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Sir David Tweedie
Chairman of the
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Berlin, 15 July 2009

Discussion Paper 'Leases – Preliminary Views'

Dear David,

We appreciate the opportunity to respond to the International Accounting Standards Board's Discussion Paper (DP) 'Leases – Preliminary Views' (DP/2009/1). We understand that the DP has been prepared as part of a joint project by the IASB and the US Financial Accounting Standards Board (FASB) and sets out the boards' preliminary views.

This letter represents the views of the German Accounting Standards Board (GASB).

Our detailed comments regarding the boards' proposals are set out in the appendix to this document. We would like to highlight a few issues as follows:

- We believe that fundamentally changing lease accounting should be done in a comprehensive manner by including lessor accounting issues at the same time as lessee accounting issues (in contrast to the approach followed by the boards to defer consideration of lessor accounting). We also consider that lessor accounting issues, as provided in chapter 10 of the DP, require much more analysis by the boards, and its outcome should be shared with the constituents before its merits can be determined.
- We generally support the 'right-of-use' (RoU) approach since it appears to be a conceptually consistent approach and preferable compared to the other approaches laid out in Appendix C of the DP. If the RoU approach will be introduced into lease accounting, the boards may need to consider introducing this approach to other similar accounting areas it may apply to (e.g. service agreements) in order to be conceptually consistent.

- However, we note that the introduction of the ‘right-of-use’ approach as proposed in the DP may cause significant practical measurement problems and / or provide structuring opportunities in conjunction with options and contingent rentals. We think that introducing the ‘right-of-use’ approach to lease accounting will make the distinction between leases and service arrangements more important than it currently is – this would be a dividing line difficult to deal with. Additionally, we have identified some practical issues in this context which we are concerned with.
- From a conceptual point of view we consider the separate recognition and measurement of each of the rights and obligations in a complex lease to be preferable, i.e. to implement a components approach. While the boards tentatively decided not to adopt a components approach to account for complex lease contracts, we request the boards to readdress this issue since it appears that the boards may have been concessive too easily on conceptually essential elements of accounting under IFRS largely due to practical reasons. Acknowledging the practical issues brought forward by the boards in case a components approach will be introduced, we propose in the appendix an approach of how to account for the separate components.
- Regarding the subsequent measurement of contingent rentals we recommend considering changes based on contingent rentals once they have been substantiated - in contrast to considering them when the estimations have changed.
- We have concerns that some cross-cutting issues are not being dealt with consistently, e.g. we have noted that some proposals made in the DP are not consistent with the general revenue recognition principles and specifically the accounting treatment for multi-element arrangements within IFRS.

For detailed comments we refer to the appendix to this comment letter.

If you want to discuss any aspects of this letter in more detail, please do not hesitate to contact me.

Yours sincerely,

Liesel Knorr
President

APPENDIX

Chapter 2: Scope of lease accounting standard

> **Question 1:**
>
> The boards tentatively decided to base the scope of the proposed new lease accounting standard on the scope of the existing lease accounting standards. Do you agree with this proposed approach?
>
> If you disagree with the proposed approach, please describe how you would define the scope of the proposed new standard.

We agree with the boards' preliminary view that the scope of the proposed new standard should be based on the scope of the existing lease accounting standards. We recommend using the scope as laid out in IAS 17 / IFRIC 4 / SIC 27 as the starting point for the new lease accounting standard since it is the wider one compared to the corresponding US GAAP standards. However, we also recommend reviewing and addressing possible problems and issues in the context of leases of intangible assets (e.g. we noted that the lease of a software licence for three years would be treated differently from a purchase of a three-year licence, although both transactions are identical from an economic perspective; we noted, for example, differences in treatment with respect to the treatment of initial direct costs and multi-element arrangements). In this context, we also consider franchise agreements to be an area of concern.

> **Question 2:**
>
> Should the proposed new standard exclude non-core asset leases or short-term leases? Please explain why.
>
> Please explain how you would define those leases to be excluded from the scope of the proposed new standard.

The proposed new standard should neither exclude non-core asset leases nor short-term leases since we believe that the general materiality principle as included in the Framework will sufficiently address whether or not such leases will be subject to the new lease accounting standard.

