

**Meeting:** International Public Sector Accounting Standards Board

**Meeting Location:** New York, USA

**Meeting Date:** March 10–13, 2020

# Agenda Item 11

For:

Approval

Discussion

Information

## LEASES

<b>Original project summary</b>	Develop revised requirements for lease accounting covering both lessors and lessees in order to maintain alignment with IFRS 16, <i>Leases</i> , to the extent appropriate. The project will result in a new IPSAS that will replace IPSAS 13, <i>Leases</i> .	
<b>Proposed project summary</b>	Develop revised requirements for lease accounting covering both lessors and lessees or retain IPSAS 13, <i>Leases</i> .	
<b>Meeting objectives</b>	<b>Topic</b>	<b>Agenda Item</b>
<b>Project management</b>	<a href="#">Leases: Project Roadmap</a>	<a href="#">11.1.1</a>
	<a href="#">Instructions up to Previous Meeting</a>	<a href="#">11.1.2</a>
	<a href="#">Decisions up to Previous Meeting</a>	<a href="#">11.1.3</a>
<b>Decisions required at this meeting</b>	<a href="#">Project strategy and public interest</a>	<a href="#">11.2.1</a>
	<a href="#">Leases project phasing and management</a>	<a href="#">11.2.2</a>
	<a href="#">Framework of analysis for the options to make a decision on the Leases project</a>	<a href="#">11.2.3</a>
	<a href="#">IFRS 16 variant</a>	<a href="#">11.2.4</a>
	<a href="#">Stop or continue with the Leases project?</a>	<a href="#">11.2.5</a>
	<a href="#">Which option should the IPSASB develop: Option 2–IFRS 16 or Option 3–ED 64?</a>	<a href="#">11.2.6</a>
<b>Other supporting items</b>	<a href="#">Detailed analysis of options for the Leases project</a>	<a href="#">11.3.1</a>

**LEASES:  
PROJECT ROADMAP<sup>1</sup>**

<b>Meeting</b>	<b>Completed Actions or Discussions / Planned Actions or Discussions:</b>
June 2016	1. Approval of Project Brief, <i>Leases</i>
December 2017	1. Approval of Exposure Draft (ED) 64, <i>Leases</i>
September 2018 to September 2019	1. Review of responses to ED 64, <i>Leases</i> 2. Redeliberation of issues
December 2019	1. What is the objective and scope of the Leases project? 2. Framework of analysis of IPSAS 13, <i>Leases</i> , IFRS 16, <i>Leases</i> , and Exposure Draft 64, <i>Leases</i> 3. Concessionary leases 4. Retain or replace IPSAS 13? 5. If replace IPSAS 13, what is the IPSASB emerging view: Option 2 or Option 3?
March 2020	1. Project strategy and public interest 2. Leases project phasing and management 3. Framework of analysis for the options to make a decision on the Leases project 4. IFRS 16 variant 5. Stop or continue with the Leases project? 6. Which option should the IPSASB develop: Option 2–IFRS 16 or Option 3–ED 64?
June 2020 onwards	1. [To be added after decisions at the March 2020 meeting]

<sup>1</sup> This roadmap only contains the main steps, is forward-looking and therefore does not repeat all the actions taken since project commencement in March 2016.

**INSTRUCTIONS UP TO PREVIOUS MEETING**

Meeting	Instruction	Actioned <sup>2</sup>
December 2019	<ol style="list-style-type: none"> <li>1. In relation to the analysis of the three options, the Board instructed staff to: <ul style="list-style-type: none"> <li>• Refine the factors to reflect the IPSASB's discussion</li> <li>• With input from the Task Force, refine the reasoning for the shading for each of the factors.</li> </ul> </li> <li>2. In relation to Option 2 (IFRS16-based) the IPSASB instructed staff to: consider potential variants of the lessor accounting approach in IFRS 16, <i>Leases</i>, that would address concerns expressed by members and stakeholders who had responded to ED 64.</li> <li>3. In relation to concessionary leases the IPSASB instructed staff to consider examples of concessionary leases and access rights, which were to be provided by members and technical advisors and the implications these might have for how to approach this aspect of the project.</li> </ol>	<ol style="list-style-type: none"> <li>1. Agenda Items 11.2.3</li> <li>2. Agenda item 11.2.4</li> <li>3. Agenda Items 11.2.2</li> </ol>

---

<sup>2</sup> The unactioned items will be addressed once the IPSASB chooses the way forward of the Leases project at the March 2020 meeting.

Meeting	Instruction	Actioned <sup>2</sup>
September 2019	<p>The IPSASB instructed the Task Force and staff to:</p> <ol style="list-style-type: none"> <li>1. Reflect on the presentations and discussions of practical issues arising from the implementation of IFRS 16 (both lessor and lessee), review the material in Agenda Items 10.2.1 and 10.3.1, refine it to reflect the discussions at this meeting, and bring recommendations to the December IPSASB meeting.</li> <li>2. Compare the definitions of 'Asset', 'Liability' and 'Control' in the Conceptual Frameworks of IPSASB, IASB, Financial Accounting Standards Board and Governmental Accounting Standards Board.</li> <li>3. Develop a more detailed Basis for Conclusions presenting all the nuances in each issue, including the relationship with GFS.</li> <li>4. Merge criterion 'Consistency with IPSAS 32' with criterion 'Consistency with IPSAS'.</li> <li>5. Analyse practical issues on lessee accounting.</li> <li>6. Include practical issues on lessee accounting in the lessor accounting analysis.</li> <li>7. Assess the benefits of adopting the right-of-use model in the public sector for lessors and lessees.</li> <li>8. Assess in more detail property leases and other types of leases.</li> <li>9. Monitor the activity of the IASB and IFRIC as it relates to IFRS 16. Correspond with counterparts as necessary.</li> <li>10. Assess the principles in ED 70 to lessor accounting (performance obligation satisfied over time or at a point in time?).</li> </ol>	<ol style="list-style-type: none"> <li>1.</li> <li>2.</li> <li>3. The Task Force has completed this step and will bring the detailed Basis for Conclusions at a later date.</li> <li>4.</li> <li>5.</li> <li>6.</li> <li>7.</li> <li>8.</li> <li>9. Next IPSASB/IASB liaison meeting in March 6<sup>th</sup>, 2020.</li> <li>10.</li> </ol>

