



December 4, 2020

Ms. Hillary Salo
Technical Director
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

RE: File Reference No. 2020-700

Dear Ms. Salo:

PricewaterhouseCoopers LLP appreciates the opportunity to comment on the FASB's Proposed Accounting Standards Update, *Leases (Topic 842): Targeted Improvements*.

We generally agree with the proposed amendments to Topic 842. With respect to Issue 3: *Modifications Reducing the Scope of a Lease Contract*, we agree with the FASB's conclusion that certain partial terminations within a master lease should not affect the remaining lease components. We recommend that the Board consider expanding the criteria under which the accounting for the remaining lease components should remain unchanged. Specifically, as described in our response to Question 12, we recommend the Board consider a model that is tied to the economics underlying a negotiated modification, rather than to the relative size of the change in lease payments.

The appendix contains our detailed responses to the Questions for Respondents as well as additional suggestions.

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If you have any questions regarding our comments, please contact Heather Horn (heather.horn@pwc.com), Thomas Barbieri (thomas.barbieri@pwc.com) or John Bishop (john.bishop@pwc.com).

Sincerely,

A handwritten signature in black ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive, slightly slanted style.

PricewaterhouseCoopers LLP



Appendix

Issue 1: Sales-Type Leases with Variable Lease Payments—Lessor Only

Question 1 - Are the amendments in this proposed Update operable? Why or why not?

While we believe the amendments in the proposed Update are operable, this question may best be addressed by the preparer community.

Question 2 - Should a lessor be required to classify and account for a sales-type lease with predominantly variable lease payments that do not depend on a reference index or a rate as an operating lease? Why or why not?

Yes. We agree that a lessor should not initially record a loss on an otherwise profitable transaction, as would often result in a sales-type lease with predominantly variable payments that do not depend on a reference index or a rate. Such transactions are typically inherently profitable, and operating lease accounting would reflect the underlying economics of the transaction better than recognizing an initial loss followed by profits over the lease term.

Question 3 - Should “predominant” be the threshold for determining when a lessor should classify a lease with variable payments that do not depend on a reference index or a rate as an operating lease? Alternatively, would another threshold be more appropriate and operable (for example, “substantially all”)? Please provide your rationale.

Yes, we agree that “predominant” should be the threshold to determine when a lessor should classify a lease with variable payments that do not depend on a reference index or a rate as an operating lease. We believe this threshold would capture most of the applicable transactions. Additionally, we believe that “predominant” would typically be qualitatively determinable and thus should be operable.

Question 4 - Would the proposed amendments provide improved decision-useful information for users of financial statements? Why or why not?

We believe the financial reporting that would result from the proposed amendments would better represent the underlying economics of the affected transactions. As such, the proposed amendments should provide improved decision-useful information for users of financial statements.

Issue 2: Option to Remeasure Lease Liability—Lessee Only

Question 5 - Are the proposed amendments operable? Why or why not?

While we believe the amendments in the proposed Update are operable, we believe this question is best addressed by the preparer community.



Question 6 - Should a lessee be provided with an option to remeasure lease liabilities solely for a change in a reference index or a rate on which payments are based? Why or why not?

Yes, we agree that a lessee should be provided with an option to remeasure lease liabilities for a change in a reference index or a rate on which payments are based. We agree with the Board's rationale that providing lessees with the option to remeasure lease liabilities for changes in a reference index or a rate would reduce ongoing costs and complexity for those preparers that report under both US GAAP and IFRS Standards.

Question 7 - Should a lessee be required to make an entity-wide accounting policy election to remeasure lease liabilities solely for a change in a reference index or a rate on which payments are based? Why or why not? If not, at what level should that accounting policy election be required to be applied?

We agree that an entity-wide election should be required. We believe that entity-wide application would provide improved decision-useful information for users of financial statements.

Question 8 - Would the proposed amendments provide improved decision-useful information for users of financial statements? Why or why not?

We believe that remeasuring the lease liability for a change in a reference index or a rate on which payments are based provides the most up-to-date information about a lessee's future cash obligations. As such, we believe it will improve decision-useful information for users of financial statements.

Question 9 - Would the comparability of information be significantly affected by the option to remeasure lease liabilities solely for a change in a reference index or a rate on which payments are based?

We believe this question is best answered by financial statement users. However, the proposed requirement to disclose the lessee accounting policy election to remeasure may mitigate concerns about comparability.

Other suggested edit:

We support the proposed addition of paragraph 842-10-55-231A in Example 25 that illustrates lessee accounting for a change in payments when a lessee elects to remeasure its lease liabilities to reflect changes to variable lease payments resulting from a change in an index or a rate. However, we are concerned that, as drafted, readers may misapply the intended guidance, and inappropriately record the payment as rent expense rather than as a reduction to the lease liability. We believe that the proposed paragraph should be edited to clarify that the lease liability should be remeasured once, at the beginning of Year 2, *before* the Lessee records the Year 2 lease payment, with a corresponding adjustment to the right-of-use asset. The lessee should then record the \$102,400 lease payment as a reduction of the liability.



Issue 3: Modifications Reducing the Scope of a Lease Contract

Question 10 - Are the proposed amendments operable? Why or why not?

We believe this question is best addressed by the preparer community. However, we support the Board's consideration of possible changes to the leases guidance to better reflect the underlying economics of certain lease modifications.

Question 11 - Would the proposed amendments provide improved decision-useful information for users of financial statements? Why or why not?