In our understanding, such scope exclusions would lead to unnecessary complexity since non-core assets and short-term lease contracts would need to be defined and further guidance would be necessary. Another issue in this context would be that scoping out short-term leases inevitably would encourage structuring of leases in a way that the term of a lease contract would just be less than the specified threshold.

Chapter 3: Approach to lessee accounting

Question 3:

Do you agree with the boards' analysis of the rights and obligations, and assets and liabilities arising in a simple lease contract?

If you disagree, please explain why.

We agree with the boards' analysis of the rights and obligations and the assets and liabilities arising in a simple lease contract. However, it appears to be questionable whether the analysis is truly helpful for the generally more complex contracts and those which deal with intangible assets (e.g. in the case of lease contracts for licences there would be no obligation to return any physical item at the end of the lease term to the lessor).

Question 4:

The boards tentatively decided to adopt an approach to lessee accounting that would require the lessee to recognise:

(a) an asset representing its right to use the leased item for the lease term (the right-of-use asset)
(b) a liability for its obligation to pay rentals.

Appendix C describes some possible accounting approaches that were rejected by the boards.

Do you support the proposed approach? If you support an alternative approach, please describe the approach and explain why you support it.

In general we favour the 'right-of-use' approach for conceptual reasons and consider that it will be an improvement compared to the current situation for simple leases.

However, we note that the introduction of the 'right-of-use' approach as proposed in the DP may cause significant practical measurement problems and / or provide structuring opportunities in conjunction with options and contingent rentals (i.e. more complex leases). We think that introducing the 'right-of-use' approach to lease accounting will make the distinction between leases and service arrangements more important than it currently is. Therefore, it would be unfortunate if the outcome of the DP - simply speaking - would be the replacement of one difficult border (operating vs. finance leases) with another border (leases vs. service arrangements).

There are some further concerns with regard to practical issues as follows:

- The way the 'right-of-use' approach currently is designed by the boards appears to be conceptually problematic considering the proposed accounting for leases including options (please refer to our comments with respect to the questions on chapter 6 and question 5 below). In this respect we recommend the boards to implement a components approach.

- Further, the disadvantages of the existing accounting model (mainly not recognising the assets and liabilities arising from a lease contract in the financial statements of lessees) may be addressed by the proposed 'right-of-use' approach, but the advantages of such an achievement would be reduced or even offset by the challenging measurement and reassessment issues caused by leases with options, contingent rentals and residual value guarantees.

In any case, if the boards decide to implement the 'right-of-use' approach to lease accounting, we recommend the boards to implement this approach for consistency reasons where appropriate to other similar accounting issues. Namely, the 'right-of-use' approach should also be considered for service contracts to the extent the rights and obligations that arise in such contracts give rise to assets and liabilities that can be recognised in the financial statements.

Question 5:

The boards tentatively decided not to adopt a components approach to lease contracts. Instead, the boards tentatively decided to adopt an approach whereby the lessee recognises:

(a) a single right-of-use asset that includes rights acquired under options
(b) a single obligation to pay rentals that includes obligations arising under contingent rental arrangements and residual value guarantees.

Do you support this proposed approach? If not, why?

From a conceptual point of view we consider the separate recognition and measurement of each of the rights and obligations in a complex lease to be preferable, i.e. to implement a components approach. The boards tentatively decided not to adopt a components approach to lease contracts – the arguments are laid down in DP 3.32. However, we request the boards to readdress this issue since it appears that the boards may have been concessive too easily on conceptually essential elements of accounting under IFRS largely due to practical reasons.

We consider the tentative decision not to adopt a components approach to cause conceptual problems and inconsistencies because in other areas of IFRS accounting a components approach is generally adopted (especially for multi-element arrangements). We believe that the adoption of the approach tentatively preferred by the boards could lead to obligations to pay rentals that do not meet the definition of a liability (because the lessee does not have a present obligation). We consider the separate recognition and measurement of options and other arrangements to be critical for providing users of financial statements with decision-useful information.

Acknowledging though that there are significant practical concerns about such a components approach specifically with regard to measurement issues, we propose the following three-step approach:

1) if the fair value of the elements (e.g. options or residual value guarantees) can be measured reliably, they need to be accounted for as separate components of the lease contract,

2) if the fair value of the elements cannot be measured reliably, alternative measurements shall be required (e.g. term options may be measured based on their intrinsic value),

3) if neither of the measurement bases can be determined reliably, the boards may consider providing alternative approaches (e.g.: to provide detailed information in the notes to the financial statements with respect to existing options or residual value guarantees).

