## BELGIAN ACCOUNTING STANDARDS BOARD

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Dear Sir, Madam,

The Belgian Accounting Standard Board welcomes the opportunity to comment on the Draft Comment Letter of EFRAG concerning the Discussion Paper Leases - Preliminary Views.

We recognise the importance to develop a new model for the recognition of assets and liabilities arising under lease contracts because we are aware that the existing standards provide opportunities to structure transactions so as to achieve a particular lease classification.

Our detailed comments on the questions are set out below. Generally we agree that there is a need for convergence but at the same time we want to underline the possible impact and consequences of this project. We wonder if such a structural change was really needed. Will the use of a new standard result in more useful information?

The Board tentatively decided to defer consideration of lessor accounting and to concentrate on developing an improved lessee accounting model. However, we are concerned that fundamental decisions about the future direction of lease accounting will be taken having considered the subject from only the lessee's perspective. As a consequence, we hope that the Boards is aware that there are many lessor-accounting issues that still need to be addressed and discussed before publication of a new accounting standard.

Conceptually maybe the lease project could merely supplement the revenue recognition project as related to a specific case where the buyer/lessee should not recognise a right (intangible) to services/goods but obtains the ownership of an asset (which could be tangible or intangible) during a non cancellable time.

### 1. *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.**

The Boards' preliminary view is that the scope should be based upon the scope of the existing standard. As a consequence, we emphasize the need for a better clarification of the "unit of accounting". In certain cases (leasing contracts that include service arrangements) a buyer/lessee has no expertise to operate the asset and/or the operation of the asset might be critical and very expensive to develop in-house (for example a vessel that can not sail without qualified crew, a power plant which can not deliver electricity without qualified personnel). When there is no market based evidence of the revenue generated from the asset and its servicing on a separate basis, but rather on an aggregate basis, should one distinguish two separate units of accounting? Currently, we do distinguish, especially under IFRIC 4 and IFRIC 12. If we keep doing so, clarification of the above could be useful, being aware that the answer should be consistent with the requirements in the revenue recognition project with respect to multiple elements.

**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.**

Non-core asset leases or short-term leases should not be excluded from the proposed new standards. Repetitive short-term lease contracts can also be significant. Short-term does not mean "immaterial". Having said this, the BASB wants to underline that the materiality concept has already been included in the framework. Each entity can define an entity-specific PPE capitalization threshold.

## 2. *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.**
**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.**

Will the Boards' analysis of the rights and obligations and the assets and liabilities arising in a lease contract result in more relevant and useful information? In the proposed model the liabilities arising on both financial and operational leasing will be presented in the statement of the financial position, which, in our view could lead to more objectivity. Although, this will have an important impact on the presentation of the operational lease-contracts and even on the workload (the preparation of the financial statements). In this context, again, we want to underline the importance of a decent use of the materiality principle.

Concerning the right-of-use approach, we think there should be more guidance whether the right-of-use asset is a tangible versus intangible asset. For example we can hold a legal title to a building and economically control this building. This building will, as a consequence, be recognised as a tangible, even if we control this tangible thanks to an intangible (i.e. the certificate of ownership).

What if a lease-contract do not fulfil the conditions? What with lease contracts where the payment of the rentals depends on the output? If we think, for example, at a energy wind park. If there is no wind, there will be no output neither payments. Who's bearing the risks?

Under the new definition, based on the analysis of the rights and the obligations, assets and liabilities, a lessee is able to recognise an asset which he does not own. Consequently, the difference between assets owned by the lessee and not owned by the lessee, might, in our view, not be very clear.

Lease contracts are also often more complex than the simple lease contracts described in the Discussion Paper. Those lease contracts can convey a range of rights and obligations to the lessee. For example a lease contract may include:

- options to extend the lease on payment of additional rentals;
- options to terminate the lease early;
- options to purchase the leased asset on payment of an additional amount;
- obligations to pay variable rentals or contingent rentals;
- obligations to compensate the lessor if the value of the leased asset declines below a specified value (residual value garantuees).

**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?**

We agree with the decision not to adopt a components approach.

## 3. *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.**

The BASB proposes to measure the lessee's obligation to pay rentals at the present value of the lease payments discounted using the interest rate implicit in the lease-contract.
However, in many instances the lessee will not know or be able to determine the implicit rate, particularly in cases currently classified as operating leases. If it is not practicable to determine the interest rate, the lessee's incremental borrowing rate could be used since this is also in line with the requirements of IAS 16.

