

## Agenda Item 10: Leases

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IPSASB Meeting

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## Objective of Session & Material Presented

- Agenda Item 10.2.1—Terminology: Conceptual Framework and IPSASs
- Agenda Item 10.2.2—Objective, Scope and Definitions
- Agenda Item 10.2.3—Lessor: Recognition exemptions
- Agenda Item 10.2.4—Identifying a lease, in-substance fixed lease payments, and lessee involvement with the underlying asset before the commencement date
- Agenda Item 10.2.5—Manufacturer or dealer lessors
- Agenda Item 10.2.6—Lessor—Separating components of a contract

## Objective of Session & Material Presented

- Agenda Item 10.2.7—Lessor—Lease modifications
- Agenda Item 10.2.8—Sale and leaseback transactions at below market terms
- Agenda Item 10.2.9—Lessor—Credit entry
- Agenda Item 10.2.10—Lessor—Measurement
- Agenda Item 10.3—Exposure Draft Development—Process
- Agenda Item 10.4—Draft Exposure Draft, *Leases* (marked-up from IFRS 16, *Leases*)

# Terminology–Conceptual Framework and IPSASs (Agenda Item 10.2.1)

IFRS 16	IPSASB's draft ED
Fair Value	Fair Value
Income	Revenue
Profit	Surplus
Loss	Deficit
Business unit	Operation
Business segment	Segment

- Matter for Consideration**

Does the IPSASB agree with the proposed terminology changes included in the draft ED on Leases?

# Objective, Scope and Definitions (Agenda Item 10.2.2)

- **Objective (ED.1–2)**

Inclusion of accountability and decision-making

- (a) The IPSASB decided to depart from IFRS 16 requirements on lessor; and
- (b) Providing the same objective in an IPSAS on Leases with a different lessor accounting model might be misleading to users that use both IFRSs and IPSASs.

- **Matter for Consideration**

Does the IPSASB agree with staff's approach to the Objective of the ED on Leases?

# Objective, Scope and Definitions (Agenda Item 10.2.2)

- **Scope (ED.3–4)**

- (a) Adaptation to reference IPSASs; and
- (b) Additional exclusion of leases for zero or nominal consideration

- **Matter for Consideration**

Does the IPSASB agree with staff's approach to the Scope of the ED on Leases?

# Objective, Scope and Definitions (Agenda Item 10.2.2)

- **Definitions (ED.5)**

- (a) Definition of a contract

A lease is a **contract**, or part of a **contract**, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.



Not a defined term in IPSASs. Defined in IFRS 15.

A contract is an agreement between two or more parties that creates enforceable rights and obligations.

*In the public sector there are other forms of arrangements that do not take the form of a documented contract.*

# Objective, Scope and Definitions (Agenda Item 10.2.2)

- **Definitions (ED.5)**

- (a) Definition of a contract

Option 1	Option 2
<ul style="list-style-type: none"><li>• <b>Retain</b> the IFRS 16 term “<b>contract</b>”</li><li>• <b>Add</b> the definition to the IPSASB’s glossary of defined terms</li><li>• <b>Provide</b> additional guidance in the Application Guidance – Substance over form</li></ul>	<ul style="list-style-type: none"><li>• <b>Replace</b> the IFRS 16 term “<b>contract</b>” in the definition of a lease with a definition of “<b>binding arrangement</b>” to be used only for the purpose of the Leases Standard</li><li>• <b>Explain</b> the rationale in the Basis for Conclusions</li></ul>



# Objective, Scope and Definitions (Agenda Item 10.2.2)

## • Definitions (ED.5)

### (a) Definition of a contract

	Option 1	Option 2
Advantages	<ul style="list-style-type: none"> <li>• <b>Consistency</b> with IFRS 16, IPSAS 28, and the IPSASB's project to update IPSAS 28-30 (except the contract definition)</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Consistency</b> with IPSAS 32</li> </ul>
Disadvantages	<ul style="list-style-type: none"> <li>• <b>Inconsistency</b> with IPSAS 32</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Inconsistency</b> with IFRS 16, IPSAS 28, and the IPSASB's project to update IPSAS 28-30 (except the contract definition)</li> </ul>