Chapter 4: Initial measurement

Question 6:

Do you agree with the boards' tentative decision to measure the lessee's obligation to pay rentals at the present value of the lease payments discounted using the lessee's incremental borrowing rate?

If you disagree, please explain why and describe how you would initially measure the lessee's obligation to pay rentals.

We disagree with the boards' tentative decision since we believe that the interest rate implicit in the lease and charged by the lessor is specific to the liability being measured and should therefore be the basis of its initial measurement. Regarding the practical concerns mentioned by the boards (in many instances the lessee will not know or be able to determine the implicit rate) we do not consider them strong enough to give up on the interest rate implicit in the lease as the primary basis to discount the relevant cash flows. Therefore, we recommend keeping the rule as it is currently stated in IAS 17.20 in case it will be impracticable for a lessee to determine the interest rate implicit in the lease - as a fallback position - the lessee's incremental borrowing rate shall be used.

Question 7:

Do you agree with the boards' tentative decision to initially measure the lessee's right-of-use asset at cost?

If you disagree, please explain why and describe how you would initially measure the lessee's right-of-use asset.

We agree with this tentative decision.

Chapter 5: Subsequent measurement

Question 8:

The boards tentatively decided to adopt an amortised cost-based approach to subsequent measurement of both the obligation to pay rentals and the right-of-use asset.

Do you agree with this proposed approach?

If you disagree with the boards' proposed approach, please describe the approach to subsequent measurement you would favour and why.

We agree with the tentative decision of the boards. However, for investment properties as defined in IAS 40 we propose that an entity shall be able to choose as its accounting policy either the fair value model or the cost model.

Question 9:

Should a new lease accounting standard permit a lessee to elect to measure its obligation to pay rentals at fair value?

Please explain your reasons.

A new lease accounting standard should not permit a lessee to elect to measure its obligation to pay rentals at fair value mainly because this would be inconsistent with the boards' tentative decision to require measurement at cost on initial recognition. We also consider it preferable not to provide alternative measurements in accounting standards.

Question 10:

Should the lessee be required to revise its obligation to pay rentals to reflect changes in its incremental borrowing rate? Please explain your reasons.

If the boards decide to require the obligation to pay rentals to be revised for changes in the incremental borrowing rate, should revision be made at each reporting date or only when there is a change in the estimated cash flows? Please explain your reasons.

The lessee should not be required to revise its obligation to pay rentals to reflect changes in its incremental borrowing rate because it is inconsistent with the way many non-derivative financial liabilities are subsequently measured (under the amortised cost-based approach, the carrying amount of financial liabilities is not revised for changes in market interest rates). It would also be inconsistent with an amortised cost-based approach to subsequent measurement since it would factually end up in a fair value measurement. This is because any changes in the lessee's credit spread would result in revisions of the obligation to pay rentals; changes in the own credit risk of a lessee should not be reflected in subsequent measurement of the obligation to pay rentals.

Question 11:

In developing their preliminary views the boards decided to specify the required accounting for the obligation to pay rentals. An alternative approach would have been for the boards to require lessees to account for the obligation to pay rentals in accordance with existing guidance for financial liabilities.

Do you agree with the proposed approach taken by the boards?

If you disagree, please explain why.

We agree with the proposed approach to specify the accounting of the obligation to pay rentals. Since there is different existing guidance for financial liabilities under US GAAP and IFRS, the alternative approach would cause additional problems.

Nevertheless, we would like to point out that the boards are inconsistent in their argumentation on different subjects. On the one hand, the lessees based on the preliminary view of the boards are not going to be required to account for the obligation to pay rentals in accordance with existing guidance for financial liabilities since this approach "would result in the obligation to pay rentals being accounted for in the same way under US GAAP and IFRSs even before the two boards' financial instruments standards converge" (DP 5.36). The very same argument, on the other hand, has been disregarded by the boards during their June 2009 meetings with respect to the determination of how a 'right-of-use' asset shall be reviewed for impairment. Both boards preliminary decided to require entities to refer to existing applicable standards (IAS 36 for IFRS preparers, SFAS 144 for US GAAP preparers).

