Lease

IFRS 16

Objective and scope

- IFRS 16 sets out the principles for the **recognition, measurement, presentation,** and **disclosure** of leases. The objective is to ensure that lessees and lessors provide relevant information in a manner that faithfully represents those transactions. This information gives a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of an entity.
- except for the following:

(a) Leases to explore for, or use, minerals, oil, natural gas and similar non-regenerative resources.

(b) Leases of biological assets within the scope of IAS 41 Agriculture held by a lessee.

(c) Service concession arrangements within the scope of IFRIC 12 Service Concession Arrangements.

(d) Licenses of intellectual property granted by a lessor within the scope of IFRS 15 Revenue from Contracts with Customers.

(e) Rights held by a lessee under

Definitions

- lease : **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.**

- contract An agreement between two or more parties that creates enforceable rights and obligations.
- period of use: The total period of time that an asset is used to fulfil a contract with a customer (including any non-consecutive periods of time).
- Terms defined in other Standards and used in this Standard with the same meaning.

Rights – Identified asset

identified asset to control the use of an identified asset; a customer is required to have the right to obtain substantially all of the economic benefits from use of the identified asset throughout the period of use.

Right to direct the use of the identified asset

The customer has the right to direct how and for what purpose the asset is used throughout the period of use.

- The relevant decisions about how and for what purpose an asset is used are predetermined and the customer either: (1) has the right to operate the asset, or to direct others to operate the asset in a manner that it determines, throughout the period of use, without the supplier having the right to change those operating instructions; or (2) designed the asset, or specific aspects of the asset, in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

Substantive substitution rights

A supplier's right to substitute an asset is substantive when both of the following conditions are met:

- The supplier has the practical ability to substitute alternative assets throughout the period of use (e.g., the customer cannot prevent the supplier from substituting an asset and alternative assets are readily available to the supplier or could be sourced by the supplier within a reasonable period of time).
- The supplier would benefit economically from the exercise of its right to substitute the asset (i.e., the economic benefits associated with substituting the asset are expected to exceed the costs associated with substituting the asset).

separating lease and non-lease components of a contract and allocating contract consideration

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Identifying and separating lease components of a contract

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Identifying and separating lease from non-lease components of a contract

Identifying and separating lease components of a contract

- The lessee can benefit from the use of the asset either on its own or together with other resources that are readily available to the lessee (i.e., goods or services that are sold or leased separately, by the lessor or other suppliers, or that the lessee has already obtained from the lessor or in other transactions or events).

And

- The underlying asset is neither highly dependent on, nor highly interrelated with, the other underlying assets in the contract.

Identifying and separating lease from non-lease components of a contract

- That do not relate to the transfer of goods or services by the lessor to the lessee:

Provides services (e.g., maintenance, supply of utilities) or operates the underlying asset (e.g., vessel charter, aircraft wet lease), the contract would generally contain non-lease components.

- **Practical expedient – lessees**

IFRS 16 provides this expedient to alleviate concerns that the costs and administrative burden of allocating consideration to separate lease and non- lease components may not be justified by the benefit of more precisely reflecting the right-of-use asset and the lease liability.

Determining and allocating the consideration in the contract

- **Lessees**

Allocate the consideration in the contract to the lease and non-lease components on a relative stand-alone price basis.

- **Lessors**

Allocate the consideration in the contract to the lease and non-lease components as per IFRS 15 basis.

Keys

Lease payments

Lease payments are payments, made by a lessee to a lessor, relating to the right to use an underlying asset during the lease term and include the following amounts:

- Fixed (including in-substance fixed) payments, less any lease incentives receivable from the lessor.
- Variable lease payments that depend on an index or a rate.
- The exercise price of a purchase option if the lessee is reasonably certain to exercise that purchase option.
- Payments for penalties for terminating a lease, if the lease term reflects the lessee exercising an option to terminate the lease.
- Amounts expected to be payable by the lessee under residual value guarantees (lessee only).
- Residual value guarantees provided to the lessor by the lessee, a party related to the lessee or a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee (lessor only).