# Objective, Scope and Definitions (Agenda Item 10.2.2)

- **Definitions (ED.5)**

- (a) Definition of a contract

Staff supports Option 1 because:

- (a) Both proposed draft Application Guidance and Basis for Conclusions will **inform preparers** that the term “contract” requires leases to be legally enforceable; and
    - (b) **Keeps convergence** with IFRS 16, consistency with IPSAS 28, and the IPSAS’s project to update IPSAS 28-30.

- **Matter for Consideration**

Does the IPSASB agree to retain the term “contract” or replace it with the term “binding arrangement” in the ED?

# Objective, Scope and Definitions (Agenda Item 10.2.2)

- **Definitions (ED.5)**

- (b) Other definitions (by exception)

- (i) Amendments to the definitions: initial direct costs and interest rate implicit in the lease  related to IFRS 16 lessor accounting

- (ii) Exclusion from ED:

- (a) IFRS 16 lessor accounting definitions

- (b) Fair value, Unguaranteed residual value, Useful life

- **Matter for Consideration**

Does the IPSASB agree with staff's approach to the other definitions in the draft ED?

# Lessor–Recognition Exemptions (Agenda Item 10.2.3)

- **Optional Recognition Exemptions in Lessee Accounting**
  - Short-term leases
  - Leases for which the underlying asset is of low value
- **Staff's View**
  - Reasons for lessee accounting recognition exemptions **are also applicable** to lessor accounting.
  - **No additional criteria identified** for lessors to classify leases for which the underlying asset is of low value (ED.AG6)
- **Staff's Recommendation**
  - **Adopt** the same optional recognition exemptions in lessor accounting

# Lessor–Recognition Exemptions (Agenda Item 10.2.3)

- **Matter for Consideration**

Does the IPSASB agree with the staff's recommendation to:

- (a) **Adopt** the optional recognition exemptions for lessor accounting on short-term leases and leases for which the underlying asset is of low value?
- (b) **Not include** additional criteria for lessors to classify leases for which the underlying asset is of low value?

# Identifying a lease, in-substance fixed lease payments, lessee involvement with the [...] (Agenda Item 10.2.4)

(a) Identifying a lease		(b) In-substance fixed lease payments		(c) Lessee involvement with the underlying asset before the commencement date	
IFRS 16	ED	IFRS 16	ED	IFRS 16	ED
9–11, B9–B31	10–12, AG10–G32	B42	AG48	B43–B44	AG49–G53

- **Staff's View**
  - No public sector specific reason identified that warrants different guidance in the ED
- **Staff's Recommendation**
  - **Adopt** the same guidance in the ED

# Identifying a lease, in-substance fixed lease payments, lessee involvement with the [...] (Agenda Item 10.2.4)

- **Matter for Consideration**

Does the IPSASB agree with staff's recommendation to include in the ED the IFRS 16 guidance on:

- (a) How to identify a lease?
- (b) In-substance fixed lease payments?
- (c) Lessee involvement with the underlying asset before the commencement date?

## Manufacturer or dealer lessor (Agenda Item 10.2.5)

- Based on risks and rewards incidental to ownership
- **Staff's Recommendation – Reasons to exclude from the ED:**
  - (a) The lessor model proposed for the ED is **not based** on risks and rewards;
  - (b) Manufacturer or dealer lessor **is expected to be very rare** in the public sector; and
  - (c) Developing new manufacturer or dealer lessor accounting guidance in the context of the right-of-use model would **require additional time to complete the project**, while providing limited benefits.



# Manufacturer or dealer lessor (Agenda Item 10.2.5)

- **Matter for Consideration**

Does the IPSASB agree with staff's recommendation to exclude guidance on manufacturer or dealer lessor in the ED?

