

A decorative horizontal bar at the bottom of the slide, composed of various colored rectangular segments in shades of blue, yellow, orange, red, and purple. The word "Leases" is centered above this bar.

Leases

Main concerns



- What is a lease?
- Should all leases be accounted in the same way?
- How should options and contingent rentals be treated?

Other concerns



- Leases of intangible assets
- Short-term leases
- Sale and leaseback transactions

What is a lease?

- What did the ED say?
 - The ED maintained the same definition as in IAS 17.
 - Entities should identify leases based on the two criteria:

The arrangement involves a specified asset

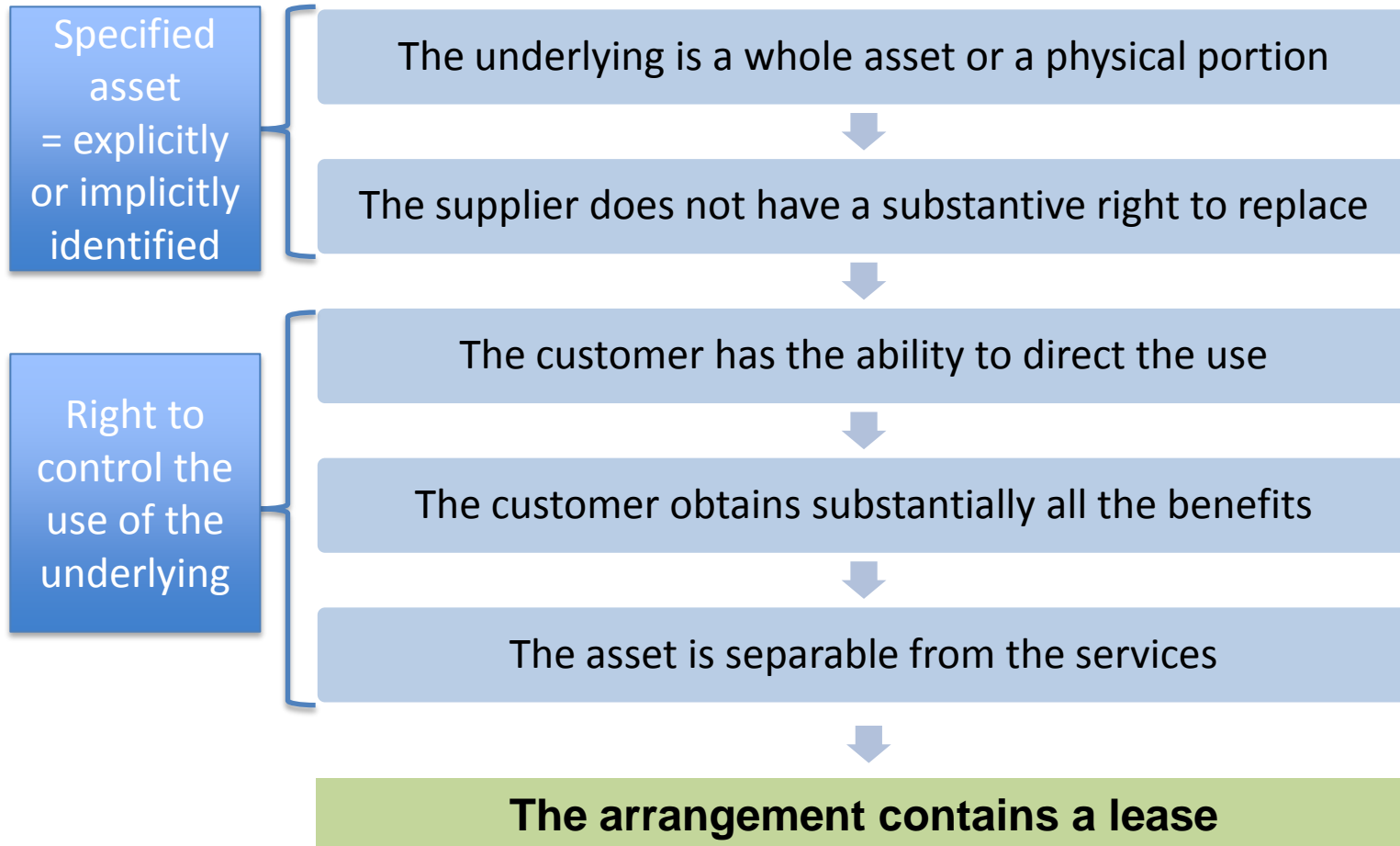
AND

The arrangement conveys the right to control the use

What is a lease?