Question 12:

Some board members think that for some leases the decrease in value of the right-of-use asset should be described as rental expense rather than amortization or depreciation in the income statement.

Would you support this approach?

If so, for which leases? Please explain your reasons.

Although this chapter deals with 'subsequent measurement', we consider the question raised to be a presentation issue.

However, to be consistent with the chosen 'right-of-use' approach, we consider it necessary to describe the decrease in value of the 'right-of-use' asset as depreciation.

Chapter 6: Leases with options

Question 13:

The boards tentatively decided that the lessee should recognise an obligation to pay rentals for a specified lease term, i.e. in a 10-year lease with an option to extend for five years, the lessee must decide whether its liability is an obligation to pay 10 or 15 years of rentals. The boards tentatively decided that the lease term should be the most likely lease term.

Do you support the proposed approach?

If you disagree with the proposed approach, please describe what alternative approach you would support and why.

We have concerns about the approach tentatively proposed by the boards. As laid down in our answer to Question 5, from a conceptual point of view we consider the separate recognition and measurement of each of the rights (and obligations) in a complex lease to be preferable (i.e. to implement a components approach). In our understanding this approach better reflects the economic substance of a non-financial option and makes its value visible to the users of financial statements.

We understand that the boards considered the practicability of measuring these options and decided tentatively in favour of the so-called ‘looking-through-the-option approach’ (for the reasons please refer to DP 3.32: difficulties to apply in practice; components are often interrelated; possibility to structure leases; fair value of options is difficult to measure; may not provide users with complete information about the economic position of the lease). We do not consider these (practical) reasons to be strong enough to outweigh the conceptual concerns mentioned above. Further, the approach as tentatively suggested by the boards would lead to the recognition of a liability although there is no ‘present obligation’ based on a ‘past event’, so that the liability would not be in line with current IFRS-principles. Only in rare circumstances we would agree to this approach: if the lessee was economically compelled to exercise the option - since factually there is no other economic alternative for the lessee.

We realise that because of our requirement to account for options as separate components of the lease contract, the lessee will be required to measure (at least at initial recognition) options to extend or terminate the lease. We acknowledge that options of this type are difficult to measure reliably as they are rarely priced separately from the main lease contract. Therefore we propose the following three-step approach:

1) if the fair value of the options can be measured reliably, they need to be accounted for as separate components of the lease contract,

2) if the fair value cannot be determined reliably, the options shall be measured based on their intrinsic value and be accounted for as separate components of the lease contract,

3) if neither the fair value nor the intrinsic value of the options can be measured reliably, the boards may consider to provide alternative approaches (e.g.: to provide detailed information in the notes to the financial statements with respect to existing options).

In this context we would like to propose a clarification to be included in the new lease standard that the accounting for options as a separate component as proposed by us needs to be applied only to options which are options in their substance and economic reality (and not merely because of their legal form).

Regarding the approach as suggested by the boards, we further have some concerns about the factors to be considered in determining the lease term (please refer to para. 6.38 – 6.41 of the DP: contractual; non-contractual financial; business; lessee specific). According to the boards' views the lessee's intention and past practice (= lessee specific factors) shall not be included – as we do not consider this proposal to be practicable since there is no clear dividing line between the factors which should be considered and those which should not.

Moreover, we also would like to bring forward the following concern: in case a lease contract with a term option is
a) either prolonged as the lessee exercises the option,
b) or the option will not be exercised and the original lease contract is considered to be ceased but a new, subsequent lease contract is entered into with identical features as agreed for the optional lease term,

the accounting treatment would be different for the two scenarios although in both instances the economic substance is the same. The boards should either explain why it is appropriate to have different accounting methods for these substantively identical transactions or make sure that the accounting is consistent for both transactions.

The following questions 14 and 15 on this chapter 'Leases with options' are based on the assumption that the respondent agrees with the basic approach as proposed by the boards (i.e. including the adoption of a non-components approach and looking at the 'most likely' outcome when options are involved). Since we have some concerns to this proposal, we respond to the remaining questions based on the view favoured by us. Therefore, please read our responses to questions 14 and 15 in that context.