<b>Meeting</b>	<b>Instruction</b>	<b>Actioned<sup>2</sup></b>
December 2018	The IPSASB <b>instructed</b> staff: <ol style="list-style-type: none"><li>1. To include in the Basis for Conclusions the reasons not to include additional guidance on transfer of control;</li><li>2. To include in the analysis the consequential amendments to other IPSAS; and</li><li>3. To include in the analysis the IASB's deliberations on lessor accounting;</li></ol>	<ol style="list-style-type: none"><li>1.</li><li>2.</li><li>3.</li></ol>

**DECISIONS UP TO PREVIOUS MEETING**

Meeting	Decision	BC Reference
December 2019	1. The IPSASB <b>decided</b> to revisit the objective and scope of the leases project in the context of solving a public sector problem.	
September 2019	1. The IPSASB <b>decided</b> that departure from IFRS 16 is conceptually justified. The practical implications of departure would now be considered.	
June 2019	1. None.	
March 2019	<p>1. To adopt the following criteria in assessing departures from the lessor accounting requirements in IFRS 16, Leases:</p> <ul style="list-style-type: none"> <li>a. Consistency with Conceptual Framework;</li> <li>b. Consistency with IPSAS;</li> <li>c. IFRS Alignment;</li> <li>d. Implementation Issues;</li> <li>e. User needs of financial community;</li> <li>f. Relationship with Government Finance Statistics; and</li> <li>g. Relationship with public-private partnerships</li> </ul> <p>2. To adopt two phases for evaluating approaches to lessor accounting:</p> <ul style="list-style-type: none"> <li>a. Phase 1: <ul style="list-style-type: none"> <li>i. Examine all responses focusing on the reasons submitted for departing, or not departing, from IFRS 16;</li> <li>ii. Subject to conclusions on 1 (above), evaluate implications and make recommendations to the IPSASB in June 2019;</li> <li>iii. IPSASB to consider/redeliberate the approach in June 2019;</li> <li>iv. Outcome of c. will determine next steps after the June 2019 meeting, including instructions to the Task Force; and</li> <li>v. Accounting for concessionary leases is only to be addressed once step d. has been completed.</li> </ul> </li> <li>b. Phase 2 will depend on the discussions at the June 2019 meeting.</li> </ul>	

Meeting	Decision	BC Reference
December 2018	<ol style="list-style-type: none"> <li>1. To confirm the provisional decision made in September to adopt the lessee accounting requirements in ED 64, subject to decisions on the approach to be taken to lessor accounting, and where relevant, concessionary leases;</li> <li>2. Not to publish lessee accounting requirements based on ED 64 ahead of the decisions on lessor accounting, and where relevant, concessionary leases;</li> <li>3. To create a Task Force to consider all the issues raised by respondents;</li> <li>4. Not to adopt the "bundle of rights" approach to lessee accounting;</li> <li>5. Not to adopt exemption for leases between public sector entities;</li> <li>6. Not to provide additional guidance on transfer of assets;</li> <li>7. To create a Task Force for the Leases project to be established at March 2019 meeting;</li> <li>8. Review all IPSASB's decisions in light of respondents' views;</li> <li>9. Only take a final decision on lessee accounting, lessor accounting and concessionary leases after all issues have been discussed;</li> </ol>	
September 2018	<ol style="list-style-type: none"> <li>1. To provisionally adopt the proposals in ED 64, Leases, on lessee accounting in the draft IPSAS, Leases, subject to a more detailed analysis of the responses;</li> <li>2. To extend the timeline of the Leases project in order to carry out a detailed analysis of all the issues raised by respondents; and</li> <li>3. To get CAG's views on the Leases project at the December 2018 meeting.</li> </ol>	

## **Project Strategy and Public Interest**

### **Question**

1. The IPSASB is asked to agree the strategic direction to take the Leases project forward.

### **Detail**

2. The IPSASB added Leases to the Work Plan in 2015, as a project to maintain convergence with IFRS 16, *Leases*. The project brief approved in June 2016 noted: *“the objective was to issue a revised IPSAS 13 (or new IPSAS) on lease accounting which would be converged with the new IFRS.”*
3. As the project developed, the IPSASB decided to develop a public sector specific approach in ED 64, *Leases*, to address the following issues:
  - (a) **Lessor accounting.** ED 64 proposed a single right-of-use model for lessees and lessors. IFRS 16, requires a right of use model for lessees, and a risk and rewards model for lessors.
  - (b) **Concessionary Leases.** ED 64 proposed guidance for concessionary leases because of the prevalence in the public sector of leases at below market terms. IFRS 16 does not include guidance for leases at below market terms.
4. Respondents were divided on the ED 64 proposed approaches for public sector specific issues. In particular there were:
  - (a) Strong views that IPSASB should develop an aligned standard with IFRS 16; and
  - (b) Equally strong views that public sector specific proposals in ED 64 should be taken forward.
5. Despite this support, concerns were noted with the ED 64 approaches to lessor accounting and concessionary leases. However, there was a lack of consensual views provided on how those could be addressed.
6. In March 2019, the IPSASB decided to extend the project timeline to better understand respondent views on both IFRS 16 and ED 64. The IPSASB therefore explored issues by:
  - (a) Forming a Leases Task Force that met during the year, including an intensive in-person meeting in July 2019, the primary focus of which was to address departure or not from IFRS 16 for lessor accounting; and
  - (b) Inviting stakeholders to share their differing perspectives on lease accounting with the IPSASB, including those representing national standard setters, preparers, auditors and the GFS community.
6. Staff notes these efforts were helpful to better understand the issues on both sides related to lease accounting. However, this work has highlighted to staff that constituents are divided on the issue of lease accounting, and it is unlikely that a consensual approach is feasible on lessor accounting and concessionary leases for both lessors and lessees.
7. The staff recommendation is that, rather than undertaking further research, the IPSASB needs to make a strategic decision now on the future direction of the Leases project. From a public interest perspective, an approach and timeline need to be identified, so that the Board and staff resources can be effectively deployed in delivering a solution on leases, and to avoid taking up further Board and staff time on further research that is unlikely to identify any further viable approaches that neither