## Lessor—Separating components of a contract (Agenda Item 10.2.6)

- IFRS 16 cross-references to IFRS 15
- IPSASB's literature does not have the equivalent guidance
- IPSAS 9.18 is the most applicable guidance

- **Two options:**

### Option 1—Replace the cross-reference to IFRS 15 with IPSAS 9

- **Advantage**—provides guidance that did not exist in IPSAS 13
- **Disadvantage**—provides guidance that is different from IFRS 15

### Option 2—Remove paragraph 18 of the draft ED

- **Maintain** IPSAS 13 approach (no explicit requirements to allocate the transaction price to components of a contract)
- Currently, preparers rely implicitly on IPSAS 9

# Lessor—Separating components of a contract (Agenda Item 10.2.6)

- **Staff's Recommendation**

Option 1. **Consistency** with previous IPSASB's decisions (ex: sale and leaseback transactions)

- **Matter for Consideration**

Does the IPSASB agree with staff's recommendation to replace the cross-reference to IFRS 15 with IPSAS 9 (Option 1)?

## Lessor–Lease modifications (Agenda Item 10.2.7)

- Retention of IFRS 16.79 in the ED with minor amendments (see ED.74)
  - This guidance can be applicable to lessor accounting
- Exclusion of IFRS 16.80 in the ED
  - This guidance relates to the risk and rewards model in IFRS 16 that has not been retained in the ED
- Use the lessee accounting requirements in IFRS 16.45–46 as a basis for lessor accounting (see ED.75–76)

# Lessor–Lease modifications (Agenda Item 10.2.7)

- **Matter for Consideration**

Does the IPSASB support staff's approach to lease modifications for lessor accounting in the draft ED?

## Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- ED 85(a) and IFRS 16.101(a)

- **Two options:**

**Option 1 – Leasebacks at below market terms accounted for in accordance with IFRS 16;**

**Option 2 – Leasebacks at below market terms accounted for as:**

- (i) A normal concessionary lease when there is evidence it has the same economic substance; and
- (ii) In accordance with IFRS 16 when there is evidence that the transaction is not a concessionary lease.

## Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- In Option 2, the entity considers the following indicators:
  - The transaction may be a sale and concessionary leaseback where:
    - A public sector entity has entered into a leaseback transaction with another public sector entity.
    - Entering into a contract with below market terms for the leaseback are approved, by the government or through laws, as a subsidy.
    - Below market terms are accepted for reasons other than to compensation for service.

## Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- In Option 2, the entity considers the following indicators:
  - The transaction may be a sale and leaseback where:
    - A public sector entity has entered into a transaction with a private sector entity.
    - Public sector has entered into a transaction with public sector, but with statements by the government or through laws, that the whole transaction is an exchange transaction.
    - In the contract there is clear evidence that below-market terms are prepayments.



# Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- Arguments in favor of Options 1 and 2

Option 1	Option 2
<ul style="list-style-type: none"> <li>Leaseback at below market terms <b>different transaction</b> from a concessionary lease:               <ul style="list-style-type: none"> <li>(a) The leaseback at below market terms <b>is linked</b> to a sale in the first place</li> <li>(b) Concessionary lease <b>is not linked</b> to a sale in the first place with the same party</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>In the public sector a leaseback below market terms is made with the <b>purpose</b> of giving a subsidy to the lessee</li> </ul>
<ul style="list-style-type: none"> <li><b>There is no public sector specific</b> difference that warrants different accounting from IFRS 16</li> </ul>	<ul style="list-style-type: none"> <li>The <b>high frequency</b> of leases below market terms in the public sector <b>makes the case to</b> account for leasebacks below market terms in the same way as “normal” concessionary leases.</li> </ul>

# Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- **Staff's Views on Option 2**
  - **“Rules of the Road” – Public sector specific?**
    - Are not public sector specific; and
    - Assumption that leasebacks at below market terms and concessionary leases are in substance the same transaction.
  - **IPSAS 40, *Public Sector Combinations***
    - The IPSASB considered transfers between public and private sectors.
    - The IPSASB did not proceed with that rationale, noting that sector classification was a Government Finance Statistics phenomenon that does not have an equivalent in IPSAS.
    - Consequently, it would be difficult to include this in the ED (See IPSAS 40.BC4, BC5 and BC31(a)).

# Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- **Staff's View**

- Different starting points:
  - In substance, different transactions
  - Almost impossible to know whether the price of the sale was influenced by the price of the leaseback

- **Staff's Recommendation**

- **Adopt** the IFRS 16 requirements on leasebacks at below market terms.

# Sale and leaseback transactions at below market terms (Agenda Item 10.2.8)

- **Matter for Consideration**

Does the IPSASB want to adopt:

- (a) Staff's recommendation to apply the IFRS 16 accounting requirements on leasebacks at below market terms (Option 1); or
- (b) The concessionary lease accounting requirements and the IFRS 16 accounting requirements depending on the economic substance of the sale and leaseback at below market terms (Option 2)?

## Lessor–Measurement (Agenda Item 10.2.10)

- Initial Measurement of the Lease Receivable (ED.57-60)
  - Present value of the lease payments that are not received at that date
- Initial Measurement of the Unearned Revenue (ED.61)
  - Initial value of the lease receivable, plus the amount of any lease payments received at or before the commencement date of the lease that relate to future periods (for example, the final month's rent) [not included in the ED]
- Subsequent Measurement of the Lease Receivable (ED.62-71)
  - Mirrors the requirements of lessee accounting to the extent possible
  - Additional guidance for concessionary leases and derecognition and impairment of the lease receivable is provided

# Lessor–Measurement (Agenda Item 10.2.10)

- Subsequent Measurement of the Unearned Revenue (ED.72–73)
  - According to the substance of the lease contract
- Lease Modifications (ED.74–76)
  - Mirrors the requirements for lessee accounting in the draft Exposure Draft, to the extent possible
- Sublease (ED.AG60–AG61)
  - Head lease and the sublease as two separate transactions
  - No offsetting against one another

# Lessor–Measurement (Agenda Item 10.2.10)

- Underlying Asset
  - In accordance with IPSAS 16, IPSAS 17 or IPSAS 31, as appropriate
  - The IPSASB agreed to continue to recognize the underlying asset in its entirety in lessor's accounts.
    - Entities can continue applying the cost model for measurement after recognition that exists in IPSAS 16, 17 and 31
  - The IPSASB did not decide on the consequential amendments to those Standards by using a fair value measurement basis in order to avoid double-counting

## Lessor–Measurement (Agenda Item 10.2.10)

- Staff will also bring the issue on subsequent measurement of the underlying asset to the September 2017 meeting because:
  - Subsequent measurement of the underlying asset is within the scope of other IPSASs;
  - IFRS 16 introduced extensive consequential amendments to other IFRSs, including IAS 16 and IAS 40, (from which IPSAS 16 and IPSAS 17 are, respectively, primarily drawn) that needs to be assessed for public sector financial reporting; and
  - The IPSASB is proposing in the ED different lessor accounting requirements from IFRS 16 that needs to be assessed its impact in other IPSASs together with the IFRS 16 amendments.



# Lessor–Measurement (Agenda Item 10.2.10)

- **Matter for Consideration**

Does the IPSASB agree with the requirements in:

- Initial measurement of the lease receivable (ED.57–60)?
- Initial measurement of the unearned revenue (ED.61)?
- Subsequent measurement of the lease receivable (ED.62–71)?
- Subsequent measurement of the unearned revenue (ED.72–73)?
- Lease modifications (ED.74–76)?
- Underlying asset (ED.77)?
- Sublease (ED.AG60–AG61)?