We believe this question is best answered by financial statement users. However, we believe the proposed amendments would maintain the decision usefulness of information provided to financial statement users.

Question 12 - Are there other aspects of the modification accounting model in Topic 842 that could be improved without compromising the decision usefulness of the information provided?

We believe the Board's proposed amendments are a good start in simplifying the guidance related to partial terminations of an arrangement with multiple lease components. However, we are concerned that the proposed amendment may have limited applicability, and, even in cases in which the proposed amendments would apply, it would not apply consistently to similar modifications or transactions.

We note that the proposed amendment would not apply to common changes in lease payments due to casualties or force majeure events that are often incorporated into the original terms and conditions of the lease, and would not require the lease to be modified.

When a lessee wishes to negotiate a modification outside of the terms incorporated into the original lease to partially terminate a master lease, we have observed that lessors typically demand reimbursement for resultant losses, including, for example, lost rents; unreimbursed occupancy costs; and exposure to market volatility. As such, the resulting negotiated lease payments may not be "substantially the same" as the original lease payments, and, as such, not qualify for the intended relief.

In addition, whether changes in lease payments would be "substantially the same" as the original lease payments - and, thus, qualify for the proposed accounting - may result solely due to the relative size of the partial termination, rather than from a consistent application of a principle. For example, a partial termination of 10 out of 100 leased assets is more likely to result in a smaller *relative* change in rents compared to the total agreement than a termination of 10 out of 20 leased assets, even though the amount of and economic rationale for the change in rents is the same. Similarly, a lessor may accept a lower change in lease payments late in the lease term than it would early in the lease term. In either case, the economics driving the negotiated changes are the same, yet some of those changes will qualify for the proposed amendment while others would not.

As a result of these concerns, we suggest that the Board further explore the modification accounting model in Topic 842 by considering additional relief to entities upon the early termination of one or more lease components in a lease contract if certain criteria are met. For example, the Board could consider a model in which accounting for the remaining lease components remains unchanged when the change in total lease payments is to reimburse the lessor solely for its losses from the partial termination. We



believe this approach would better reflect the economics underlying the negotiated modification, and be unaffected by the relative size of the change in lease payments.

Other suggested edits:

We support the amendments in the proposed Update intended to exempt entities from applying modification accounting to the remaining lease components within a lease contract for transactions in which one or more lease components are terminated before the end of the lease term when early termination does not economically affect the remaining lease components. However, we have concerns with the proposed amendments, including the following:

- a. We believe additional clarification should be made to paragraph 842-10-55-177 under Example 18. The proposed amendment to this paragraph is contrary to the intent stated in BC29. BC29 states, in part, “The Board decided that not separating lease components at the commencement date should not preclude an entity from subsequently applying the amendments in this proposed Update if it is apparent at the termination date that more than one separate lease components existed at lease commencement and the remaining lease components are economically unaffected by the termination.” We agree that the commencement date determination of whether the lease includes more than one lease component should not govern whether the proposed guidance should apply.

The change proposed to Example 18 may suggest that the subsequent accounting is, in fact, conditioned on the lessee’s determination of lease components at lease commencement. We believe that such interpretation would be inconsistent with BC29 and would result in accounting for a partial termination of a lease that is a single component that differs from the accounting for a partial termination of a lease of multiple components.

We believe that Example 18 should include the rationale as to why the modification is not eligible for the exemption from modification accounting for the remaining lease components in order to assist in its application. We believe that the Example could be amended to clarify that the change in lease payments, as described in paragraph 842-10-55-178, is not commensurate with the reduction in the leased space, and thus, the lease payments may not be “substantially the same” - as required by the amendment in paragraph 842-10-25-8B(c) in order to apply the proposed guidance.

- b. We believe that, as worded, it may be difficult for preparers to understand whether the proposed paragraph 842-10-25-8B(b)(1) articulates a broad principle or a narrow set of rules. We believe that the guidance in paragraph 842-10-25-B(b) should express the principle articulated in the last sentence of the paragraph: “...the early termination of one or more separate lease components does not affect the remaining lease component(s) when the termination of the lease component(s) does not result in a change to the **lease term** for the remaining lease components(s) as described in paragraphs 842-10-30-1 through 30-4, 842-10-35-1 through 35-3, and 842-10-55-23.” Subparagraphs (1) and (2) of paragraph 842-10-25-8B appear to describe examples of the overarching lease term evaluation; specifically, they address the evaluation of noncancellable leases (in paragraph 842-10-55-23) and lessee options, respectively. If the Board agrees with our understanding, then we suggest it reorganize the paragraph as described above, and then either indicate that the guidance in paragraph 842-10-25-8B(1) and 25-8B(2) are examples of the principle, or delete them altogether as unnecessary.



Transition

Question 13 - For entities that have not adopted Topic 842 by the effective date of a final Update of these proposed amendments, should the proposed amendments be applied at the date that an entity first applies Topic 842 using the same transition methodology in accordance with paragraph 842-10-65-1(c)? Why or why not?

Yes, we agree that entities that have not yet adopted Topic 842 should apply the proposed amendments at the date that the entity first applies Topic 842 using the same transition methodology.

Question 14 - For entities that have adopted Topic 842 by the effective date of a final Update of these proposed amendments, should the proposed amendments be applied either retrospectively or prospectively as described in this proposed Update? Why or why not?

Yes, we agree that entities that have already adopted Topic 842 should have the flexibility to adopt the proposed amendments either retrospectively or prospectively, as described in the proposed Update.