the IPSASB or IASB haven't already considered. Further delays in setting a course for the project brings reputational risks to the IPSASB.

**Decision required**

8. Does the IPSASB agree with the staff's recommendation that a decision on the direction of the Leases project is needed now?

## **Leases Project Phasing and Management**

### **Question**

1. The IPSASB is asked to agree with the staff recommended phased approach to addressing the issues in the Leases project.

### **Detail**

2. Concessionary leases is an important public sector specific issue that the IPSASB decided to address in the Leases project.
3. Responses to ED 64 confirmed the importance of the issue in the public sector but raised several challenges with the proposals to address it. Subsequent stakeholder discussions have raised questions about whether some 'concessionary leases' are really leases at all, and whether alternative approaches such as treatment as 'access rights' should be explored.
4. The December 2019 Leases agenda papers proposed delaying work on concessionary leases to allow the IPSASB and staff to focus on the lease accounting model. The IPSASB December 2019 debate confirmed the importance of the issue and that requirements for concessionary leases need to be developed.
5. Determining appropriate requirements for concessionary lease accounting is however dependent on the accounting model for both lessors and lessees.
6. Staff recommends that regardless of which accounting option the Board agrees to develop, a phased project management approach is undertaken. This approach would prioritize developing the accounting model(s) for lessors and lessees in phase 1. Phase 2 would follow and focus on developing concessionary lease requirements based on the model(s) developed.
7. In order to demonstrate to stakeholders that the Board remains committed to taking forward work on concessionary leases forward and to provide a firm foundation for this by gathering further information on the sort of issues outlined in paragraph 3, it proposed to issue a 'request for information', potentially alongside a further ED.

### **Decision required**

8. Does the IPSASB agree with the staff's recommendation to adopt a phased project management approach?

## **Framework of analysis for the options to make a decision on the Leases project**

### **Question**

1. Whether the IPSASB agrees with the framework of analysis for the options to make a decision on the Leases project.

### **Detail**

#### *Background*

2. At the December 2019 meeting, the IPSASB discussed the following factors to analyze the options to move the Leases project forward:
  - (a) Public financial management (PFM) benefits;
  - (b) Implementation costs/challenges;
  - (c) Government Finance Statistics (GFS) alignment impact;
  - (d) IPSASB Conceptual Framework;
  - (e) IFRS alignment; and
  - (f) Feasibility of Leases project.
3. The IPSASB agreed with the factors and instructed:
  - (a) Staff to refine the factors to reflect the IPSASB's discussion; and
  - (b) The Task Force to review and refine the reasoning behind the shading for each factor<sup>1</sup>.
4. Staff and the Task Force Chair refined the Factor descriptions as instructed (see [Appendix A](#)).
5. The IPSASB also requested that further consideration be given to adding additional factors, if needed. Staff and the Task Force Chair considered the completeness of the refined factors (and reasoning behind them) to determine if any additional items should be added. The view of staff and Task Force Chair is that the refined factors are sufficient, and no further items should be added.

#### *Recommended framework of analysis*

6. Attached to this agenda item is [Appendix A](#) providing a detailed description of the revised six factors to analyze the options to make a decision on how to move Leases forward.
7. As a result of the assessment of the options, a traffic light with the following meaning is attributed to each factor:
  - (a) Red – Stop / no / significant issues noted
  - (b) Green – Go / ok / no issues noted
  - (c) Amber – Not sure / proceed with caution / minor issues noted

---

<sup>1</sup> Following the December 2019 meeting Staff, the Board Chair and the TF Chair agreed this work should be done by Staff who should manage this project until a decision on project scope/objective is made by the IPSASB.

8. The traffic lights will be used to analyze the options.
9. Staff updated the traffic light colors based on the refined factors.
10. Staff recommends that the IPSASB uses the revised framework to analyze the options to make a decision on the Leases project.

**Decision required**

11. Does the IPSASB agree with the staff's recommended revised framework of analysis for the options to make a decision on the Leases project?

**Appendix A – Detailed description of factors**

<b>Factors</b>	<b>Detailed description</b>
<b>PFM benefits</b>	<p>“Public Financial Management is the system by which financial resources are planned, directed and controlled to enable and influence the efficient and effective achievement of public service outcomes.” Refer <a href="#">CIPFA ‘Whole System Approach’</a></p> <p>This definition is aligned with the <a href="#">IFAC/CIPFA International Framework: Good Governance in the Public Sector</a>.</p> <p>At the core of the model is accrual-based information in order to deliver excellent public finance management.</p>
<b>Implementation costs / challenges</b>	<p>Training, IT changes, change of processes, accounting changes (first-time adoption)                      on-going accounting (maintenance)</p>
<b>GFS alignment impact</b>	<ul style="list-style-type: none"> <li>• At conceptual level, when comparing IPSAS and GFS accounting frameworks</li> <li>• At practical level, when compiling GFS accounts using accrual based IPSAS accounts</li> </ul>
<b>IPSASB Conceptual Framework</b>	<ul style="list-style-type: none"> <li>• Objectives public sector financial reporting: accountability and decision-making</li> <li>• Recognition</li> </ul>
<b>IFRS alignment</b>	<p>Alignment with IFRS 16, <i>Leases</i></p>
<b>Feasibility of Leases project</b>	<ul style="list-style-type: none"> <li>• Straightforwardness</li> <li>• Timeliness</li> <li>• Impact on project management, IPSASB’s resource allocation, and IPSASB’s Work Program</li> </ul>