# Lessor–Credit entry (Agenda Item 10.2.9)

- **March 2017 Meeting**

- The IPSASB agreed with the principle of recognizing revenue over the lease term in the statement of financial performance
- No decision on presentation and labelling in the statement of financial position
- Directed staff to assess relationship with the IPSASB's Revenue and Non-Exchange projects

## **Lessor–Credit entry (Agenda Item 10.2.9)**

- **Three possible ways according to the Conceptual Framework:**
  - a) Liability;
  - b) Revenue; and
  - c) Other obligation.

## Lessor—Credit entry (Agenda Item 10.2.9)

- **Liability:**

“A present obligation of the entity for an outflow of resources that results from a past event.”

- **Revenue:**

“Increases in the net financial position of the entity, other than arising from ownership contributions”.

- **Other obligation:**

“Obligation that does not satisfy the definition of an element defined in the Conceptual Framework.”

- **Net financial position:**

“Difference between assets and liabilities after adding other resources and deducting other obligations recognized in the statement of financial position. Net financial position can be a positive or negative residual amount.”

## Lessor—Credit entry (Agenda Item 10.2.9)

### Liability?

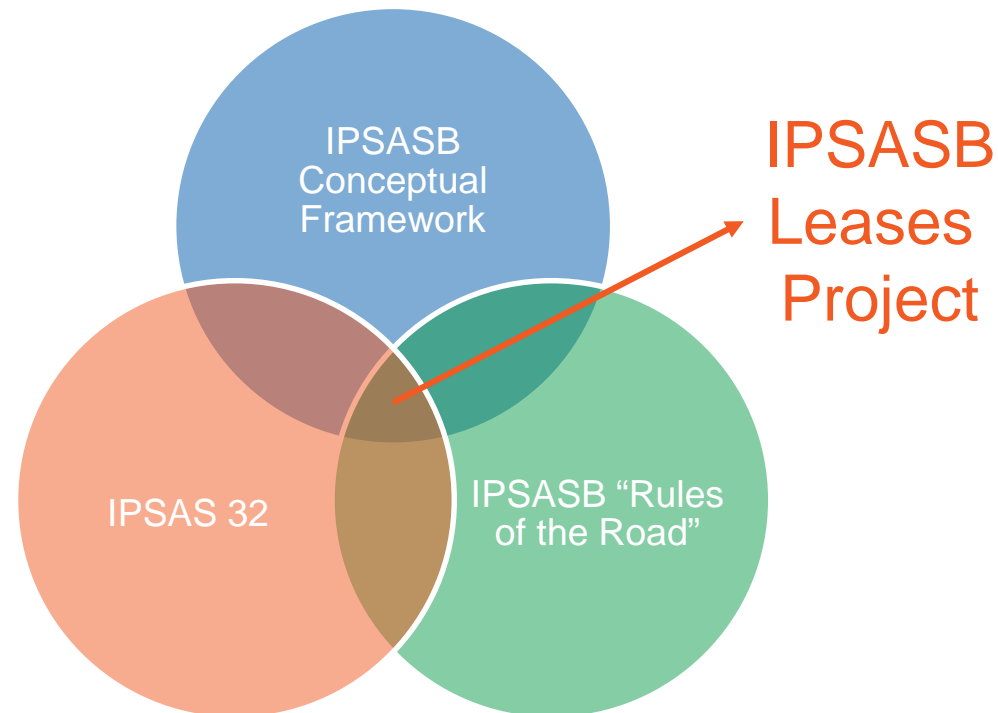
The TBG and staff are of the view that the credit entry **does not meet the definition of a liability** because there is no present obligation of the entity for an outflow of resources.



The credit entry cannot be presented as a liability in the statement of financial position.