Question 14:

The boards tentatively decided to require reassessment of the lease term at each reporting date on the basis of any new facts or circumstances. Changes in the obligation to pay rentals arising from a reassessment of the lease term should be recognised as an adjustment to the carrying amount of the right-of-use asset.

Do you support the proposed approach?

If you disagree with the proposed approach, please describe what alternative approach you would support and why.

Would requiring reassessment of the lease term provide users of financial statements with more relevant information? Please explain why.

We do not support the underlying approach as proposed by the boards (please refer to our response to question 13).

Based on the approach as favoured by us (see comments as laid out answering question 13 – i.e. we propose the components approach), we would suggest a reassessment of the measurement of the option accounted for as a separate component of the lease contract as detailed below. According to the three-step approach suggested by us the subsequent measurement could be structured as follows:

1) if the option is measured initially at its fair value, the subsequent measurement shall be based on the fair value;

2) if the fair value cannot be determined reliably for the initial measurement or the subsequent measurement of an option, it shall be remeasured when indications exist that the measurement has changed; the measurement shall be based on the intrinsic value of the option;

3) if neither the fair value nor the intrinsic value of the options can be measured reliably, the boards may consider providing alternative approaches (e.g.: providing detailed information in the notes to the financial statements with respect to existing options).

On the other hand, for subsequent measurement of term options the boards may consider a similar approach as determined in IFRS 2 for equity-settled share-based payment transactions (IFRS 2.23: ‘... the entity shall make no subsequent adjustment ...’).

In this context, it is considered preferable that the boards provide the approach how to account for changes in the subsequent measurement of the options (e.g.: recognition of measurement changes through profit or loss or directly in equity).

Question 15:

The boards tentatively concluded that purchase options should be accounted for in the same way as options to extend or terminate the lease.

Do you agree with the proposed approach?

If you disagree with the proposed approach, please describe what alternative approach you would support and why.

We do not agree with the proposed approach. We prefer to apply a components approach (basic lease contract separated from term options and purchase options) and to measure all components separately. In this context, purchase options should be accounted for in the same way as term options.

However, additional guidance needs to be provided by the boards with regard to the question of how to account once the purchase option has been exercised.

Chapter 7: Contingent rentals and residual value guarantees

Contingent rentals

Question 16:

The boards propose that the lessee's obligation to pay rentals should include amounts payable under contingent rental arrangements.

Do you support the proposed approach?

If you disagree with the proposed approach, what alternative approach would you recommend and why?

We support the proposed approach because otherwise
- the assets of the lessee would be understated,
- it would be possible, at the start of the lease, to minimise both the 'right-of-use' asset and the obligation to pay rentals by including a significant portion of contingent rentals in the lease contract.

Further, the proposed approach could improve comparability for users because it is consistent with the treatment of other asset acquisitions.

With reference to the ED of proposed amendments to IAS 37 we consider the contingent rentals to be unconditional (or non-contingent) obligations which are not contingent or conditional on the occurrence or non-occurrence of a future event. The contingency relates to one or more uncertain events that affect the amount that will be required to settle the unconditional obligation.

Question 17:

The IASB tentatively decided that the measurement of the lessee’s obligation to pay rentals should include a probability-weighted estimate of contingent rentals payable. The FASB tentatively decided that a lessee should measure contingent rentals on the basis of the most likely rental payment. A lessee would determine the most likely amount by considering the range of possible outcomes. However, this measure would not necessarily equal the probability-weighted sum of the possible outcomes.

Which of these approaches to measuring the lessee’s obligation to pay rentals do you support? Please explain your reasons.

For practicability reasons we prefer to measure contingent rentals on the basis of the most likely rental payment. We are aware that this proposal would not be in line with the current development of ED of Proposed Amendments to *IAS 37 Provisions Contingent Liabilities and Contingent Assets and IAS 19 Employee Benefits*. However, since the obligation to pay rentals is considered to be a financial liability, we consider this proposal to be acceptable.

Question 18:

The FASB tentatively decided that if lease rentals are contingent on changes in an index or rate, such as the consumer price index or the prime interest rate, the lessee should measure the obligation to pay rentals using the index or rate existing at the inception of the lease.

Do you support the proposed approach? Please explain your reasons.