## **IFRS 16 variant**

### **Question**

1. Whether the IPSASB agrees with staff's recommendation on the IFRS 16 variant.

### **Detail**

#### *Background*

2. At the December 2019 meeting, the IPSASB instructed staff to consider potential variants of the lessor accounting approach in IFRS 16, *Leases*, that may address concerns expressed by members and stakeholders on ED 64.
3. The IFRS 16 variant proposed would require all lessors to account for leases as operating leases only.
4. The IFRS 16 variant would ensure that the underlying asset is always recognized by the lessor, thus addressing the practical issues with IPSAS 13, *Leases*<sup>1</sup> of:
  - (a) Recognition of the underlying asset by both the lessor and lessee (when the lessor classifies the lease as an operating lease, and the lessee classifies the lease as a finance lease); and
  - (b) Non-recognition of the underlying asset by either the lessor or the lessee (when the lessor classifies the lease as a finance lease, and the lessee classifies the lease as an operating lease).
5. The aim of the variant is also to deal with an issue arising from IFRS 16, *Leases*, which is the non-recognition of the underlying asset by either the lessor or the lessee if the lessor classifies the lease as a finance lease<sup>2</sup>.

#### *IFRS 16 variant issues*

6. Staff has identified several significant issues with the IFRS 16 variant, as follows:
  - (a) Conceptual issues:
    - (i) Lack of economic rationale—Requiring operating lease accounting for all lessor transactions removes judgement by preparers because the approach is rules-based, without sufficient economic rationale. This change might be perceived as exacerbating the conceptual flaw with IFRS 16, rather than diminishing it, as it means there is no principle supporting the approach.
    - (ii) Inconsistent approach to the same transaction—The lessee is required to recognize a lease liability at the commencement of the lease, but the lessor is not required to

---

<sup>1</sup> These issues also arose under IAS 17, *Leases*.

<sup>2</sup> A problem that only occurred in practice applying IPSAS 13, *Leases*, is also a problem with IFRS 16, *Leases* at a more theoretical level. While under IPSAS 13 the underlying asset could not be recognized by both the lessor and the lessee because different parties were making different judgment calls when applying the same accounting model, under IFRS 16 the underlying asset is not recognized by both the lessor and the lessee because both parties are applying different accounting models, not because of different application of the same accounting model.

recognize a lease receivable at the commencement of the lease, for the purchase/sale of the right-of-use asset<sup>3</sup>. Some may view this accounting as flawed because the lessor's statement of financial position does not portray a faithful representation of all the rights that arise from leases.

- (iii) A lease is not a service—Accounting by the lessor in this way treats the lease as a service contract. However, leases and service contracts are different because in a lease the right-of-use of the underlying asset is controlled by the lessee ('customer') and in a service it is controlled by the supplier ('lessor').
- (b) Practical issues:
- (i) Creates consolidation issues where both lessor and lessee are part of the same controlling entity applying IPSAS;
  - (ii) Creates mixed group issues where some government business enterprises (state owned enterprises) apply IFRS but are controlled by public sector entities; and
  - (iii) Because of the inconsistent approach to head leases described in paragraph 6(a)(ii), the IFRS 16 variant leads to an inappropriate accounting treatment also for sub-leases, because the intermediate lessor is not required to recognize a lease receivable but is required to recognize a lease liability as the lessee in the head lease, even when the sublease has the same rights and obligations as the head lease. For example, an intermediate centralized public sector lessor that is a lessee in a head lease with a private sector entity, and subsequently subleases those assets to other public sector entities will have all the lease liabilities from the head lease, but no lease receivables from the subleases, while both types of leases may have the same rights and obligations.<sup>4</sup>
7. Staff further questions the IFRS 16 variant because:
- (a) No respondent to ED 64 proposed such a model for lessor accounting;
  - (b) No such model has been considered or developed previously by an international or national standard setter<sup>5</sup>; and
  - (c) Might raise IPSASB credibility issues by pursuing an accounting model that removes judgement, by eliminating any assessment of risks and rewards as it is implicit in the model.

*Staff's recommendation*

8. Staff does not recommend the IPSASB consider the IFRS 16 variant.

---

<sup>3</sup> Just like in a purchase/sale of a good that is paid for over time it is expected that the purchaser recognizes a liability and the seller recognizes the receivable, in a lease it is also expected that the lessee (purchaser) recognizes a lease liability and the lessor (seller) recognizes a lease asset for the purchase/sale of the right-of-use asset that is paid over time.

<sup>4</sup> This problem with subleases highlights more clearly why the IFRS 16 variant is flawed at the head lease level in the first place.

<sup>5</sup> The International Accounting Standards Board (IASB), the United States Governmental Accounting Standards Board (GASB) and the United States Federal Accounting Standards Advisory Board (FASAB)<sup>5</sup> never proposed such a model in their consultation documents nor does it exist in their Standards on Leases.

**Decision**

9. Does the IPSASB agree with staff's recommendation not to consider IFRS 16 variant?

## **Continue with the Leases project?**

### **Question**

1. Whether the IPSASB wants to continue with the Leases project

### **Detail**

#### *Background*

2. At the December 2019 meeting, the IPSASB agenda papers noted retention of IPSAS 13 as one of three options to move the leases project forward (Option 1). Retaining IPSAS 13 would essentially stop the Leases project.

