Rådet för finansiell rapportering

The Swedish Financial Reporting Board

RFR-rs 2009:11

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sirs,

Re: Discussion Paper DP/2009/1 Leases: Preliminary Views

The Swedish Financial Reporting Board is responding to your invitation to comment on the International Accounting Standard Board's Discussion Paper DP/2009/1 Leases.

We question the proposed model to recognize assets and liabilities for **any** leases entered into without consideration of whether substantial risks and rewards are transferred or not. We believe that only such lease contracts that in substance represent financing transactions for lessees to acquire effective economic ownership of an asset should be recognized in the statement of financial position.

Also, if IFRS 7 would cover all liabilities under this new leasing approach, the workload will substantially increase, as we can foresee that thousands of new items would need to be revalued. Under the current model, only finance lease obligations are revalued at the balance sheet date in order to disclose fair values.

We acknowledge that there are needs for improvement of IFRS in relation to leasing, both from the lessee and lessor perspectives. However, we do not consider that the existing accounting model for leases is broken, as explained below. Instead, we consider that improvements can be achieved by considering the disclosure requirements for annual reports and interim financial reports in order to reflect the specific characteristics of the leasing contracts entered into by lessors and lessees. Under IAS 17 disclosures are given on a yearly basis in the notes to the financial statements. Our view is that material changes to these disclosures should be provided also in the interim financial statements.

The by us proposed improvement of disclosures should not cover only leased assets. In the Financial Statement Presentation DP it is proposed to introduce a presentation of information about the maturities of its contractual long-term assets and liabilities in the notes to financial statements, as we understand similar to "Contractual obligations" under US GAAP today.

By only focusing on the equipment part (as will be the consequence of the proposed model in the discussion paper) the reader will not be given the full information required to understand future cash flows and financial exposure. For example, if a company

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outsources its IT-function not only future costs related to leasing of IT-equipment should in our view be disclosed, but the full "rights to use" of the IT-provider's whole service organization should be presented.

By keeping the present model and adding more disclosures readers will get a better view of the financial position of a company, both compared to the present model and proposed model. Our proposal could also be seen as an at least temporary improvement while IASB develops a model also for lessor accounting. Just amending the lessee part would cause problems for those companies that are both lessors and lessees.

We believe that the present model where leases are classified either as operating or finance leases works in many aspects well. The objective of IAS 17 is to ensure that leases are accounted for in the financial statements of both lessees and lessors in accordance with their commercial substance. A lease that transfers substantially all the risks and rewards to the lessee is classified as a finance lease and the related assets and liabilities is recognized in the statement of financial position by the lessee. Thus, a finance lease is an arrangement that has the substance of a financing transaction for the lessee to acquire effective economic ownership of an asset.

One important argument in the DP for proposing a new accounting model for leases is the statement that preparers and auditors have criticized the existing model for its complexity. Our opinion is that the proposed model is even more complex in its nature, especially in considering the most likely lease term and a probability weighted calculation of contingent rents. The complexity in the existing model relates normally to a few significant lease contracts in an entity that is solved by using professional judgment. Replacing such a model with a system where all leases (including operating leases) are to be analysed as to what is the most likely lease term does in our view create much more complexity. Instead of looking at a few contracts (to categorise as finance and operating leases) entities will have to consider a significant amount of lease contracts (hundreds or maybe thousand of contracts). The factors to be considered in determining the lease term also appear to be very subjective and arbitrary. Accordingly, we think that preparers and auditors will face far more complexity with the proposed model.

It is stated in the DP that users routinely are adjusting the recognized amounts in the statement of financial position in an attempt to recognize assets and liabilities related to operating leases and to reflect the effect of lease contracts in profit or loss. We believe that this statement might be true for lenders, but lenders do not constitute all users of financial statements. We are not aware that user groups other than lenders are adjusting for this.

As stated above we consider that the present model of only capitalising finance leases should be retained. However, we note that, if the present model in IAS 17 is retained, the DP includes certain proposals which would have an impact also on the present principles for accounting for finance leases, if they are introduced. Our views on these proposals are as follows:

- We do not agree with that the lessee should be required to revise its obligation to pay rentals to reflect changes in its incremental borrowing rate. We agree with the FASB's decision not to require reassessment. We note that IAS 39 does not allow changes in the effective interest rate to affect the measurement of financial liabilities in subsequent periods. We also believe that reassessment would lead to a lot of additional work with limited benefits.

- We are concerned with the proposed idea to recognize a liability (and asset) also for likely renewals of the lease term. We do not agree that the inclusion of a renewal option in a lease contract gives rise to a present obligation that arises from past events, and thus the definition of a liability is not met. Under a lease with an option, the lessee can avoid paying rentals after the end of the original lease term. By requiring the recognition of a liability (and an asset) also for renewal periods that are likely to arise, the accounting ignores the fact that the lease could be for a shorter period. Such an approach would also fail to differentiate between a ten-year lease with an option to extend for an additional five years that is likely to be exercised and a fifteen-year lease, where the lessee cannot terminate the lease in advance.

- We consider that contingent rent obligations should not be included in the financial lease obligation.

We do not consider that the DP is an improvement and our strong recommendation is that a revised standard should not be issued. Instead the IASB should improve the disclosure requirements for both lessees and lessors.

If you have any questions concerning our comments please address our Executive member Carl-Eric Bohlin by e-mail to: carl-eric.bohlin@radetforfinansiellrapportering.se.

Stockholm, July 6, 2009

Kind regards,

Anders Ullberg
Chairman