Lease incentives

are received by the lessee at or before the lease commencement date reduce the initial measurement of a lessee’s right-of-use asset. Lease incentives that are receivable by the lessee at lease commencement date reduce a lessee’s lease liability (and therefore, the right-of-use asset as well).

- **For lessors,** lease incentives that are paid or payable to the lessee are also deducted from lease payments and affect the lease classification test. For finance leases, lease incentives that are payable to the lessee reduce the expected lease receivables at the commencement date and, thereby, the initial measurement of the lessor’s net investment in the lease. For operating leases, lessors should defer the cost of any lease incentives paid or payable to the lessee and recognise that cost as a reduction to lease income over the lease term.

lease payments that do not depend on an index or rate

Variable lease payments that do not depend on an index or rate and are not, in substance, fixed such as those based on performance (e.g., a percentage of sales) or usage of the underlying asset (e.g., the number of hours flown, the number of units produced), are not included as lease payments. Instead, they are recognised in profit or loss (unless they are included in the carrying amount of another asset in accordance with other IFRS) in the period in which the event that triggers the payment occurs.

Security deposits

prevailing market rate of interest for a similar loan to the lessor, considering the lessor’s credit-worthiness and, depending on facts and circumstances, any additional security available to the lessee, in accordance with IFRS 9.

- When the deposit earns interest below the market rate, the excess of the principal amount of the deposit over its fair value is accounted for by both the lessee and lessor as a prepaid lease payment. It is therefore considered by the lessor in determining whether the lease is an operating or finance lease. The lessee includes this amount in the cost of its right-of-use asset at the lease commencement date. For the lessor, if the lease is classified as an operating lease, the prepaid lease payment is included in the total lease payments that are recognised as income on either a straight-line basis or another systematic basis, if that basis is more representative of the pattern in which benefit from the use of the underlying asset is diminished. If the lease is classified as a finance lease, the lessor includes the prepaid lease payment in the consideration for the lease (i.e., lease payments) and, therefore, in the determination of the

Discount rates

Interest rate implicit in the lease: The rate of interest that causes the (a) present value of the lease payments and (b) the unguaranteed residual value to equal the sum of (i) the fair value of the underlying asset and (ii) any initial direct costs of the lessor. (Lessor and Lessee)

Lessee's incremental borrowing rate: The rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. (Lessee only)

Initial direct costs

- Incremental costs of obtaining a **lease** that would not have been incurred if the lease had not been obtained, except for such costs incurred by a manufacturer or dealer **lessor** in connection with a **finance lease**.
- **Lessor:**

Finance lease, the initial measurement of their net investments in finance leases and reduce the amount of income recognised over the lease term.

Operating lease, these initial direct costs are recognised as an expense over the lease term on the same basis as lease income.

- **Lessee:**

Include their initial direct costs in their initial measurement of the right-of-use asset.

Lessee accounting

Initial recognition

- IFRS 16 requires lessees to recognise a liability to make lease payments and an asset representing the right to use the underlying asset during the lease term for all leases, except for short-term leases and leases of low-value assets if they choose to apply such exemptions.
- short-term leases, at the commencement date, has a lease term of 12 months or less (a lease that contains a purchase option that is reasonably certain to be exercised is not a short-term lease).
- Leases of low-value assets, a lessee assesses the value of an underlying asset based on the value of the asset when it is new, regardless of the age of the asset being leased (US$5,000 or less).

Initial measurement

- **Right-of-use assets:**

- The amount of the initial measurement of the lease liability.
- Any lease payments made to the lessor at or before the commencement date, less any lease incentives received from the lessor.
- Any initial direct costs incurred by the lessee.
- An estimate of the costs to be incurred by the lessee in dismantling and removing the underlying asset, restoring the site on which the underlying asset is located or restoring the underlying asset to the condition required by the terms and conditions of the lease, unless those costs are incurred to produce inventories.
- a lessee may sign a lease contract with a lessor and make a payment to the existing lessee in return for vacating the property.

