



September 12, 2018

Ms. Susan M. Cospers
Technical Director
File Reference No. 2018-260
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116
director@fasb.org
Delivered Electronically

Subject: File Reference No. 2018-260, FASB Exposure Draft, *Narrow-Scope Improvements for Lessors*

Dear Ms. Cospers,

STORE Capital Corporation (STORE or the Company) appreciates the opportunity to comment on the proposed Accounting Standards Update (ASU) on ***Leases (Topic 842): Narrow-Scope Improvements for Lessors*** (the exposure draft), issued by the Financial Accounting Standards Board (FASB or Board).

STORE is a publicly-traded, internally managed net-lease real estate investment trust, or REIT, that acquires, manages and currently leases over 2,000 Single Tenant Operational Real Estate (i.e., "STORE") locations in 49 states. STORE is dedicated to single-tenant, net-leased profit-center real estate where our locations are integral to the business of our tenants. STORE's portfolio of net-lease real estate investments totals approximately \$6.5 billion with granular investments that average just over \$3 million per property. The portfolio is highly diversified with no single tenant's rent exceeding much more than 3% of our revenues. STORE's senior leadership team has been investing in single-tenant operational real estate for over 30 years, at STORE and at two prior, successful publicly-traded REITs.

Nearly all (more than 99%) of STORE's leases are triple-net; therefore, our tenants are required by their leases to pay the real estate property taxes, insurance and maintenance associated with the properties that they lease from STORE. The vast majority of our leases are originated through sale-leaseback transactions of individual property locations where the seller/lessee simply continues to pay these costs after the sale, directly to the third party (i.e., taxing jurisdictions and other vendors). If a property becomes vacant through a tenant default or expiration of the lease term with no tenant renewal, STORE incurs the property costs not paid by the tenant, as well as those property costs accruing during the time it takes to locate a substitute tenant or sell the property. STORE may also accrue and recognize an expense for property costs, such as property taxes billed in arrears, if the Company believes the tenant is likely to vacate the property before these obligations are paid. As vacancies are rare (i.e., less than 1% throughout the history of the Company), STORE incurs property costs very infrequently.

We appreciate the FASB's objective to simplify the implementation and continued application of Topic 842 by lessors resulting in a cost reduction to financial statement preparers and thus to current investors. We do not believe that the proposed changes provide any less useful information to users of financial statements.

Sales Taxes and Other Similar Taxes Collected from Lessees

We support the Board's objective to address lessor stakeholders' concerns about costly and complex evaluations required to determine whether sales taxes and other similar taxes are collected on behalf of third parties. We agree with the Board's proposed amendment to permit lessors, as an accounting policy election, to not evaluate whether certain sales taxes and other similar taxes are costs of the lessor or costs of the lessee. Instead, lessors would account for those amounts as if they were costs of the lessee and exclude them from lessor lease revenue and expenses (i.e., "net reporting").

Certain Lessor Costs Paid Directly by Lessees

We support the Board's objective to address lessor stakeholders' concerns that reporting lessor costs paid by lessees directly to third parties on behalf of the lessor would be costly and complex, with limited, if any, financial reporting benefits to users of lessors' financial statements. We believe the Board's proposal would contribute to that objective; however, as discussed below, we believe additional relief should be provided.

We believe that the Board should allow lessors, as an accounting policy election (similar to the proposed election related to sales taxes), to not evaluate whether certain lessor costs paid directly by lessees are *readily determinable*. Instead, lessors could elect to account for those amounts as if they were costs of the lessee and exclude them from lessor lease revenue and expenses (i.e., "net reporting"). We believe that "gross reporting" ultimately masks the data that the users of lessor financial statements truly need. While this accounting policy election would apply broadly to all lessee-paid costs, our discussion below is focused on property taxes. We believe that lessors should be permitted to make this additional election for the following four reasons:

1. Operational Challenges

Under STORE's triple-net leases, our tenants are required to pay all expenses associated with the operation and maintenance of the property, and that includes real estate property taxes and building insurance. As noted above, the vast majority of our leases originate with sale-leaseback transactions where the seller/lessee previously paid these costs as the property owner; under their STORE lease, the lessee simply continues to pay the same costs.

Upon STORE's acquisition of a property to be leased under a triple-net lease, the recorded deed to the property sets forth the tenant's name and address for purposes of receiving all property tax information (i.e., assessments, notices and bills).

