We are Making a Difference

The FASB listened to feedback

By Bill Bosco, Leasing 101

Although the joint IASB/FASB Lease Project is still a work in progress the FASB has listened to the industry feedback and adjusted its position on both lessee and lessor accounting. The FASB has decided to keep the current lessee GAAP premise that there are two types of leases with different P&L cost and balance sheet treatment. The IASB remains stuck on having lessees account for all material leases as though they are capital leases. The position of both boards is to keep lessor accounting unchanged with minor exceptions. Both boards did also significantly reduce the compliance burden for lessees.

Success!

I feel that, no matter what the eventual outcome of the project, it is not too early to declare some measure of success from the ELFA's efforts and from all those of you in the leasing industry that made the effort to write comment letters and let your concerns be known. Our noble objective was to make the Lease Project proposed rules reflect the substance of leases for both lessees and lessors.

There is a secret formula for successful results in work or life. It is: the results of your work/life = the product of ability X attitude X effort X how well you work with others. To develop this formula I borrowed from the philosophic writings of noted Japanese business philosopher Dr. Kazuo Inamori and the input of noted accountant John E. Stewart who is the co-founder and Managing Director of Financial Reporting Advisors, LLC.

The ELFA used that formula to get the results that look so promising today. When the project first began it looked as though our customers might change their behavior because of the proposed distortive accounting for lease costs and the heavy compliance burden to continually reassess estimates of lease payments and rebook leases. It looked as though lessors would have to completely change accounting systems and also be subject to distortive accounting for both the balance sheet and income statement.

The Roadmap to Success - Ability

The first step was to assemble the people with the ability to make it happen. That meant filling leadership and execution roles. The leadership started with Michael Fleming, former ELFA President. Mike perceived the initial threat in the "G4+1" papers written in the 1990's by members of the FASB and IASB, describing a new approach to lease accounting and the association began monitoring and commenting on those papers. He foresaw that if a re-write of the lease accounting rules was added to the FASB agenda they would base the rules on the G4+1 papers' approach to lease accounting. When Mike retired in 2006, Ralph Petta, ELFA Chief Operating Officer, took over the leadership role. An execution team was assembled of key members of the ELFA financial accounting committee: current Chairperson, Rod Hurd, John Bober, Mindy Berman and me. We also got assists from various ELFA financial accounting committee and legal committee members. The execution team had diverse leasing business experience. They were tasked with monitoring the board meetings, analyzing issues, and commenting on the project's deliberations and Exposure Drafts. The ELFA also nominated me to be a member of joint IASB/FASB Lease Project Working Group designed to provide the boards and staff with technical advice and input from "the real world". Another member of our execution team, John Bober, was also selected to serve on the Working Group. All in all, the association was well-positioned to provide input, guidance and technical expertise to the Boards and staff as the project proceeded.

The Roadmap to Success: Attitude

From the start, the ELFA adopted a "High Ground" approach – that is, we always took the position on issues that was objective, credible, and did not appear self serving. It meant that we would not defend rules that in the full light of day would be viewed as abusive. Said another way, we did not want to be perceived as defending rules that obfuscate and distort the financial results of lease transactions . Using this high ground approach has gotten us a "seat at the table" as the FASB views us with a high level of trust and credibility and accepts our feedback as being helpful in achieving their project's goals. Early on, the ELFA went on record supporting the FASB's Lease Project. The catalyst to this strategic position was the SEC's stated goal to capitalize operating leases as an improvement in financial reporting for the benefit of users of financial statements. That is the "high ground" position as the SEC is tasked by Congress with ensuring that US securities markets are fair and honest. They are also responsible for ensuring that US investors are adequately informed and their interests are protected.

The ELFA also maintained a "never give up" mentality as we aggressively pressed our advocacy issues through comment letters, public and private meetings with the boards and participation in Lease Project outreach and working group meetings.

The Roadmap to Success: Effort

The ELFA recognized that there was a need to raise US businesses' awareness of the impact of the proposed rules. We did an analysis of major companies who reported large amounts of future operating lease payments in their footnotes. We developed impact analyses by industry and leased asset type. It was at that point that we realized that real estate leases accounted for about 80% of the dollar volume of reported operating lease payments. We had to raise awareness in the real estate industry and joined an informal coalition with real estate industry participants. The most heavily impacted industries were retail, banking and transportation companies. We made the effort to reach out to those industries through their trade associations, their trade magazines and general business publications. We did webinars targeted to lessees. We made presentations at industry conferences of lessee groups most impacted, including retail, real estate, auto fleet and truck rental. We developed a capitalization model that lessees could use to predict the financial impact of the project on their existing operating leases. The ELFA developed a section on its website devoted to the Leases Project and provided information and tools for use by the public to understand the impact of the project. In addition, the work was augmented by the Equipment Leasing and Finance Foundation, which developed an important study on the project's potential negative impact on US business's performance and the economy.

The Roadmap to Success: Working with Others

From the outset of this project in 1995 when the first G4+1 new approach to lease accounting paper was issued , the ELFA began efforts to work with other leasing trade organizations, lessee trade organizations and the US Chamber of Commerce. In that regard we kept each other informed on intelligence and tried to coordinate efforts where possible. The ELFA met regularly with the FASB and occasionally with the IASB to share our views and comment on issues. We reminded them that our intentions were to provide them with useful information and help if they needed it. They have taken us up on that offer many times. The ELFA also met and continues to meet annually with the SEC and its Office of Chief Accountant to provide them with our input.

What Defines Success?

As it stands (and some of this can change as it's not over 'till it's over), we can measure many key elements of success that would not have occurred had we not put in place and executed on our strategy My prediction: Our lessee customers will record only the present value of operating leases on balance sheet and the lower the present value the more the balance sheet benefit. The P&L cost will remain the same (straight line cost) as current GAAP and not front loaded. The accounting treatment for lessees will still mesh with the tax and legal view as all will be based on the substance of the contract. Separately reporting capitalized operating lease obligations should mean debt limit covenants should not be impacted. There are fewer instances where lessees have to reassess calculations of lease payments and the lease term, thus reducing the burden of adjusting and rebooking leases. Lessors will continue to use current GAAP saving systems costs and preserving what works today.

The Road Ahead

There is still work to be done. We have to continue to follow the project to ensure there is no back sliding. We need to keep up the pressure. We still have to fight to preserve current sale leaseback accounting. Saving leveraged lease accounting is still on our list but I was reminded by a friend of Don Quixote's impossible dream. To paraphrase: " We will, still scorned and covered with scars, continue to strive with our last ounce of courage to reach the unreachable star/impossible dream." But, why not keep trying as we captured so many other seemingly unreachable stars?

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