- **Lease liabilities:**

At the commencement date, a lessee shall measure the lease liability at the present value of the lease payments that are not paid at that date. The lease payments shall be discounted using the interest rate implicit in the lease, if that rate can be readily determined. If that rate cannot be readily determined, the lessee shall use the lessee's incremental borrowing rate.

- fixed payments, less any lease incentives receivable;
- variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date ;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option; and
- payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

Subsequent measurement

- **Right-of-use assets:**

- Cost Model, at cost less any accumulated depreciation and any accumulated impairment losses and adjusted for any remeasurement of the lease liability.

- The fair value model, that meet the definition of investment property in IAS 40.

- the revaluation model.

- **Lease liabilities:**
  - increasing the carrying amount to reflect interest on the lease liability;
  - reducing the carrying amount to reflect the lease payments made; and
  - remeasuring the carrying amount to reflect any reassessment or lease modifications or to reflect revised in-substance fixed lease payments.

- **Expense recognition:**

- The lessee recognises depreciation and impairment of the right-of-use asset in profit or loss.
- Interest on the lease liability.
- Variable lease payments not included in the measurement of the lease liability in the period in which the event or condition that triggers those payments occurs.

Remeasurement of lease liabilities

as an adjustment to the right-of-use asset.

- However, if the carrying amount of the right-of-use asset is reduced to zero and there is a further reduction in the measurement of the lease liability, a lessee shall recognise any remaining amount of the remeasurement in profit or loss.
- **Conditions:**

- change in the lease term.
- change in the assessment of an option to purchase the underlying asset.
- change in the amounts expected to be payable under a residual value guarantee.
- future lease payments resulting from a change in an index or a rate used to determine those payments.
- a lessee shall use an unchanged discount rate, unless the change in

Lease modifications

A change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease (for example, adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual

Separate lease

Change in the accounting for the existing lease

Separate lease

- The modification increases the scope of the lease by adding the right to use one or more underlying assets;

  and

- The consideration for the lease increases commensurate with the stand-alone price for the increase in scope and any adjustments to that stand-alone price reflect the circumstances of the particular contract.

Change in the accounting for the existing lease

The lessee require to recognise the amount of the remeasurement of the lease liability as an adjustment to the corresponding right-of-use asset without affecting profit or loss.

For a modification that fully or partially decreases the scope of the lease, a lessee require to decrease the carrying amount of the right-of-use asset to reflect partial or full termination of the lease. Any difference between those adjustments is recognised in profit or loss at the effective date of the modification.

Presentation

Financial statement	
Statement of financial position	• Right-of-use assets presented either: • Separately from other assets (e.g., owned assets) • Together with other assets as if they were owned, with disclosures of the statement of financial position line items that include right-of-use assets and their amounts. • Right-of-use assets that meet the definition of investment property are presented as investment property • Lease liabilities presented either: • Separately from other liabilities. • Together with other liabilities with disclosure of the statement of financial position line items that include lease liabilities and their amounts.
Statement of profit or	Lease-related depreciation and lease-related interest expense are presented separately (i.e., lease-

Presentation

Statement of cash flows	• Cash payments for the principal portion of the lease liability are presented within financing activities. • Cash payments for the interest portion of the lease liability are presented based on an accounting policy election in accordance with IAS 7*Statement of Cash Flows* • Lease payments for short-term leases and leases of low-value assets not recognised on the statement of financial position and variable lease payments not included in the lease liability are presented within operating activities • Non-cash activity (e.g., the initial recognition of the lease at commencement)

Disclosure

The objective of lessee disclosures is to enable financial statement users to assess the effect that leases have on a lessee's financial statements.

Contents:

- Carrying amount of right-of-use assets and depreciation charge for those assets, split by class of underlying asset
- Interest expense on lease liabilities
- Short-term lease expense for such leases with a lease term greater than one month
- Low-value asset lease expense (except for portions related to short-term leases)
- Variable lease expense (i.e., for variable lease payments not included in the lease liability)
- Income from subleasing right-of-use assets
- Total cash outflow for leases
- Additions to right-of-use assets
- Gains and losses arising from sale and leaseback transactions
- Carrying amount of right-of-use assets at the end of the reporting period by class of underlying asset

Additional disclosures

(a) the nature of the lessee’s leasing activities;

(b) future cash outflows to which the lessee is potentially exposed that are not reflected in the measurement of lease liabilities. This includes exposure arising from:

(i) variable lease payments.