Thereafter, all real estate property tax assessments and the related billing statements are mailed by each jurisdiction directly to our tenants, at their specified address. Our tenants make payments as required by the lease directly to the jurisdictions and, in fact, could independently initiate real estate property tax protests without our assistance, when allowed by the jurisdiction.

We have no visibility into any part of our tenants' processes (the assessment, the billing or the payment) and most importantly, none of our tenants are required under the terms of our current triple-net leases to provide any of this information to us. If STORE were to require tenants to provide property tax

information under terms of their leases, we would have to renegotiate this provision into all outstanding leases, it would add an unnecessary burden to our tenants and it would be challenging and time-consuming to enforce. As the lessor, STORE would have little leverage and no practical recourse if this information were not provided by a tenant (i.e., STORE would be reluctant to declare a default under the lease simply because the lessee did not provide property tax information).

We have researched the availability of property tax information from jurisdictions in which we have properties. The information is technically available to us as the property owner; however, the lessee receives property tax information directly from, and makes required payments directly to, the respective jurisdictions under terms of our triple-net leases. Therefore, it would create undue cost and effort for STORE to attempt to independently and separately obtain all relevant billing and payment information on our granular, 2,000+ property locations from the jurisdictions. Additionally, our 2,000+ property locations have greater than 2,000 taxing authorities because a single location often has multiple parcels and each parcel can have two to three taxing jurisdictions levying property taxes.

To further illustrate this, below are several broad challenges as well as specific examples of the burdensome nature of obtaining the required information directly from the respective jurisdictions:

- There is currently no “single source” to obtain property tax information, as jurisdictions are all separate entities with no common database.
- The large and varied number of taxing authorities (county, city, town, school district, etc.) on a single property parcel complicates the process to obtain information.
- Duplicate property tax information generally cannot be requested on a recurring basis (i.e., the jurisdiction is unable to send one copy to the tenant and a second copy to STORE, as the owner).
- Certain jurisdictions (e.g., Cranberry Township, PA and Allegheny Township, PA) do not have online information available where a lessor could retrieve property tax assessments, notices, invoices or tenant payment information. Alternatively, an email, telephone call, fax or letter is required to obtain a copy of any recent property tax information. A lessor like STORE would likely need to contact the same jurisdiction multiple times during the fiscal year to receive all necessary information on a single property.
- Certain jurisdictions in some states limit the number of bills to be requested or questions to be asked per phone call (e.g., certain jurisdictions in California).
- Certain jurisdictions have limited business hours (e.g., only open 9AM to 3PM Monday, Tuesday and Wednesday) so lessors are only able to contact them during certain times. This is true in several states (e.g., jurisdictions in Alaska, Maine, Maryland, Michigan, Pennsylvania as well as others).

To potentially address Topic 842’s requirement to report certain lessor costs paid by lessees directly to third parties on behalf of the lessor in our financial statements, we have explored the option of engaging a third-party provider who offers property tax administration and employee resources to obtain and report on property tax assessments, billing and payments. This approach would eliminate any burden on our tenants to provide STORE with the information. The provider would manually obtain the information by searching websites, calling, faxing and/or writing to jurisdictions and enduring all of the challenges outlined above. The provider estimates that this ongoing service would require four (4) full-time

equivalents (FTEs) (including three (3) offshore FTEs to minimize the cost) and would cost STORE \$80,000 to \$100,000 per year based on our current portfolio size. We would expect the cost to increase as our portfolio continues to grow. One-time onboarding costs would exceed \$50,000. Such costs would ultimately be borne by our shareholders.

If it is necessary to attempt to collect this information for financial reporting purposes, we will be required to create documented, SOX-compliant, auditable processes to account for and report on property taxes paid by the lessee in our financial statements. However, as there is no STORE cash inflow or outflow related to the property tax revenue and expense associated with the lessee-paid costs, we face additional challenges as to how we will capture amounts paid, reconcile outstanding balances and true-up any changes in estimates. Needless to say, the requirement to be SOX-compliant would also entail added time and expense that would be borne by our shareholders.