- What were the concerns?
 - The criteria may capture arrangements that in substance are services.
 - The criteria in IFRIC 4 are unclear and raise common application issues.

What is a lease?



□ Are all leases the same?

- What did the ED say?
 - Lessees should recognise a purchase of a right-of-use asset (RoU) and a liability to make lease payments.
 - At inception, the RoU and the liability are measured at the present value of future payments.
 - The liability is subsequently measured at amortised cost.
 - The RoU is subsequently amortised using IAS 38 (normally on a straight-line basis).

□ Are all leases the same?

- What were the concerns?
 - Not all leases are financing transactions.
 - The accounting treatment front loads expenses.

Are all leases the same?

LIABILITY				RIGHT OF USE			
Opening	Interest	Payment	Closing	Opening	Amort	Closing	P&L
476.65	33.37	(100.00)	410.02	476.65	79.44	397.21	112.81
410.02	28.70	(100.00)	338.72	397.21	79.44	317.77	108.14
338.72	23.71	(100.00)	262.43	317.77	79.44	238.33	103.15
262.43	18.37	(100.00)	180.80	238.33	79.44	158.88	97.81
180.80	12.66	(100.00)	93.46	158.88	79.44	79.44	92.10
93.46	6.54	(100.00)	-	79.44	79.44	-	85.98

□ Are all leases the same?

- What has been done?
 - Acknowledgement that not all leases are financing transactions.
 - A dual model to differentiate between finance and other-than-finance (OTF) leases.
 - Distinction based on current guidance in IAS 17 (exposure to risks and rewards).
 - All leases are recognised on the balance sheet.
 - OTF leases, the recognition of the total cost (interest expense + amortization) is straight-line over the lease term.

Are all leases the same?

LIABILITY				RIGHT OF USE			
Opening	Interest	Payment	Closing	Opening	Amort	Closing	P&L
476.65	33.37	(100.00)	410.02	476.65	66.63	410.02	100.00
410.02	28.70	(100.00)	338.72	410.02	71.30	338.72	100.00
338.72	23.71	(100.00)	262.43	338.72	76.29	262.43	100.00
262.43	18.37	(100.00)	180.80	262.43	81.63	180.80	100.00
180.80	12.66	(100.00)	93.46	180.80	87.34	93.46	100.00
93.46	6.54	(100.00)	-	93.46	93.46	-	100.00

□ How should options be treated?

- What did the ED say?

OPTIONS TO EXTEND OR TERMINATE

- Amounts due under renewal options should be included based on the longest lease term more likely than not to occur.
- This is different from IAS 17, that requires including those amounts only when the exercise of the option is reasonably certain.

□ How should options be treated?

- What did the ED say?

OPTIONS TO PURCHASE

- A lease that includes a bargain purchase option should be treated as a purchase
- Other purchase options should be ignored until exercise.

□ How should options be treated?

- What were the concerns?
 - Amounts due under options are not liabilities.
 - Options should receive the same accounting treatment.
 - Options should be separately recognised and measured.
 - Assessment of “more likely than not” difficult and creates volatility on the balance sheet.

How should options be treated?

- What has been done?
 - The Boards now require recognition of amounts due under renewal and purchase options only when they create a significant economic incentive for the holder.
 - A significant economic incentive may exist because:
 - The rentals in the optional period are at favorable terms;
 - The lessor offers some incentive in case the lessee exercises the options;
 - The lessee has made significant investments in the leased asset (i.e. leasehold improvements) that would be lost if the option is not exercised.

How should contingent payments be treated?



- What did the ED say?
 - Contingent payments should be included in the measurement of lease assets and liabilities.
 - Contingent payments should be measured using an expected value approach, and remeasured subsequently.
 - This is different from IAS 17, that excludes contingent payments from minimum lease payments.