(ii) extension options and termination options.

(iii) residual value guarantees.

(iv) leases not yet commenced to which the lessee is committed.

(c) restrictions or covenants imposed by leases.

(d) sale and leaseback transactions

Lessor accounting

- **Lease classification:**

- Finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset.

- Operating lease if it does not transfer substantially all the risks and rewards incidental to ownership of an underlying asset.

to a lease being classified as a finance lease

asset to the lessee by the end of the lease term.

- The lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception date, that the option will be exercised.
- The lease term is for the major part of the economic life of the asset even if title is not transferred.
- At the inception date, the present value of the lease payments amounts to at least substantially all of the fair value of the asset.
- The asset is of such a specialised nature that only the lessee can use it without major modifications.
- If the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee.
- Gains or losses from the fluctuation in the fair value of the residual accrue to the lessee .
- The lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent .

Reassessment of lease classification

- Lessors are required to reassess the lease classification only if there is a lease modification (i.e., a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease). Lessors reassess lease classification as at the effective date of the modification using the modified conditions at that date. If a lease modification results in a separate new lease, that new lease would be classified in the same manner as any new lease.

Key concepts applied by lessor

- The **lessor's gross investment** in a finance lease consists of the following undiscounted amounts:

  - **Lease payments** receivable by the lessor under a finance lease.

  - Any **unguaranteed residual value** accruing to the lessor - the unguaranteed residual value is the portion of the residual value of the underlying asset, the realisation of which by a lessor is not assured or is guaranteed solely by a party related to the lessor.

- A **lessor's net investment** in a finance lease consists of the gross investment in the lease discounted at the interest rate implicit in the lease.

Finance leases

Initial measurement

At the commencement date, the lease payments included in the measurement of the net investment in the lease comprise the following payments for the right to use the underlying asset during the lease term that are not received at the commencement date:

- Fixed payments (including in-substance fixed payments),less any lease incentives payable;
- Variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- guarantees provided to the lessor by the lessee, a party related to the lessee or a third party unrelated to the lessor that is financially capable of discharging the obligations under the
- The exercise price of a purchase option if the lessee is reasonably certain to exercise that option (assessed considering the factors described in paragraph B37); and
- Payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

At lease commencement, a lessor accounts for a finance lease, as follows:

- Derecognises the carrying amount of the underlying asset
- Recognises the net investment in the lease
- Recognises, in profit or loss, any selling profit or selling loss

Manufacturer or dealer lessors

manufacturer or dealer lessor shall recognise the following for each of its finance leases:

(a) revenue being the fair value of the underlying asset, or, if lower, the present value of the lease payments accruing to the lessor, discounted using a market rate of interest;

(b) the cost of sale being the cost, or carrying amount if different, of the underlying asset less the present value of the unguaranteed residual value; and

(c) selling profit or loss (being the difference between revenue and the cost of sale) in accordance with its policy for outright sales to which IFRS 15 applies. A manufacturer or dealer lessor shall recognise selling profit or loss on a finance lease at the commencement date, regardless of whether the lessor transfers the underlying asset as described in IFRS 15.

Subsequent measurement

Recognises finance income (in profit or loss) over the lease term in an amount that produces a constant periodic rate of return on the remaining balance of the net investment in the lease. Income is recognised on the components of the net investment in the lease, including:

- Interest on the lease receivable
- Interest via accretion of the unguaranteed residual asset to its expected value at the end of the lease

Reduces the net investment in the lease for lease payments received (net of finance income calculated above)

Separately recognises income from variable lease payments that are not included in the net investment in the lease in the period in which that income is earned.

Recognises any impairment of the net investment in the lease.