STORE acknowledges that it is sometimes necessary to obtain property tax information for vacant properties, but only on a very limited basis as vacancies have been less than 1% throughout the history of the Company. When a property becomes vacant through a tenant default or expiration of the lease term with no tenant renewal, we incur all property costs not paid by the tenant, as well as those property costs accruing during the time it takes to locate a substitute tenant or sell the property. STORE may also recognize expense for property costs, including property taxes, if the Company believes the tenant is likely to vacate the property before these obligations are paid. In these infrequent situations, we initiate the manual process to obtain the information from the jurisdiction, accrue any necessary costs and reflect such amounts in our income statement. Because it is so infrequent, we are able to manage this process internally and have allocated limited resources to do so (approximately 0.5 FTE). This is the only instance where obtaining property tax information is integral to our business and provides meaningful information to our financial statement users, as it results in a net expense and cash outlay to STORE. Given the traditionally high rate of occupancy at STORE and at other companies engaged in providing net-lease real estate capital, it is the property management costs that we incur directly that investors and analysts most want to see.

2. Lack of Value to Management or Financial Statement Users

We believe that recording the property taxes paid directly by our lessees in STORE's financial statements (on a gross basis as an equal revenue and expense) would not provide users of our financial statements with any financial reporting benefits or decision-useful information for several reasons.

First, our triple-net leases obligate the lessee to pay property taxes (directly to the respective jurisdiction) because property taxes are costs associated with the utilization of the property to operate the business of the tenant. Property taxes largely support programs in the community where the property is located such as: local municipal employees (police, firefighters and the local public works department), organized recreation (parks and other recreational areas) as well as traffic and street lights, sidewalks and public transportation. Property taxes also fund local public schools in many areas. When taking into consideration the purpose and usage of property taxes collected by a jurisdiction, we believe the tenant, as a member of the community, serving members of the community, receives the greatest benefit for the payment of property taxes, not the lessor located in another city/state.

Second, property taxes related to occupied, leased properties do not represent costs for STORE to conduct our business. Management allocates no resources related to personnel, third-party services, capital expenditures, or any other business functions based on property tax assessments. Property taxes are costs of our tenants' businesses, not a cost of STORE's business. Management has never made a business decision based on property taxes assessed to occupied, leased properties.

Third, as property taxes paid by a lessee are not ultimately a cash outlay or expense to STORE, the information is not decision-useful to an investor. By grossing up our revenues for property tax payments made by the lessee and then by grossing up our expenses, by including the identical amounts due to the respective jurisdictions, we would effectively be lowering our gross and net profit margin percentages and distorting the economic fundamentals of our business. Through the operation of three successful, publicly-traded companies over 30 years, the STORE senior leadership team has never once had a shareholder request information regarding the gross amount of property taxes paid by our tenants. We do recognize that investors may be interested in the amounts that are ultimately deemed uncollectible as this reflects a shift in burden from lessee to lessor. When this burden does shift to STORE, we accrue any necessary costs and reflect such amounts in our income statement therefore providing meaningful information to our investors, as it results in a net expense and cash outlay to STORE. As noted earlier, it is this direct property management cost that investors and analysts want to understand; therefore, we take the time to address this, both in our management discussion and analysis (MD&A) and in our regular quarterly earnings conference calls.

Fourth, we do not believe that our analysts, investors or lenders will consider the gross-up of revenues and expenses meaningful. Therefore, including such information will not only impose a cost burden to our shareholders as discussed above, but we believe it will require us to "undo" the gross-up and provide our revenues and expenses on a net basis (through a non-GAAP measure) in our MD&A in order to illustrate our true profit margin percentages. Grossing up revenues and operating costs will also render companies less comparable, since the net-lease real estate portfolios that they hold may have different property tax characteristics. Were we to not provide a non-GAAP measure in our MD&A to present revenues and expenses on a net basis, we fully believe that analysts, investors and lenders will request that we separately provide enough information to allow them to eliminate the gross-up before utilizing our reported results to complete any financial modeling. In fact, our failure to deconstruct the revenue and expense gross-up associated with our tenants' obligations would result in the diminution of our current disclosure related to the portion of such costs that we bear directly. Without a deconstruction of revenue and expense gross-ups, we would have gone through extensive time, effort and cost to attempt to disclose information that no one has ever requested and, in that process, concealed material information that everyone wants to see.

We directly contacted several of our lenders to obtain their input and perspective on the gross-up of lessor costs paid directly by lessees in the income statements of lessors. Several lenders indicated that the gross-up of revenue and expense would detract from the information they do need and not a single lender believed there was any value in this presentation. Many stated that they would have to eliminate the gross-up when reviewing our financial statements. Others expressed that such a presentation was not applicable to a triple-net lessor and it is not appropriate to try to compare a triple-net lessor to a gross lease real estate investment enterprise. The former is engaged in an alternative form of tenant real estate financing resulting in generally predictable and stable income streams, while the latter is engaged in more speculative real estate investing and development that generally accompanies

elevated return volatility. Finally, one lender expressed that banks “care about net income and free cash flow, not a noncash gross-up.”