#### *Problems with IPSAS 13*

3. There are four main problems with IPSAS 13:
  - (a) The underlying asset might:
    - (i) Not be recognized by both the lessor and the lessee (when the lessor classifies the lease as a finance lease and the lessee classifies the lease as an operating lease); and
    - (ii) Be recognized by both the lessor and the lessee (when the lessor classifies the lease as an operating lease and the lessee classifies the lease as a finance lease<sup>1</sup>);
  - (b) Lessor does not recognize a lease receivable and the lessee recognizes a lease liability arising from the same lease contract or vice-versa (when the lessor classifies the lease as an operating lease and the lessee classifies the lease as a finance lease or vice-versa)<sup>2</sup>; and
  - (c) The lessee might not recognize a lease liability if the lessee classifies the lease as an operating lease<sup>3</sup>.

#### *Continue with the Leases project?*

4. The table below summarizes the results of the analysis by applying the framework referred to in [Agenda Item 11.2.2](#).
5. [Agenda Item 11.3.1](#) provides the detailed information supporting the traffic light colors<sup>4</sup>.
6. [Appendix A](#) to this Agenda Item presents the main accounting features of all three options.

---

<sup>1</sup> In other words, just like in a sale/purchase it is not expected that both parties recognize the same good or no one recognizes it. In a lease it is not expected that the underlying asset to be derecognized from the financial statements of the lessor because the lessor has only transferred the right to use an underlying asset, not the underlying asset itself.

<sup>2</sup> Just like in a purchase/sale of a good that is paid for over time it is expected that the purchaser recognizes a liability and the seller recognizes the receivable, in a lease it is also expected that the lessee (purchaser) recognizes a lease liability and the lessor (seller) recognizes a lease receivable for the purchase/sale of the right-of-use asset that is paid for over time.

<sup>3</sup> Staff notes that the main objective of the IASB Leases project was to address the off-balance sheet financing that operating leases for lessees allowed.

<sup>4</sup> Including the problems and solutions identified with each option, as suggested by the IPSASB at the December 2019 meeting.

Factors \ Options	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13 (risks and rewards model for lessee and lessor)		Option 2 – IFRS 16 (right-of-use model for lessee and risks and rewards model for lessor)		Option 3 – ED 64 (right-of-use model for both lessee and lessor)	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>PFM benefits</b>						
<b>Implementation costs / challenges</b>						
<b>GFS alignment impact</b>						
<b>IPSASB Conceptual Framework</b>						
<b>IFRS alignment</b>						
<b>Feasibility of Leases project</b>						

7. Retaining IPSAS 13 would mean that there would be no change to the IPSASB literature. Therefore, the issues identified in paragraph 3 will persist.
8. The staff’s view based on the analysis, as shown in the table, is that retaining IPSAS 13 is the least favorable option in terms of PFM benefits, consistency with the Conceptual Framework and IFRS Alignment because it:
  - (a) Continues to allow off-balance sheet financing of operating leases for lessees;
  - (b) May result in the underlying asset not being recognized by either lessee or lessor, or being recognized by both;
  - (c) Is inconsistent with the control-based approach to asset recognition/derecognition in the Conceptual Framework; and
  - (d) Continues with accounting requirements that differ from those in IFRS 16 for both lessees and, to a smaller extent, lessors.
9. On the other hand, retaining IPSAS 13 is the best option in terms of “GFS Alignment”<sup>5</sup>, “Implementation costs/challenges” and “Feasibility of Leases project” (as the standard exists and has been in place since January 1, 2008).
10. In addition to the problems mentioned in paragraph 3 above, there are other issues in pursuing Option 1 including, but not limited to:
  - (a) Mixed group issues where some publicly owned controlled entities are required to comply with IFRS; and
  - (b) Public interest issues with the potential impact on IPSASB’s credibility by frustrating constituents’ expectations that the IPSASB has committed to a replacement of IPSAS 13.

<sup>5</sup> However, as noted in Agenda Item 11.3.1 GFS does not use the data directly from the financial statements.

*Staff's recommendation*

11. Staff recommends the IPSASB to continue with the Leases project and develop a replacement for IPSAS 13 because:
- (a) Of the reasons identified in paragraphs 8 and 10;
  - (b) While acknowledging the informal nature of the decision, no IPSASB member supported retention of IPSAS 13 at the December 2019 meeting; and
  - (c) It is in the public interest (for reasons of transparency, accountability and decision making) to address:
    - (i) Lessee's off-balance sheet financing through leases;
    - (ii) The different accounting outcomes resulting from independent lease classifications by each entity to the same lease contract which leads to:
      - a. Possible disappearance (lack of recognition of the underlying asset by either entity to the lease contract), or recognition in duplicate (same asset recognized by two entities), of the underlying asset in the financial statements; and
      - b. Possible non-recognition (lack of recognition) of the lease receivable by the lessor while the lessee possibly recognizes a lease liability<sup>6</sup>.

**Decision required**

12. Does the IPSASB agree with staff's recommendation to continue with the Leases project?

---

<sup>6</sup> While staff is not proposing symmetrical accounting, it is a common understanding that, for a lease transaction between two public sector entities in the same jurisdiction, the rights and obligations are clear and that the transaction is accounted for in a similar way by both parties, just like in a purchase/sale of goods that is not paid upfront.