Remeasurement of the net investment in the lease

- **Reasons:**

- The lease is modified
- The lease term is revised when there is a change in the non-cancellable period of the lease.
- There is a change in the estimated unguaranteed residual value.

Operating leases

Modifications to a finance lease

Separate lease

- The modification increases the scope of the lease by adding the right to use one or more underlying assets; and
- The consideration for the lease increases by an amount commensurate with the stand-alone price for the increase in scope and any appropriate adjustments to that stand-alone price to reflect the circumstances of the particular contract.

Does not result in a separate lease

- If the lease would have been classified as an operating lease had the modification been in effect at the inception date, lessors account for such modifications as the creation of a new lease that commences on the effective date of the modification. The carrying amount of the underlying asset is measured as the net investment in the original lease immediately before the effective date of

Modification to an operating lease

- If an operating lease is modified and the arrangement continues to be or contains a lease, it is treated as a new lease from the effective date of the modification.

Presentation

- Lessors recognise assets held under a finance lease in the statements of financial position and present them as a receivable at an amount equal to the net investment in the lease under IFRS 16.
- In addition, lessors are required under IFRS 16 to present underlying assets subject to operating leases according to the nature of that asset in the statement of financial position. The net investment in the lease is subject to the same considerations as other assets in classification as current or non-current assets in the statement of financial position.

Disclosure

Finance leases:

(i) Selling profit or loss;

(ii) Finance income on the net investment in the lease; and

(iii) Income relating to variable lease payments not included in the measurement of the net investment in the lease.

Operating leases:

- Lease income, separately disclosing income relating to variable lease payments that do not depend on an index or a rate.

Additional qualitative and quantitative information

- An explanation of the significant changes in the carrying amount of the net investment in finance lease
- A maturity analysis of the lease payments receivable, showing the undiscounted lease payments to be received on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years. A lessor shall reconcile the undiscounted lease payments to the net investment in the lease. The reconciliation shall identify the unearned finance income relating to the lease payments receivable and any discounted unguaranteed residual value.

Subleases

If a lessee subleases an asset, or expects to sublease an asset, the head lease does not qualify as a lease of a low-value asset.

- **Sublease classification**

if the head lease is a short-term lease that the entity, as a lessee, has accounted for applying paragraph 6, the sublease shall be classified as an operating lease.

otherwise, the sublease shall be classified by reference to the right-of- use asset arising from the head lease, rather than by reference to the underlying asset (for example, the item of property, plant, or equipment that is the subject of the lease).

Intermediate lessor accounting:

- If the sublease is classified as an operating lease, the original lessee continues to account for the lease liability and right-of-use asset on the head lease like any other lease. If the total remaining carrying amount of the right-of-use asset on the head lease exceeds the anticipated sublease income, this may indicate that the right- of-use asset associated with the head lease is impaired need to be assessed for impairment under IAS 36.
- If the sublease is classified as a finance lease, the original lessee derecognises the right-of-use asset on the head lease at the sublease commencement date and continues to account for the original lease liability in accordance with the lessee accounting model.
- The original lessee, as the sublessor, recognises a net investment in the sublease and evaluates it for impairment.

Sale and leaseback transactions

- A sale and leaseback transaction involves the transfer of an asset by an entity (the seller-lessee) to another entity (the buyer-lessor) and the leaseback of the same asset by the seller-lessee.
- the transfer of an asset is a sale – IFRS 15.

the transfer of an asset is not a sale – financing

- The seller-lessee keeps the transferred asset subject to the sale and leaseback transaction on its statement of financial position and accounts for amounts received as a financial liability in accordance with IFRS 9. The seller-lessee decreases the financial liability by the payments made less the portion considered interest expense.
- If the transfer of an asset is not a sale, the buyer-lessor does not recognise the transferred asset and accounts for the amounts paid as a receivable in accordance with IFRS 9.

Disclosure

- The lessee’s reasons for sale and leaseback transactions and the prevalence of those transactions;
- Key terms and conditions of individual sale and leaseback transactions;
- Payments not included in the measurement of lease liabilities; and
- The cash flow effect of sale and leaseback transactions in the reporting period.

Thanks,

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