We believe that it is important to consider the two reasons discussed above together: when the application of GAAP requires significant incremental costs to a company (as noted above in **Operational Challenges**) AND provides no value to the business, to the Company’s critical decision makers and most importantly to the users of the financial statements, it becomes a costly compliance exercise without substantive benefit or meaning.

3. No Impact to Net Income

Reporting lessor costs paid directly by lessees as both a revenue and an expense in the financial statements of the lessor results in a net zero impact to net income and net income per share.

Additionally, there is no cash inflow or outflow for STORE associated with the reported revenues and expenses.

As noted above, in the infrequent situations where STORE is responsible for property taxes due to a default or vacancy, we accrue any necessary costs and reflect such amounts in our income statement which provides meaningful information to our financial statement users, as it results in a net expense and cash outlay to STORE.

4. Interpretation of “Readily Determinable”

We note that the Board decided that a lessor should exclude from rental revenue lessor costs paid by the lessee to a third party when the amounts are not *readily determinable* by the lessor. We further note that the Board decided to propose using the term “readily determinable” because there already is guidance in Topic 842 using that term and using that term for lessee-paid costs would appear to address the operability challenges raised by lessor stakeholders. Finally, the Board cautioned that an entity should apply reasonable judgment in determining whether the proposed amendments discussed in paragraph BC17 could be applied to its facts and circumstances.

As noted in the **Operational Challenges** discussion above, STORE, a triple-net lease REIT lessor, does not currently have an established method or reasonable ability to access property tax information as it is directly billed to and paid by our tenants. While property taxes may ultimately be *determinable* if we were able to obtain all the relevant information (i.e., assessments, billing and payments) from the numerous jurisdictions, we considered whether property taxes are *readily determinable*. We considered that *readily* can be defined as “without much difficulty or easily”. We assert that the factors described in the **Operational Challenges** discussion above demonstrate that the information cannot be obtained “without much difficulty” or “easily”. The relatively small dollar value of the investments we make and the large number of properties we hold in a highly granular portfolio serve to compound these operational challenges.

Further, we believe that there would be an expectation for lessors to evaluate the *readily determinable* criteria on a **lease by lease, property by property** and **jurisdiction by jurisdiction** basis. This evaluation would be burdensome and subject to the same factors described in the **Operational Challenges** discussion above.

We have concluded, based on our fact pattern, that the amounts are NOT *readily determinable* by STORE, the lessor. Additionally, as noted above, obtaining this information independently from each of the jurisdictions would be difficult, time-consuming and costly with no benefits to the business or users of the Company's financial statements.

Despite our conclusion, STORE also believes that the concept *readily determinable* is subject to interpretation and could cause diverse application in practice based on various points of view. Through recent discussions with several preparers in multiple industries and different audit firms, STORE has concluded that *readily determinable* is, in fact, being interpreted differently based on individual perspectives. These varied interpretations will result in preparers having protracted discussions with their auditors in an attempt to reach consensus on the "correct" application of *readily determinable* in order to implement Topic 842.

Our recommendation to permit an election by the lessor to report lessee-paid costs on a net basis would avoid practice issues around the interpretation of *readily determinable*, as well as added costs in this area, with no loss of useful information to financial statement users.

Transition for Lessor Costs Paid Directly by Lessees

The exposure draft asks whether the guidance in proposed paragraph 842-10-15-40A should be applied to new lease contracts only or to all existing and new lease contracts. We believe the Board should explicitly provide transition guidance that allows a lessor to make an election as to which approach they select. While application to new lease contracts only would likely result in an easier implementation, reporting such costs on a gross basis for only a subset of total lease contracts on an ongoing basis may prove to be difficult and make the information even less beneficial and more confusing to financial statement users. Ultimately, we believe an election available to lessors would allow each lessor to make the best determination.

However, we believe our recommendation to permit an election by the lessor to report lessee-paid costs on a net basis would alleviate any concerns around transition.

* * * * *

Thank you for the opportunity to comment on the exposure draft. If you have any questions regarding our comments, please contact Stacy LaFrance or Catherine Long at (480) 256-1100.

Very truly yours,



Stacy LaFrance
Senior Vice President and Chief Accounting Officer
STORE Capital Corporation



Catherine Long
Executive Vice President and Chief Financial Officer
STORE Capital Corporation