# Lessor–Credit entry (Agenda Item 10.2.9)

- Methodology – Boundaries



## Lessor–Credit entry (Agenda Item 10.2.9)

- **Possible conflict between Conceptual Framework and IPSAS 32**

The credit entry is labelled as **liability (unearned revenue)** in IPSAS 32

IPSAS 32 needs to be updated  
to the Conceptual Framework

or

### Option 1

In the Leases project

### Option 2

In a future project to update IPSASs  
for the Conceptual Framework

Amend IPSAS 32 now

Amend IPSAS 32 later

# Lessor–Credit entry (Agenda Item 10.2.9)

## • Possible conflict between Conceptual Framework and IPSAS 32

	Option 1 – Amend IPSAS 32 now	Option 2 – Amend IPSAS 32 later
Advantages	<ul style="list-style-type: none"> <li>• <b>Consistency</b> with Conceptual Framework</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Consistency</b> with previous IPSASB's decisions on IPSAS 39 and IPSASB's project to update IPSAS 28-30</li> <li>• <b>Consistent</b> approach in a project to update IPSASs to the Conceptual Framework or in the Revenue project</li> <li>• <b>Faster</b> development of the Leases project</li> </ul>
Disadvantages	<ul style="list-style-type: none"> <li>• <b>Slower</b> development of the Leases project</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Inconsistency</b> with Conceptual Framework</li> </ul>



## Lessor—Credit entry (Agenda Item 10.2.9)

### Revenue?

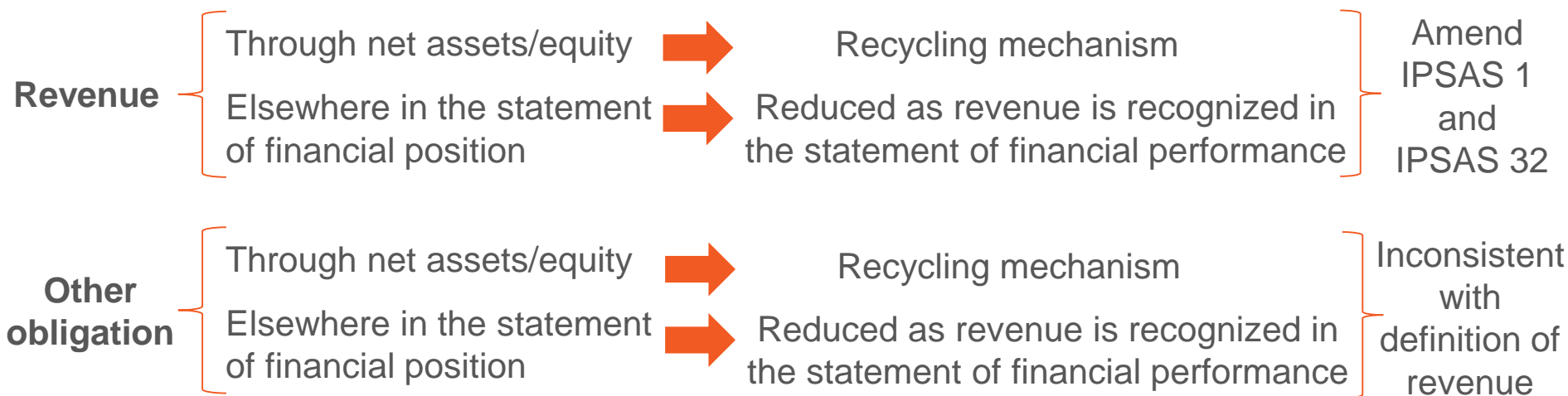
Meets the definition of revenue. However, the Conceptual Framework does not link elements to a particular financial statement.



Revenue may be initially  
recognized in any  
financial statement.

