proposed paragraph ASC 842-10-15-42A. As drafted, the proposal is unclear about whether Lessor can apply the practical expedient in this example. We believe that it was the Board's intent that Lessor would account for the eligible components (e.g., the lease and common area maintenance) as a single component and would separately account for the other related non-lease services as a separate component. We also recommend that the Board clarify whether entities could elect the proposed practical expedient for all leases that exist at the date of initial application or whether the expedient is only available for new or modified leases accounted for under ASC 842.

Further, if the Board decides to finalize the proposed criteria for use of the practical expedient, we recommend that the Board clarify how an entity that elects the package of practical expedients in ASC 842 and previously accounted for lease components and associated non-lease components separately under ASC 840 would evaluate whether the combined lease component is an operating lease. For example, it is unclear whether a lessor would apply the classification guidance in ASC 840 or ASC 842 when evaluating the proposed criterion in ASC 842-10-15-42A(b). We note that lessees may have similar questions in determining whether they are eligible to apply the practical expedient to not separate the lease component from associated non-lease components.

**Question 5:** Would the information in the financial statements, including disclosures, provided by lessors electing the practical expedient in this proposed Update be decision useful? If not, please explain why.

Yes, we believe the information in the financial statements, including disclosures, provided by lessors electing the practical expedient in this proposal would be decision useful. Given the diverse needs of the users of financial statements, we recommend that the Board conduct outreach about whether the proposal would provide decision useful information to them.

## **Appendix B – Editorial comments**

ASC 842 provides illustrations of lessee transition to the new leases standard. Lessee transition examples 28 and 29 describe the date the lessee first applies the guidance in ASC 842 as the beginning of the earliest comparative period presented in the financial statements. We recommend that the Board clarify that, in these examples, the lessee has not elected the proposed transition method that would allow it to present comparative periods in accordance with ASC 840.

We also suggest the FASB include a reference to proposed paragraph ASC 842-10-15-42A in ASC 842-10-15-30 and ASC 842-10-55-17, which currently refer only to other paragraphs related to lessor allocation of consideration in the contract to lease and non-lease components.