We do not support the approach as suggested by the FASB since we consider the contingency in lease rentals subject to changes in an index or a rate to be the change in the index or the price. This contingency shall be reflected in the lessee’s obligation to pay rentals measuring the obligation initially since otherwise the obligation would be measured unrealistically and not be reflecting the economic substance of the obligation ignoring expected future market conditions. Specifically, we suggest basing the measurement of such contingent rentals on expected future trend information (e.g. forward curves), which we consider to be a better basis than to purely base the measurement of the obligation on the index or rate existing at the inception of the lease.

Since we acknowledge the practical issues with this approach, we would consider it appropriate if the new lease standard would - as a fall-back position - allow the lessee to measure the obligation to pay rentals using the index or rate existing at the inception of the lease. Once changes in the index or the rate have been substantiated, they shall be considered in measuring the obligation to pay rentals.

Question 19:

The boards tentatively decided to require remeasurement of the lessee's obligation to pay rentals for changes in estimated contingent rental payments.

Do you support the proposed approach? If not, please explain why.

We support the boards' tentative view to require remeasurement. However, a mere change in estimate about a future contingency shall not give rise to remeasurement. A remeasurement should be required and considered only in case the lessee's obligation to pay rentals is subject to a substantiated change.

Question 20:

The boards discussed two possible approaches to recognising all changes in the lessee's obligation to pay rentals arising from changes in estimated contingent rental payments:

(a) recognise any change in the liability in profit or loss
(b) recognise any change in the liability as an adjustment to the carrying amount of the right-of-use asset.

Which of these two approaches do you support? Please explain your reasons.

If you support neither approach, please describe any alternative approach you would prefer and why.

We consider it to be theoretically correct to distinguish between the changes affecting the value of the 'right-of-use' asset and those that do not, and to account for the former by adjusting the carrying amount of the asset and for the latter by debiting or crediting profit or loss. On that basis we ask the boards to provide clear guidance on these different accounting treatments.

However, if such an approach introduced too much complexity and practical problems, we would accept a pragmatic approach that treats all changes in the estimated rental obligation in the same way. In such case we would prefer treating all changes in contingent rental payments as an adjustment to the carrying amount of the 'right-of-use' asset. In this context it should be noted that any possible overstatement of the 'right-of-use' asset, which may be caused by such an approach, would be subject to the impairment rules, which the boards consider necessary as indicated in the DP (chapter 5 paragraph 44).

Residual value guarantees

Question 21:

The boards tentatively decided that the recognition and measurement requirements for contingent rentals and residual value guarantees should be the same. In particular, the boards tentatively decided not to require residual value guarantees to be separated from the lease contract and accounted for as derivatives.

Do you agree with the proposed approach?

If not, what alternative approach would you recommend and why?

We do not agree with the proposed approach. In accordance with our previous answers in which we propose the implementation of a components approach, we consider the residual value guarantee to be an obligation that should be accounted for as a separate component of the lease contract.

We realise that because of our proposal to account for the residual value guarantee as a separate component of the lease contract, the lessee will be required to recognise and measure the residual value guarantee. We acknowledge that residual value guarantees are difficult to measure reliably as they are rarely priced separate from the main lease contract. However, by comparing current market prices of the leased items and projecting these prices to the end of the lease term, and comparing these values with the price guaranteed to the lessor, a measurement may generally be possible. Although we are aware of the inherent practical challenges (e.g. difficulties to estimate future market prices; huge numbers of lease contracts; subjectivity and judgement issues involved), we propose the following two-step approach (as done similarly to account for term and purchase options, for which we proposed a three-step approach):

1) if residual value guarantees can be measured reliably, they need to be accounted for as separate components of the lease contract and a provision in accordance with IAS 37 based on the fulfilment value (the expected cash outflows) should be recognised (in contrast to accounting for them in line with IAS 39 as derivatives),

2) if they cannot be measured reliably, it would be preferable, if the boards could provide alternative approaches (e.g. to provide detailed information in the notes to the financial statements with respect to existing residual value guarantees).

Chapter 8: Presentation

Question 22: Should the lessee's obligation to pay rentals be presented separately in the statement of financial position? Please explain your reasons. What additional information would separate presentation provide?

