November 23, 2011

Mr. Hans Hoogervorst, Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Ms. Leslie Seidman, Chairman
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856

Dear Sir and Madam,

I am writing on behalf of Financial Executives International (FEI) to provide the preparer perspective on the current direction of the Leasing project. Our members are intensely interested in all developments related to this project. We follow the Boards' deliberations very closely and study the implications of the Boards' conclusions on reporting entities. FEI believes that there are significant issues with the current version of the proposed Lessee model which we believe need to be addressed prior to issuing a revised Exposure Draft (ED). In our view, to issue a revised ED as is, without addressing these concerns, would be a significant missed opportunity to finalize and issue a high quality standard. The basis for FEI's concerns is provided below.

A high quality accounting standard is one that provides the users of financial statements with decision useful information. This is accomplished by providing both present and potential investors with financial information that facilitates predicting the amount and timing of net future cash flows. The Boards undertook this project in order to address concerns about leasing as a source of off-balance sheet financing. It is noteworthy that our members fully accept capitalization of leases as a necessary consequence of this project. However, this support has been misconstrued as implicit support for the Right of Use model with all of its inherent weaknesses. We wish to clarify that FEI disagrees with the consequential effects of the Right of Use model on the Statement of Earnings and the Statement of Cash Flows. Specifically, we believe that the Boards' current conclusions obfuscate, rather than clarify, the effect of leasing transactions on future cash flows. We believe that this will render the financial statements less useful to investors.

In order to achieve the capitalization objective under the Right of Use premise, the proposal separates the lease contract into asset and liability elements, while leaving open to debate the true nature of the asset (i.e., tangible or intangible). Further, notwithstanding that the resulting

asset and liability are integrally linked and inseparable, the Boards propose that amortization of the asset must follow existing conventions usually reserved for free-standing assets. This approach distorts the cost allocation pattern and causes the reported amounts to diverge from the pattern of future cash outflows related to the lease contract. The reported expense will either overstate or understate cash outflows, depending upon where in the lease term the contract is. As a result, investors will need to prepare a normalized projection of leasing expenses if they are attempting to value an entity based upon its accounting earnings. As this model causes the asset to amortize more quickly than the obligation, it also has the effect of misstating a lessee's net position in the lease contract. A lease entered into at market will always have zero value at lease commencement and will have minimal value over the term of the lease, absent changes in market conditions. The proposed presentation will, however, present all leases as if they were off market contracts in a net loss position after initial recognition until the lease term ends. In addition, by parsing and re-segmenting the economic components of the lease contract, treating some components as operating cash flows and others as financing, investors will have to make their own adjustments to get back to the financial statement presentation provided under current IFRSs or U.S. GAAP, which they expressly prefer.

We observe that the population of leasing transactions affected by this standard is bimodal: a relatively small number of large dollar transactions (e.g., real estate and large capital equipment) and a relatively large number of small dollar transactions (e.g., copiers, automobiles, etc.) with very little in between. Although we do not have robust statistics on the number of leases, we expect, for most companies, it is in the tens of thousands. For example, we know of two U.S. utility companies that have completed an inventory and determined that they each have in excess of 50,000 leases. Just one operating division of a major diversified manufacturer has determined that it has in excess of 60,000 lease assets. Many of these lease contracts cover items that are both non-core in nature and employed pervasively throughout the organization. This explains why it has been so challenging for companies to get a robust inventory of all of their leases. This level of activity should raise concerns for Board members about the complexity and cost of applying a completely different approach to expense allocation to this population of leased items. FEI has significant doubts as to whether application of the proposed standard to such items at an individual unit of account level (typically a single asset, such as a forklift) is cost beneficial.

We also observe that investors, generally speaking, are not accountants. To the extent that accounting diverges from the underlying economics, it impairs the relevance and utility of the financial statements to investors. From an investor's standpoint, it is difficult to make economic sense out of a change in the pattern of cost allocation for a contract that results solely because of capitalization of its components on the balance sheet.

FEI notes that there are alternative treatments available to the Boards that avoid these consequential effects and are more theoretically supportable, from both economic and technical perspectives. The annuity method of depreciation is one such alternative. That method recognizes that the economics of a lease are best reflected by the cash flow effects of the overall lease contract. Furthermore, the premise for the annuity method is that it best reflects a leased asset's economic benefits which are consumed by the entity over time. Specifically, considering the linked nature of the asset and liability, this method captures the expected change in value of those benefits over time (exclusive of market-related effects). This view is objectively supported by the fact that it resolves the distortion to the earnings' statement and the understatement of the net investment on the balance sheet that results from the Boards' Right of Use model.

From a conceptual standpoint, it also is more representationally faithful and consistent with prior IFRSs and U.S. GAAP for the accounting to reflect the fact that the asset and liability are not economically independent of each other after initial recognition. In the past, GAAP has required separation of a contract into elements when such elements could modify the cash flows of the host. For example, accounting for derivatives requires separation of a conversion feature in a convertible debt instrument when the conversion feature creates the possibility that the debt instrument may be settled either through the payment of cash or through the conversion into an equity instrument. Derivative accounting also provides guidance on when two or more contracts must be accounted for as a single unit of account. Combination is required when two or more transactions are entered into contemporaneously and in contemplation of one another, with the same counterparty and the underlying transactions relate to the same risk. The objective of this guidance is to ensure that each of the components considered individually do not provide a different overall financial reporting effect than what would result from the transactions when considered as a whole. There is no doubt that the latter approach is the only one that faithfully represents the economics of a lease contract.

We understand that the concerns expressed above have been raised consistently by both investor and preparer constituents during the Boards' outreach initiative. It is our view that the true measure of a high-quality due process is not the number of meetings held or comment letters read but rather whether the key issues are appropriately identified and resolved through a thoughtful and deliberate decision-making process. Said more plainly, a high-quality due process is learning as much as you can about issues with a proposed standard and making the best decisions you can to resolve them. That would suggest that it is imperative that the Boards find a means to address the cost pattern issue so that it may move forward with a proposed standard that is of high quality and capable of being implemented in a cost effective manner.

It is our sincere hope that the Boards will take the opportunity to reconsider its collective views on this issue prior to the next ED. Members of FEI would be pleased to assist the Boards in answering any questions related to this letter. Please feel free to contact Lorraine Malonza at (973) 765-1047 or me at (973) 765-1001, if you would like to arrange a meeting.

Sincerely,

Marie N. Hollein
President and Chief Executive Officer
Financial Executives International

Cc: James Kroeker, SEC Chief Accountant