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Discussion Paper DP/2009/1 – Leases Preliminary Views

Dear Sir David

Thank you for the opportunity to comment on the discussion paper "DP/2009/1 – Leases Preliminary Views", which was published by the International Accounting Standards Board (IASB) in March 2009.

We welcome the initiative of the IASB in undertaking a clarification of the accounting system for leasing transactions. However, we believe that the right-of-use approach still requires more conceptual work. The application of right-of-use accounting principles leads to unnecessary inflation of the balance sheet and correspondingly to the impairment of its clarity and information value.

Furthermore, it is questionable whether the right-of-use approach is actually suitable for providing the relevant, transparent and complete information regarding leasing conditions and relationships desired by the standard setters. In view of the treatment of options, conditional leasing payments and residual value guarantees currently under discussion, the latitude for discretionary measures and formative influence would increase significantly, so that the balance sheet values would convey only a spurious accuracy.

In any case, the additional accounting effort and expense for most leasing relationships is not in any appropriate proportion to the benefit of the information for the balance sheet users. Additional information requirements regarding off-balance-sheet transactions could be better met by expanded disclosure obligations in an appendix.

Due to the overly hasty measures, the opportunity to prepare a coherent and definitive concept is being wasted. The separation of lessor and lessee

accounting results in the toleration of conceptual discontinuities in the system. In particular, this would result in problems when companies – possibly in various divisions – function both as lessors and lessees. In the future, the same set of circumstances would be described using differing accounting concepts for lessors and lessees, which would unnecessarily increase complexity and impair the clarity of the balance sheet.

Furthermore, there are **connections between the leasing reform and other "reforms in progress"** in the area of international standards. Uncoordinated activity in the area of leasing poses the risk of new inconsistencies and a renewed need for reform. A "reform of the reform" which would be required in the foreseeable future is simply unacceptable for balance sheet preparers, users and auditors.

The standard setters have given the leasing project top priority within the convergence process between IFRS and US GAAP. From their point of view, failure or postponement of the leasing project would endanger the superordinate goal of adoption of the IFRS in the United States and in other major industrial countries by 2013/2014. However, in the United States an increasing number of people are demanding postponement of the initial application of IFRS in that country. Mr. Herz of the FASB believes that convergence will take 10 to 15 years. In view of these signs, the overhasty passage of a leasing standard should be avoided.

Specifically, we wish to address the following four points, which are particularly important for our member institutions as lessees.

1. Avoidance of unnecessary complexity

As part of the reform, complexity and unnecessary accounting effort and expense are to be avoided. In any case, it must be ensured that the additional accounting effort and expense with which the lessees are burdened are in an appropriate proportion to the value of the information conveyed. In particular, the new requirements must not be oriented in an undifferentiated fashion to what some of the balance sheet users would possibly expect as additional balance sheet information in the case of individual big-ticket leases with especially complex structures. The economic attractiveness of the great majority of completely routine leasing transactions must not be impaired by excessive accounting requirements. This applies particularly to the probability-based initial valuation and revaluation issues relating to options, conditional leasing payments and residual guarantees.

2. Exceptions for properties that are not part of the core business of the lessee

An appropriate relationship between accounting effort and expense and information requirements would be facilitated if certain routine leasing transactions were exempted from the scope of application of the new standard and further handled according to the current operating lease procedure. Contracts for

leased properties that are not part of the core business of the lessee would be affected in this case. In particular, properties that are individually of subordinate importance, that are fungible and that are not directly part of the production or distribution process of the lessee could be removed from the scope of application. Examples of these include company cars, copy machines and IT equipment. For leasing transactions involving such property, which make up a substantial part of the overall leasing market, the balance sheet users should not require additional information, so that the application of the right-of-use approach could be eliminated with a view to accounting effort and expense.

3. Leasing should be shown as a separate construct in the balance sheet

The reflection of leasing relationships in the balance sheet should do justice to their character as an independent construct sui generis. An implementation of the reform would expand the latitude for appropriate, functional solutions, even if these deviate from existing standards which, however, are based on different constructs (e.g. purchase transactions). Among other things, the character of leasing means that the resulting liabilities are very closely tied to the resulting right of use. After all, both of these are based on one and the same contract (in contrast to a loan for financing a purchase). Thus the de-linked approach should be rejected, as over time it leads to a discrepancy between the book values of the right of use and the liability. Only an accounting-based synchronisation of leasing assets (right of use) and leasing liabilities will be appropriate to the character of leasing.

4. Balance sheet structure and regulatory arrangements

The right-of-use approach has direct effects on the balance sheet structure and key earnings figures for the lessee. The additional accounting approach of operating leases would cause an extension of the balance sheet; an increasing external capital ratio and a falling equity ratio would result.

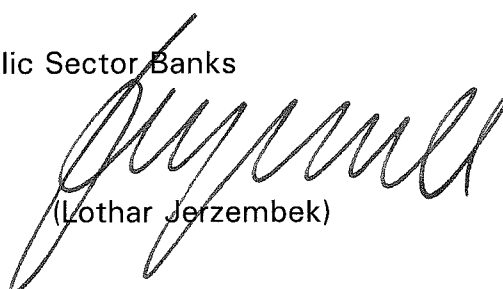
With regard to the application of the IFRS for regulatory purposes, far-reaching bank supervisory consequences could result. In the case that no regulatory corrective measures ensue, the revised leasing accounting would result in a sustained change in the regulatory equity capital ratios. In our opinion, this has a direct influence on the possible scope of business in the future, on the specification of terms and conditions and on the profitability of institutions and their position in the capital market.

Should you have questions or require further discussions, we will be pleased to assist you at any time.

Yours sincerely
Association of German Public Sector Banks



(Karl-Heinz Boos)



(Lothar Jerzembek)