How should contingent payments be treated?



- What were the concerns?
 - Amounts due under certain types of contingent payment arrangement (based on usage or performance) are not liabilities.
 - These amounts often cannot be reliably measured.
 - Expected value approach is complex and creates volatility

How should contingent payments be treated?



- What has been done?
 - The Boards now require recognition of contingent payments only if:
 - The payments are contingent on a future rate or index; or
 - The payments are in-substance fixed minimum payments.

Leases of intangible assets

- What did the ED say?
 - Leases of intangible assets are excluded from scope.
 - IAS 17 excludes from its scope only leases of certain intangible assets.

Leases of intangible assets

- What were the concerns?
 - There is no conceptual reason to exclude leases of intangible assets from the scope.
 - Contracts that include leases of both tangible and intangible assets would have to be separated.
- What has been done?
 - The Boards tentatively decided that leases of intangibles are not required to be accounted for in accordance with the leases standard.

Short-term leases

- What did the ED say?
 - Lessors may elect not to apply lease accounting to short-term leases.
 - Lessees may elect not to discount the liability and the right of use asset.

Short-term leases

- What were the concerns?
 - No real relief for lessees.
- What has been done?
 - No change for lessors.
 - Lessees will be allowed to elect not to account for assets and liabilities arising from short-term leases.
 - The election must be made for each category of underlying assets.

Sale and leaseback transactions

- What did the ED say?
 - In a sale and leaseback (S&LB) the parties must assess if the first part qualifies as a sale.
 - If it does not qualify as a sale, the transaction is a borrowing.
 - If it qualifies as a sale:
 - the lessee should derecognise the asset in full and recognise the RoU and liability arising from the leaseback;
 - The lessor should recognise the asset and a receivable, and apply PO approach to the leaseback.

Sale and leaseback transactions

- What did the ED say?
 - If the sale consideration or the rentals due in the leaseback term are not at fair value:
 - The seller/lessee should adjust the RoU and the gain.
 - The buyer/lessor should adjust the underlying asset and the lease liability in the PO approach.
 - The proposals were different from IAS 17, which requires deferral of the gain made by the seller/lessee if the leaseback is a finance lease.

Sale and leaseback transactions

- What were the concerns?
 - There should be no additional criteria to assess if the first part of the transaction is a sale.
 - The lessee should derecognise only a portion of the asset.
 - The lessor should only recognise the residual asset.

Sale and leaseback transactions

- What has been done?
 - The criteria in the Revenue Recognition Standard should be applied to assess if the first part of the transaction is a sale.
 - The Boards require that the final Leases standard is applied to the leaseback part of the transaction.

□ And for the lessors?

- What did the ED say?
 - Lessors should apply a dual approach based on exposure to risks and benefits.
 - When the risks and benefits are transferred, the lessor would derecognise a part of the asset and recognise a receivable (so called *derecognition approach*).
 - If not, the lessor would maintain the asset, recognise a receivable and a lease liability for the same amount (so called *performance obligation approach*).
 - The lease liability is accreted over the lease term.

□ And for the lessors?

Book value of the asset	600,000
Fair value of the asset	800,000
Expected value of the residual	100,000
Lease period in years	5
Interest rate	7%

	PO approach		Derecognition approach	
PPE	600,000		53,474	
Lease receivable	728,701		728,701	
Lease liability		728,701		-
Gain in P&L		-		182,175

□ And for the lessors?

- What were the concerns?
 - The performance obligation (PO) approach is inconsistent with the notion that the lease is executed when the lessor gives access to the underlying asset.
 - The PO approach grosses up assets and liabilities and creates application issues relating to impairment calculations.
 - The dual approach is inconsistent with the single accounting approach for the lessees.

□ And for the lessors?

- What has been done?

THE BOARDS HAVE NOT COMPLETED REDELIBERATIONS ON LESSOR ACCOUNTING

- Dual model for lessors still confirmed. Distinction to be made using the same criteria as for lessees.
- The Boards will consider accretion of the residual or fair value accounting in the derecognition approach.
- The Boards will consider net presentation in a PO approach, or operating lease accounting. Gross presentation in a PO approach has been dropped.