When obtaining an at arm's length compensation for the lessor's financing risk incurred, we would think the rate implicit in the lease approximates the lessee's incremental borrowing rate, unless the lessor also incurs servicing risks or bears a significant residual value risk.
As fair value accounting has been pushed in so many IFRSs, it seems strange to develop a different measurement basis here. We agree that in case of difficulty in determining the fair value, the lease standard should, indeed, provide specific guidance. In such cases, the lessee's incremental borrowing rate seems appropriate.

**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.**

Once we have defined the type of the asset/liability we wonder what is the technical merit of creating a separate measurement basis when existing IFRSs adequately address those? If IAS 16, 36, 38 and 39 will change, will we change the lease standard as well? And what in case the US GAAP lease standard wouldn't follow? Different measurement bases in IFRS or US GAAP of the underlying seems insufficient justification, because this will mean that depending on whether we buy/lease the asset, different measurement bases could be distinguished, without underlying economic reality justifying this difference.

We agree to initially measure the lessee's right-to-use asset at cost (which will generally equal the fair value of the obligation to pay rentals)

## 4. *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 proposed approach.

**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.**

We do not believe there should be an option to measure a lease obligation at fair value.

**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.**

We believe that the obligation to pay rentals should not be revised for changes in the incremental borrowing rate.

**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 that a lessee's obligation to pay rentals meets the definition of a financial liability and could be accounted for correspondingly.

**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 amortisation or depreciation in the income statement. Would you support this approach? If so, for which leases? Please explain your reasons.**

We do not agree that for some leases the decrease in value of the right-to-use asset should be described as rental expenses rather than amortization or depreciation in the income statement, since this means that several assets of the same entity can be treated in different ways. This contradicts the treatment of other intangibles and tangibles.

## 5. *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 support the idea that the lease term should be based on the best estimation of the lease term. Since IAS 39 already provides guidance on the "expected life of the financial instrument", what is the benefit of creating an assessment specific to leases?

**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 support the proposal that the lease term should be reassessed at each reporting date on the basis of any new facts or circumstances because we think such an approach is likely to provide users with more relevant information.

**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 support the Boards' proposal.

## 6. *Contingent rentals and residual value guarantees*

**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 proposal.

**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.**

We agree with the approach to measure the lessee's obligation to pay rentals including a probability-weighted estimation of contingent rentals payable.

**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 agree with the proposed approach.

**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.**

The BASB supports the boards tentative decision.

**Question 20— The boards discussed two possible approaches to recognizing 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, or (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 support the recognition of any change in the liability as an adjustment to the carrying amount of the right-of-use asset.

**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?**

Yes, we agree with the proposed approach.

## 7. *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 BASB is of the opinion that the lessee's obligation to pay rentals should not be presented separately from other liabilities in the statement of the financial position, because the difference with the other liabilities is not so significant. This kind of information could be presented in the notes.

**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?**

In case of a lease contract without a purchase option, the BASB supports the Boards' tentative decision to require a separate presentation of the right-to-use asset, according to the nature of the underlying lease on the face of the statement of financial position.
If the lessee does have a purchase option, we are of the opinion that the right-to-use asset should be presented according to the nature of the underlying asset

## 8. *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.**

In our view also the next topics should be dealt with in the Discussion Paper: the timing of initial recognition; sale and leaseback transactions; treatment of initial direct costs and leasing contracts that include service arrangements.

## 9. *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.**
**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.**
**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.**
**Question 28—Should accounting for investment properties be included within the scope of any proposed new standard on lessor accounting? Please explain your reasons. Question 29—Are there any lessor accounting issues not described in this discussion paper that the boards should consider? Please describe those issues.**

The Board tentatively decided to defer consideration of lessor accounting and to concentrate on developing an improved lessee accounting model. Chapter 10 on lessor accounting describes only how a right-of-use model may be applied to lessors. However, we are concerned that fundamental decisions about the future direction of lease accounting will be taken having considered the subject from only the lessee's perspective.

As a consequence, we hope that the Boards is aware that there are many other lessor-accounting issues that still need to be addressed and discussed before publication of a new accounting standard.

Yours sincerely

Jan Verhoeye
Chairman