**Appendix A – Main accounting features of options to move the leases project forward**

	No change/Stop the Leases project	Change/Continue with the Leases project	
		Partial change	Full change
	Option 1 – IPSAS 13	Option 2 – IFRS 16	Option 3 – ED 64
<b>I – Lease contract</b>			
<b>Model</b>	<b>Lessee</b>		
	Dual model based on risks and rewards	Single right-of-use model	
	<b>Lessor</b>		
	Dual model based on risks and rewards	Single right-of-use model	
<b>Recognition</b>	<b>Lessee</b>		
	<ul style="list-style-type: none"> <li>• Debit: Right-of-use asset</li> <li>• Credit: Lease liability</li> </ul>		
	<b>Lessor</b>		
	<ul style="list-style-type: none"> <li>• <b>Finance lease:</b> <ul style="list-style-type: none"> <li>○ Debit: lease receivable</li> <li>○ Credit: underlying asset</li> </ul> </li> <li>• <b>Operating lease:</b> <ul style="list-style-type: none"> <li>○ revenue on a straight-line basis</li> </ul> </li> </ul>	Same as IPSAS 13 plus changes related to subleases, disclosures, lease modifications, initial direct costs and variable lease payments.	<ul style="list-style-type: none"> <li>• Debit: Lease receivable</li> <li>• Credit: Lease liability (unearned revenue)</li> </ul>
<b>II – Underlying asset</b>			
<b>Recognition and measurement</b>	<b>Lessor</b>		
	<b>Finance lease:</b> derecognized <b>Operating lease:</b> continues to be recognized and measured according to the applicable Standards*	Continues to be recognized and measured according to the applicable Standards*.	
<b>Additional guidance</b>	–		Detailed guidance to distinguish a lease from a sale of the underlying asset to be applicable to both lessors and lessees.

**\* Note:** Under the cost model of IPSAS 17, *Property, Plant, and Equipment* in operating leases of IPSAS 13 and IFRS 16, and in ED 64, the lessor applies IPSAS 21, *Impairment of Non-Cash Generating Assets* and IPSAS 26, *Impairment of Cash-Generating Assets* to determine whether an underlying asset is impaired and to account for any impairment identified.

Double-counting might occur in these options if the lessor uses the same cash-flows from the lease that are already recognized as assets or liabilities to measure the recoverable amount under IPSAS 26.

However, according to IPSAS 26.56, “to avoid double-counting, estimates of future cash flows do not include:

- (a) Cash inflows from assets that generate cash inflows that are largely independent of the cash inflows from the asset under review (for example, financial assets such as receivables); and

(b) Cash outflows that relate to obligations that have been recognized as liabilities (for example, payables, pensions, or provisions).”

\* **Note (cont.):** Double-counting might also occur under the fair value model of IPSAS 16, *Investment Property* in operating leases of IPSAS 13 and IFRS 16, and ED 64 in lessor accounting.

Therefore, in order to prevent double-counting, according to IPSAS 16.59 the lessor “in determining the carrying amount of investment property [...], an entity does not double-count assets or liabilities that are recognized as separate assets or liabilities. For example:

[...]

(d) The fair value of investment property excludes prepaid or accrued operating<sup>7</sup> lease revenue, because the entity recognizes it as a separate liability or asset.

[...]”

In ED 64, as the lessor can sell or securitize the recognized lease receivable like any other financial instrument, thus transforming the lease receivable into cash, it has the same practical accounting consequence for the lease liability (unearned revenue) as if the lessor had received upfront full payment of the lease for the entire lease term directly from the lessee under IPSAS 13 and IFRS 16: in all cases the lessor recognizes a liability (unearned revenue) and unwinds this liability over time during the lease term.

## **Which option should the IPSASB develop: Option 2–IFRS 16 or Option 3–ED 64?**

### **Question**

1. Which option should the IPSASB develop: Option 2—IFRS 16 or Option 3—ED 64<sup>1</sup>?

---

<sup>7</sup> ED 64 proposes to remove the wording “operating” as consequential amendment to IPSAS 16 because this term does not exist in ED 64.

<sup>1</sup> This agenda paper is drafted on the assumption that the IPSASB supports Staff recommendation in 11.2.5 that Option 1—Stop the Leases project is not be pursued.

## Detail

2. The IPSASB should decide whether to proceed with the right-of-use model for:
  - (a) Lessees only – by proceeding to develop an aligned standard with IFRS 16 (Option 2); or
  - (b) Both lessees and lessors – by proceeding with ED 64 (Option 3).
3. Staff notes that the if IPSASB choses Option 3, then it would be deciding to proceed to change the existing approach for lessor accounting to one based on the core principles for lessor accounting as proposed by ED 64:
  - (a) The underlying asset continues to be recognized by the lessor; and
  - (b) A lease receivable and a lease liability (unearned revenue) is recognized at the commencement of the lease.
4. However, both Options 2 and 3 will need to be modified in order to make the final Standard fit for public sector financial reporting, while retaining their core principles.
5. If the IPSASB selects Option 2, then it will apply the [“Process for Reviewing and Modifying Documents”](#) (also known as “Rules of the Road”), as for any other IFRS alignment project.
6. If Option 3 is selected, then the IPSASB will consider how to respond to potential flaws in ED 64 identified by respondents without losing the two core principles identified in paragraph 3.

## Results of the Analysis

7. The table below summarizes the results of the analysis by applying the factors referred to in [Agenda Item 11.2.2](#).

Factors \ Options	Option 2 – IFRS 16 (right-of-use model for lessee and risks and rewards model for lessor)		Option 3 – ED 64 (right-of-use model for both lessee and lessor)	
	Partial change		Full change	
	Lessee	Lessor	Lessee	Lessor
<b>PFM benefits</b>				
<b>Implementation costs / challenges</b>				
<b>GFS alignment impact</b>				
<b>IPSASB Conceptual Framework</b>				
<b>IFRS alignment</b>				
<b>Feasibility of Leases project</b>				

10. [Agenda Item 11.3.1](#) provides the detailed information supporting the traffic light colors for each option.
11. The main conclusion from the table is that there is no optimal solution. Both options have advantages and disadvantages and have different overall results when taking all the factors together.

## Staff's views

12. The key difference between Options 2 and 3 relate to the lessor accounting model. Therefore, the paragraphs below focus on lessor accounting, except where otherwise stated.