# Lessor–Credit entry (Agenda Item 10.2.9)

## Revenue or Other Obligation?



# Lessor—Credit entry (Agenda Item 10.2.9)

## Revenue?

**Revenue** in the statement  
of financial position



**Inconsistent** with  
IPSASB's decision not to  
include deferred inflows  
and deferred outflows as  
elements in the  
Conceptual Framework



The IPSASB included  
other obligations and other  
resources as possible  
approaches to addressing  
deferrals in the  
Conceptual Framework

# Lessor—Credit entry (Agenda Item 10.2.9)

## Other Obligation?

**Other obligation** in the  
statement of financial  
position



**Inconsistent** with  
definition of revenue



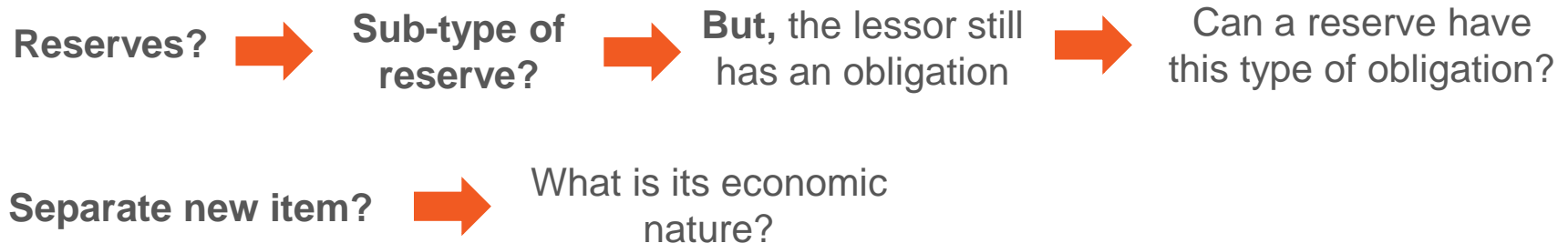
The IPSASB may conclude that, where there is no matching liability, revenue should be recognized in the statement of financial performance. This could justify the treatment of the credit as an other obligation.

# Lessor–Credit entry (Agenda Item 10.2.9)

## Net Assets/Equity?

**Net assets/equity** is the residual interest in the assets of the entity after deducting all its liabilities.

- Contributed capital
- Other reserves
- Translation reserve
- Accumulated surpluses



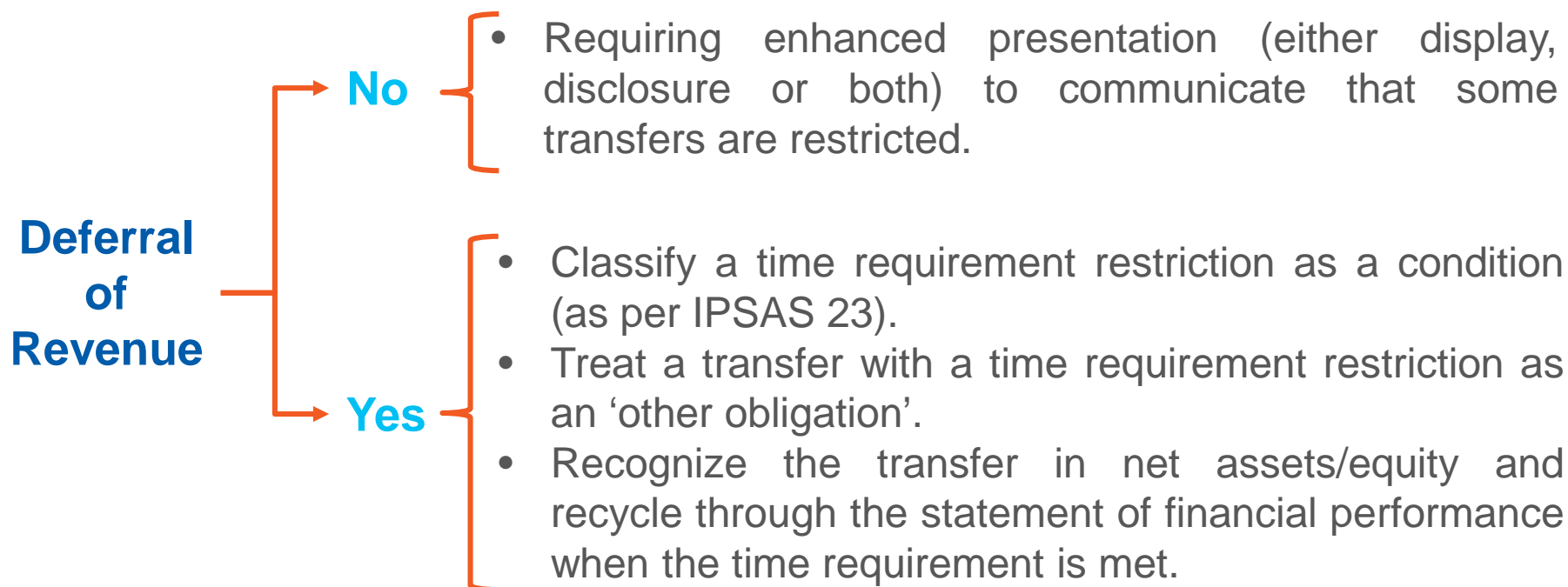
## Lessor–Credit entry (Agenda Item 10.2.9)

