



Japan Leasing Association

Fukoku Seimei Bldg., 2-2-2, Uchisaiwai-cho, Chiyoda-ku, Tokyo 100-0011
JAPAN Tel. +81(3)3595-1501 Fax. +81(3)3595-2230 [http://www.leasing.or.jp]

November 21th, 2012

Mr. Hans Hoogervorst
Chairman
International Accounting Standards Board

Dear Mr. Hoogervorst,

Japan Leasing Association (JLA) has ever commented on the lease project conducted by IASB and FASB. JLA submitted a comment letter on July 25th 2012 just after the boards made a tentative decision on the lease expense recognition patterns for lessees in June 2012. However, JLA would like to emphasize its view on the tentative decision again, because the tentative decision is inappropriate from the standpoint of concept and practicability. According to the tentative decision, a lessee and a lessor are required to distinguish between two different types of lease on the basis of whether the lessee acquires and consumes more than an insignificant portion of the underlying asset over the lease term, by using a practical expedient based on whether the underlying asset is property or not.

In the comment letter on July 25th 2012, JLA commented that the criterion in IAS 17 *Leases* should be adopted as an indicator to distinguish between two different types of lease. If the boards were to finalize the new lease accounting standard including the tentative decision, the new standard would not be an improvement over the current standard. Instead of the tentative decision, adding some improvements to the current standard would be more reasonable and understandable among constituents including users of financial statements, considering practicability and comparative analysis related to cost-benefit.

Finally, many constituents would be likely to comment on the re-exposure draft that will be published in the first quarter in 2013 as they did so when the exposure draft was published in August 2010. JLA would like the boards to carefully and thoroughly consider comment letters to be received again before IASB and FASB publish a final standard.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Tsutomu Abe', written over a horizontal line.

Tsutomu Abe
Chairman
Japan Leasing Association

Japan Leasing Association's Proposal on the Lease Accounting

Japan Leasing Association (JLA) has a deep respect for analyses and efforts International Accounting Standards Board (IASB) and Financial Accounting Standards Board (FASB) have ever made in order to improve the current lease accounting.

It has taken a lot of time for IASB and FASB (the boards) to re-deliberate the lease accounting since the publication of the Exposure Draft. This implies that applying a single accounting model for various leases makes economics of some leases inappropriately reflected on financial statements and it is difficult to solve this concern. As a result, the boards changed the fundamental concept of applying a single accounting approach for all leases.

JLA has ever made many proposals to the boards from the standpoint of both rationale and practicality. In the JLA's previous proposals, JLA was supportive of applying the right of use model to some leases that include non-cancelable term (including some leases currently classified as operating leases), and also required some practical expedients to the proposed accounting model from a practicability perspective. In addition, JLA was also supportive of the tentative decision in April 2011 that there were two types of lease (i.e. finance leases and other-than-finance leases) because that tentative decision was the most acceptable proposal by the boards.

However, In JLA's view, the latest tentative decision is inappropriate from the standpoint of concept and practicability. According to the decision, a lessee and a lessor should distinguish between two different types of lease on the basis of whether the lessee acquires and consumes more than an insignificant portion of the underlying asset over the lease term, by using a practical expedient based on whether the underlying asset is property or not. JLA would like to emphasize again what JLA has already insisted on in the comment letter "Japan Leasing Association (JLA)'s Proposal on the Tentative Decision on the Distinction between Different Types of Lease" dated as July 25th 2012.

<Concerns>

- a. There are various types of lease. The proposal made by the boards would not reflect the characteristics and nature of the main types of lease (i.e. finance leases and other than finance leases), and would not reflect differences between those leases.
- b. According to the proposed criterion for a lease of assets other than a property, a lessee would not be able to apply the single lease expense (SLE) approach to the majority of current operating leases of assets other than a property (where a lessor prices those leases in order to be able to generate return on the whole underlying asset such as an automobile or a measuring instrument by leasing out the

underlying asset to multiple lessees, which is similar to a lease of a property), because the lessee would be forced to determine that the lessee acquires and consumes more than an insignificant portion of the underlying asset over the lease term. If the underlying asset is leased out to several lessees, the remaining economic life of the underlying asset would be likely to be significantly covered by the lease term. In addition, the fair value of that underlying asset would be likely to be significantly covered by the present value of lease payments. Therefore, a lessee would be forced to apply the interest and amortization (I&A) approach to leases of assets other than a property.

There can be many operating leases of assets other than a property which are economically similar to a lease of a property. However, the boards have not yet clarified the reason why a lessee should apply to a lease of assets other than property an accounting approach different from the one applied to a lease of a property.

- c. The proposed criterion for a lease of a property is similar to the one in IAS 17 *Leases* to classify a lease into either a finance lease or operating lease, while the criterion for a lease of assets other than a property is hardly understandable and it would be also difficult to add a detailed and rational guideline. Therefore, this means that it would be difficult to practically apply the proposed criterion from practicability and audit perspectives. Furthermore, there is a concern about subjectivity in determining which expense recognition pattern should be applied. As a result, there could be a problem associated with comparability. If the boards develop a detailed and complex guideline in order to solve these concerns, costs associated with applying the new standard would significantly exceed benefits arising from revising the current standard.

JLA's basic view is that several accounting models should be appropriately applied to various types of lease. In the comment letter dated as 25th July 2012, JLA commented that the criterion in IAS 17 *Leases* should be adopted as an indicator to distinguish between two different types of lease. The latest proposal made by the boards includes concerns written above. If the boards publish the re-exposure draft including concerns pointed out above, the proposal would not be an improvement over the current standard, which is widely prevalent. This is why the proposal would not achieve the main objective to appropriately reflect various economics of leases that range from those similar to a service to those similar to a purchase by using two approaches.

In addition, there has been no rational discussion about differences between executory contracts (off-balance sheet treatment) and leases that are required to be recognized on lessee's balance sheet. It would not be an improvement over the current standard that a lessee is required to recognize only leases on its balance sheet without clearly discussing why only leases should be recognized on a lessee's balance sheet, and that the receivable and residual approach, which has some concerns, should be applied instead

of the current lessor's accounting that has not been criticized.

In Japan, there are tens of listed companies which apply the US GAAP. However, there are a handful of listed companies which have already applied IFRS at this moment. If the proposal in the forthcoming re-exposure draft were to be finalized, it could make negative impact on adoption of IFRS in Japan and the number of companies which would apply IFRS.

Therefore, the tentative decision including concerns pointed out above would not be an improvement over the current standard. Instead of the tentative decision, adding some improvements to the current standard should be more reasonable and understandable among constituents including users of financial statements, considering practicability and comparative analysis related to cost-benefit. For instance, it is one of practical solutions to add items in disclosure which will meet needs of users of financial statements for a right and liability that meet the definitions of an asset and liability.

JLA believes that the boards would not finalize the new lease accounting standard without addressing concerns of practicability and cost-benefit analysis related to the proposal by the boards, neglecting the main aim of improving the current lease accounting standard.