The separate presentation of the lessee's obligation to pay rentals and other components of the lease contract such as residual value guarantees should be optional to the lessee since this would allow to choose the presentation which best supports an understanding of the lessee's financial position.

However, if the lessee opts not to present the obligation to pay rentals or other components of the lease contract separately in the statement of financial position, detailed information (including the components of a lease contract accounted for separately, as recommended by us) should be provided in the notes to the financial statements.

Question 23: This chapter describes three approaches to presentation of the right-of-use asset in the statement of financial position. How should the right-of-use asset be presented in the statement of financial position? Please explain your reasons. What additional disclosures (if any) do you think are necessary under each of the approaches?

We prefer to present the 'right-of-use' asset based on the nature of the underlying assets (including the components of a lease contract accounted for separately, as recommended by us) with further details to be provided in the notes to the financial statements.

We support this view mainly because users of financial statements are provided with information about the nature of the leased asset that could be lost if the 'right-of-use' asset is presented as an intangible asset. We understand that users are predominantly interested in the productive capacity of a business to assess the ability of the business to generate positive cash flows.

Further, we recommend that the depreciation expense stemming from the 'right-of-use" assets shall also be presented separately from depreciation expense stemming from assets owned by the lessee (in order to portray a cohesive financial picture of the lessee's activities).

Chapter 9: Other lessee issues

Question 24:

Are there any lessee issues not described in this discussion paper that should be addressed in this project?

Please describe those issues.

We have identified the following issues that are not described or addressed in this DP but should be addressed in this project:

- whether the boards have ensured to consider all major types of options and rental agreements in the course of initial measurement for the asset and the obligation to pay rentals (e.g.: obligations to incur costs to return the leased item (in a specified condition) to the lessor, obligations to maintain the leased item);
- clear guidance for 'first-time adoption' and 'transition' issues; we understand that the boards discussed these issues in their May and June 2009 meetings and intend to continue with these discussions;
- with respect to chapter 6 (leases with options) – bullet point 2: regarding recognition - term options: further guidance for long-term leases with options to exit the lease contract on an ongoing basis (e.g. 20-year lease of an office-building with option to cancel the lease on a semi-annual basis);
- guidance for the accounting treatment of lease modifications;
- guidance with respect to the differentiation of rental payment and asset retirement obligations; and
- the accounting treatment for the effect of lessee involvement in asset construction ('built-to-suit transactions'; please refer to the US GAAP pronouncement EITF 97-10).

Chapter 10: Lessor Accounting

Question 25:

Do you think that a lessor's right to receive rentals under a lease meets the definition of an asset?

Please explain your reasons.

We consider the lessor's right to receive rentals under a lease to meet the definition of an asset to the extent of so-called minimum leases.

Further guidance should be provided for the accounting of leases with options from a lessor's point of view.

Question 26:

This chapter describes two possible approaches to lessor accounting under a right-of-use model:

(a) derecognition of the leased item by the lessor or
(b) recognition of a performance obligation by the lessor.

Which of these two approaches do you support? Please explain your reasons.

We consider that lessor accounting issues require much more analysis by the boards, and its outcome should be shared with the constituents before its merits can be determined.

We suggest that the boards' analysis of lessor accounting issues shall include and may start with the two conceptually important issues as follows:

- shall lessee and lessor accounting for the 'right-of-use' approach be mirror-imaged (similar to the mirror-imaged accounting for operating and finance leases by lessees and lessors), and
- shall the lessor accounting fully be in line with the proposal made by the IASB in the Discussion Paper *Preliminary Views on Revenue Recognition in Contracts with Customers*.

Question 27:

Should the boards explore when it would be appropriate for a lessor to recognise income at the inception of the lease?

Please explain your reasons.

As stated in our answer to Question 26, more analysis should be provided by the boards and its outcome should be shared with the constituents before its merits can be determined.

Question 28:

Should accounting for investment properties be included within the scope of any proposed new standard on lessor accounting?

Please explain your reasons.

As stated in our answer to Question 26, more analysis should be provided by the boards and its outcome should be shared with the constituents before its merits can be determined.

Question 29: Are there any lessor accounting issues not described in this discussion paper that the boards should consider? Please describe those issues.

As stated in our answer to Question 26, more analysis should be provided by the boards and its outcome should be shared with the constituents before its merits can be determined.