13. As both options have amber traffic lights for PFM benefits (although for different reasons), this factor does not provide a clear indication on which option is preferable.
14. Regarding the factor Implementation costs/challenges, Option 3 entails greater implementation costs/challenges than Option 2 because IFRS 16 carried forward the model that existed in IAS 17, *Leases* with only some minor changes.
15. From the GFS Alignment perspective, the Option 2 accounting model is aligned for lessors, but not for lessees. While the Option 3 accounting model is not aligned for either lessors or lessees. The statistical community notes that Option 2 requires more effort from a GFS perspective, as they would have to use surveys to obtain data on the underlying asset in a lease (when the lessor has a finance lease). However, Option 2 is currently being applied in the private sector and any additional statistical information or processes needed to collect information should be available if the IPSASB chooses this option.
16. Option 2 is aligned with IFRS, but it is less consistent with the IPSASB Conceptual Framework. However, it has the advantage that is more straightforward and predictable than Option 3 from a project management perspective.
17. Option 3 is more consistent with the IPSASB Conceptual Framework, but it is not aligned with IFRS. However, this option will be more challenging from a project management perspective because of the variability in views on ED 64 lessor accounting proposals, which make the timeline unpredictable.

*Staff's recommendation*

18. Staff recommends the IPSASB Option 2 – IFRS 16 because:
  - (a) It is less costly/challenging to implement;
  - (b) It is aligned with the IPSASB's Strategy & Work Plan strategic theme of Maintaining IFRS Alignment, which was the original objective of the Leases project; and
  - (c) It is the most feasible option because it allows greater certainty on the timeline and outcome for a new IPSAS on Leases. This is important from a public interest perspective because the IPSASB has a challenging work program and an extended timeline for leases negatively impacts the progress on other projects.

**Decision required**

19. Which option does the IPSASB want to develop?
  - (a) Option 2 – IFRS 16, *Leases*; or
  - (b) Option 3 – ED 64, *Leases*.

**DETAILED ANALYSIS OF OPTIONS FOR THE LEASES PROJECT**

	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13		Option 2 – IFRS 16		Option 3 – ED 64	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>Problems / Solutions</b>						
<b>Underlying asset</b>	<b>Problem:</b> <ul style="list-style-type: none"> <li>Underlying asset might not be recognized by both the lessor and the lessee if the lessor classifies the lease as a finance lease and the lessee classifies the lease as an operating lease.</li> <li>Underlying asset might be recognized by both the lessor and the lessee if the lessor classifies the lease as an operating lease and the lessee classifies the lease as a finance lease.</li> </ul>		<b>Solution:</b> The lessee always recognizes a right-of-use asset, not the underlying asset itself.	<b>Problem:</b> Underlying asset is not recognized by both the lessor and the lessee if the lessor classifies the lease as a finance lease.	<b>Solution:</b> The lessee always recognizes a right-of-use asset, not the underlying asset itself.	<b>Solution:</b> The lessor continues to recognize and measure the underlying asset according to the applicable Standards.
<b>Lease receivable</b>	<b>Problem:</b> Lease receivable might not be recognized by the lessor if the lessor classifies the lease as an operating lease, but the lessee might recognize a lease liability if the lessee classifies the lease as a finance lease.		N/A	<b>Problem:</b> Lease receivable is not recognized if the lessor classifies the lease as an operating lease, but the lessee always recognizes a lease liability.	N/A	<b>Solution:</b> The lessor always recognizes a lease receivable.
<b>Lease liability</b>	<b>Problem:</b> Lease liability might not be recognized if the lessee classifies the lease as an operating lease <sup>17</sup> .	N/A	<b>Solution:</b> The lessee always recognizes a lease liability.	N/A	<b>Solution:</b> The lessee always recognizes a lease liability.	N/A

<sup>17</sup> Staff notes that the main objective of the IASB Leases project was to address the off-balance sheet financing that operating leases for lessees allowed.

	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13		Option 2 – IFRS 16		Option 3 – ED 64	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>Factors</b>						
<b>PFM benefits</b>	<ul style="list-style-type: none"> <li>• <b>Operating lease:</b> Failing to recognize an obligation that meets the definition of a liability and can be measured in a faithfully representative way fails to provide information that is necessary for decision making and accountability purposes and therefore is not conducive to sound PFM. The non-recognition of the lease liability.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Finance lease and operating lease:</b> The non-recognition of the underlying asset a finance lease and the lease receivable in an operating lease impairs efficient and effective achievement of public service outcomes because that accrual information is not connected into other parts of the system concerned with monitoring and reporting that strong PFM requires.</li> </ul>	<ul style="list-style-type: none"> <li>• Provides better information for efficient and effective achievement of public service outcomes because by recognizing the lease liability it connected into other parts of the system concerned with monitoring and reporting that strong PFM requires.</li> <li>• Prevents arbitrage, gaming and information asymmetry.</li> </ul>	<ul style="list-style-type: none"> <li>• Failing to recognize the underlying asset in finance lease and the lease receivable in operating lease that meet the definition of an asset and can be measured in a faithfully representative way fails to provide information that is necessary for decision making and accountability purposes and therefore is not conducive to sound PFM.</li> <li>• However, as some respondents to ED 64 supported IFRS 16, they identify other PFM benefits.</li> </ul>	<ul style="list-style-type: none"> <li>• Provides better information for efficient and effective achievement of public service outcomes because by recognizing the lease liability it connected into other parts of the system concerned with monitoring and reporting that strong PFM requires.</li> <li>• Prevents arbitrage, gaming and information asymmetry.</li> </ul>	<ul style="list-style-type: none"> <li>• Provides financial information on both the underlying asset and the lease receivable for efficient and effective achievement of public service outcomes because that accrual information is connected into other parts of the system concerned with monitoring and reporting that strong PFM requires.</li> <li>• However, as there is no consensus from respondents to ED 64 on lessor accounting, it is not clear that ED 64 model provides the most universal benefits to PFM.</li> </ul>