- **Relationship with Revenue and Non-exchange Project**
  - Exchange transactions → IFRS 15
  - Non-exchange transactions
    - IPSAS 23 with some amendments, or
    - Extend IFRS 15 to address public sector specific issues
- Recognition of revenue is deferred until the performance obligation is met (which may be at a point of time or over time)

# Lessor–Credit entry (Agenda Item 10.2.9)

- **Relationship with Revenue and Non-exchange Project**

- For transactions that have time requirement restrictions, the Board is proposing **four options** to revise IPSAS 23:



# Lessor–Credit entry (Agenda Item 10.2.9)

- **Matter for Consideration**

Where does the IPSASB want to present the credit entry in the statement of financial position?

- Inside of net assets/equity
- Outside of net assets/equity

What label the IPSASB want to use?

- Revenue
- Unearned revenue
- Lease unearned revenue
- Other obligation



# Exposure Draft Development—Process (Agenda Item 10.3)

- Project to Maintain IASB Convergence
- Public Sector Specific Modifications
- Review of draft Exposure Draft, *Leases*
  - Objective (ED.1–2)
  - Scope (ED.3–4)
  - Definitions (ED.5)
  - Recognition Exemptions (ED.7–9)
  - Identifying a lease (ED.10–18)
  - Lease term (ED.19–22)
  - Lessee (ED.23–51)
  - Lessor (ED.56–77)
  - Sale and leaseback transactions (ED.82–87)
  - Withdrawal and replacement of IPSAS 13 (December 2001) (ED.108)
  - Application guidance (ED.AG1–AG61)
  - Basis for conclusions (ED.BC1–BC42; BC45–BC47; BC51–BC56)

## Meeting between GASB staff and IPSASB staff

- Meeting
  - March 31, 2017
  - Participants:
    - GASB: David Bean, Wesley Galloway, Jialan Su, Ken Schermann
    - IPSASB: João Fonseca
  - Discuss GASB and IPSASB Leases projects
- GASB Leases Project (no equivalent “Rules of the Road”)
  - Research project initiated April 2011
  - Agenda project April 2013
  - Preliminary views issued November 2014
  - Exposure Draft issued January 2016
  - Final Statement expected June 2017

## Meeting between GASB staff and IPSASB staff

- GASB's Exposure Draft (ED), *Leases*
  - Single model for lessors and lessees – **Leases are Financings**
  - Exceptions (lessors and lessees)
    - Short-term leases
    - Leases that transfer ownership and do not contain termination options
  - Exceptions for lessors
    - Leases of assets that are investments
    - Certain regulated leases (e.g., airport-airline agreements)
  - Lessee accounting: Lease asset and lease liability
  - Lessor accounting: Lease receivable and deferred inflow of resources
  - Underlying asset continues to be recognized in its entirety at cost



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