	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13		Option 2 – IFRS 16		Option 3 – ED 64	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>Implementation costs / challenges</b>	Based on the assumption that IPSAS 13 is already implemented there are no implementation costs/challenges.		There will be potentially significant implementation costs/challenges in recognizing and measuring the right-of-use asset and the lease liability.	Although IFRS 16 includes the risks and rewards model, there are changes compared to the IPSAS 13 model related to subleases, disclosures, lease modifications, initial direct costs and variable lease payments. So, there will be implementation costs / challenges. However, these should be less than ED 64.	There will be potentially significant implementation costs/challenges in recognizing and measuring the right-of-use asset and the lease liability.	There will be potentially significant implementation costs/challenges in recognizing and measuring the underlying asset for all former finance leases, the lease receivable for all former operating leases, the lease liability (unearned revenue) for all former finance leases and operating leases, and the changes to subleases, lease modifications, initial direct costs and variable lease payments.

	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13		Option 2 – IFRS 16		Option 3 – ED 64	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>GFS alignment impact</b>	<ul style="list-style-type: none"> <li>• <b>Guidance level:</b> <ul style="list-style-type: none"> <li>➢ Aligned as GFS also applies the risks and rewards model.</li> </ul> </li> <li>• <b>Practice level:</b> <ul style="list-style-type: none"> <li>➢ GFS does not use the data from financial statements.</li> <li>➢ Additional data is required to compile GFS accounts in order to recognize and measure the underlying asset.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Guidance level:</b> <ul style="list-style-type: none"> <li>➢ Aligned as GFS also applies the risks and rewards model.</li> </ul> </li> <li>• <b>Practice level:</b> <ul style="list-style-type: none"> <li>➢ GFS does not use the data from financial statements.</li> <li>➢ Additional data is required to compile GFS accounts in order to recognize and measure the underlying asset.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Guidance level:</b> <ul style="list-style-type: none"> <li>➢ Not aligned as GFS applies the risks and rewards model, not the right-of-use model.</li> </ul> </li> <li>• <b>Practice level:</b> <ul style="list-style-type: none"> <li>➢ GFS does not use the data from financial statements.</li> <li>➢ GFS must collect data through surveys to classify and account for leases.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Guidance level:</b> <ul style="list-style-type: none"> <li>➢ GFS applies the risks and rewards model.</li> </ul> </li> <li>• <b>Practice level:</b> <ul style="list-style-type: none"> <li>➢ GFS does not use the data from financial statements.</li> <li>➢ Additional data is required to compile GFS accounts in order to recognize and measure the underlying asset because the underlying asset may not be recognized by the lessor and the lessee if the lessor classifies the lease as finance lease.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Guidance level:</b> <ul style="list-style-type: none"> <li>➢ Not aligned as GFS applies the risks and rewards model, not the right-of-use model.</li> </ul> </li> <li>• <b>Practice level:</b> <ul style="list-style-type: none"> <li>➢ GFS does not use the data from financial statements.</li> <li>➢ GFS must collect data through surveys to classify and account for leases.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <b>Guidance level:</b> <ul style="list-style-type: none"> <li>➢ Not aligned as GFS applies the risks and rewards model, not the right-of-use model.</li> </ul> </li> <li>• <b>Practice level:</b> <ul style="list-style-type: none"> <li>➢ GFS does not use the data from financial statements.</li> <li>➢ GFS must collect data through surveys to classify and account for leases.</li> </ul> </li> </ul>
<b>IPSASB Conceptual Framework</b>	Not consistent (CF follows a control-based approach to asset recognition/derecognition, not a risks and rewards approach).		Consistent (see <a href="#">ED 64.BC6-BC8</a> for full details).	Not consistent (see <a href="#">ED 64.BC9-BC13</a> for full details)	Consistent (see <a href="#">ED 64.BC6-BC8</a> and <a href="#">ED 64.BC34-BC117</a> for full details)	

	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13		Option 2 – IFRS 16		Option 3 – ED 64	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>IFRS alignment</b>	Not aligned because IPSAS 13 applies a risks and rewards model and IFRS 16 applies a right-of-use model.	Compared to IAS 17, IFRS 16 changed subleases disclosures, lease modifications, initial direct costs and variable lease payments.	Aligned		Aligned	Not aligned in terms of classification of leases, finance lease and operating lease accounting requirements.

	No change/Stop the Leases project		Change/Continue with the Leases project			
			Partial change		Full change	
	Option 1 – IPSAS 13		Option 2 – IFRS 16		Option 3 – ED 64	
	Lessee	Lessor	Lessee	Lessor	Lessee	Lessor
<b>Feasibility of Leases project</b>	IPSAS 13 is already published. Current <i>status quo</i> is maintained.		Historically, IPSASB alignment projects with IFRS have been relatively straight forward and completed in a timely manner requiring less IPSASB's resources and are easier to manage.	<ul style="list-style-type: none"> <li>Historically, IPSASB alignment projects with IFRS have been relatively straight forward and completed in a timely manner. They require fewer IPSASB's resources and are easier to manage even with the need for re-exposure.</li> <li>Requires re-exposure</li> </ul>	<ul style="list-style-type: none"> <li>ED 64 proposals were strongly supported and IPSASB provisionally agreed to adopt this model, contingent on lessor accounting decisions.</li> <li>Historically, IPSASB alignment projects with IFRS have been relatively straight forward and completed in a timely manner requiring less IPSASB's resources and are easier to manage.</li> </ul>	<ul style="list-style-type: none"> <li>Assuming that the principles of ED 64 are not changed (continuing to recognize and measure the underlying asset according the applicable Standards and recognize the lease receivable and lease liability for almost all leases), the IPSASB will need a number of meetings to address respondents' suggestions to improve ED 64.</li> <li>Re-exposure will probably be required, unless those changes are insignificant.</li> </ul>