



Exposure Draft - *Leases*

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation

Why a lease project?

- **Existing lease accounting doesn't meet users' needs**
 - Accounting depends on classification
 - Users adjust financial statements to recognise assets and liabilities arising in operating leases
- **Complexity**
 - Difficult to define dividing line between finance and operating

Scope

- Joint project with FASB
- Excludes:
 - Lessors with investment property at fair value under IAS 40
 - Purchase and sale contracts
 - Leases of intangible assets
 - Leases of biological assets or to explore for or use natural resources
- Includes “simplified” accounting for short-term leases
- Includes certain requirements for sale/leasebacks
- Incorporates IFRIC 4 to differentiate service contracts from leases
- Requires separation of lease payments into service and lease components

Lessee model: Right-of-Use

Lessee has acquired a right to use the underlying asset and is paying for that right with its lease payments

All leases in scope			
Balance sheet		Income Statement	
• Right-of-use asset*	X	• Amortisation expense	X
• Liability to make lease payments	X	• Interest expense	X

* Shown in the property, plant and equipment category

Lessee measurement

	Initial Measurement	Subsequent Measurement
Liability to make lease payments	PV of lease payments discounted using incremental borrowing rate	Amortised cost No revision of incremental borrowing rate
Right-of-use asset	Cost (= liability to make lease payments)	Amortised cost (option to revalue*)

*Revaluation of entire class of PP&E is required if right-of-use is revalued

Lessor model: Right-of-Use

- Right to receive lease payments recorded on transfer of right to use underlying asset
- Account for underlying asset based on exposure to risks* or benefits of that asset during or subsequent to the expected term of the lease

Does the lessor retain significant risks or benefits of the underlying asset?

No

Derecognition approach

Yes

Performance Obligation approach

*Counterparty credit risk is not considered

Does the lessor retain significant risks or benefits of the underlying asset?

No

Derecognition approach

Balance sheet

- Residual asset X
- Right to receive lease payments X

Income Statement

- Revenue X
- Cost of sales (X)
(gross or net based on business model)
- Interest income X

Does the lessor retain significant risks or benefits of the underlying asset?

Yes

Performance obligation approach

Balance sheet

(Gross with linked presentation)

• Underlying asset	X
• Right to receive lease payments	X
• Lease liability	<u>(X)</u>
Net lease asset (liability)	X

Income Statement

(Separate presentation –IASB)

• Lease income	X
• Depreciation expense	(X)
• Interest income	X

Lessor model - measurement

	Initial Measurement	Subsequent Measurement
Derecognition approach		
Right to receive lease payments	PV of lease payments discounted using the rate charged in the lease	Amortised cost
Residual asset	Allocated carrying amount	No remeasurement (except for impairment)
Performance Obligation approach		
Right to receive lease payments	PV of lease payments discounted using the rate charged in the lease	Amortised cost
Lease liability	Transaction price (= right to receive payments)	Recognise income as the liability is satisfied over the lease term

Options to extend lease term

- Include longest possible lease term that is more likely than not to occur
 - In lessee's liability to make lease payments
 - In lessor's right to receive lease payments
- Reassess if facts or circumstances indicate that there is a significant change
 - Adjust liability and right-of-use asset for lessees
 - Adjust right to receive and liability or residual asset for lessors
- Purchase options
 - Account for only when they are exercised (= termination of lease)

Contingent rentals and RVG

- Include expected outcome in lease asset and liability
 - Lessees must always include, Lessors only if measured reliably
- Same for residual value guarantees provided by lessee
- Reassess if facts or circumstances indicate a significant change

Lessees	Lessors	
<p>Adjust liability to make payments and profit or loss <i>for changes related to current or past periods</i> or right-of-use asset <i>for changes related to future periods</i></p>	<p><u>Derecognition approach:</u> Adjust right to receive rentals and profit or loss</p>	<p><u>Performance obligation approach:</u> Adjust right to receive rentals and profit or loss <i>to the extent liability is satisfied</i> or liability <i>to the extent not yet satisfied</i></p>

Options to extend and contingent rentals: potential concerns

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Concerns

Response

Options to extend

Subjectivity of judgement

Requirement to reassess (true-up information)

Renewals are avoidable –understates
financial flexibility

Provides estimates of likely cash outflows

Contingent rentals

Subjectivity of information

Requirement to reassess (true-up information)

Cost/benefit of determining information

Ignoring would lead to structuring

Reliable measurement

Some users prefer estimates to no information

- Identify and explain the amounts recognised in the financial statements arising from leases; and
- Describe how leases may affect the amount, timing and uncertainty of the entity's future cash flows.
- Include:
 - Nature of lease contracts
 - Accounting policy for models used (lessor)
 - **Maturity analysis**
 - Income recognition information
 - Discount rates
 - **Roll-forward** of related assets and liabilities

Transition

- All leases
 - Simplified retrospective approach
 - Present value of remaining lease payments
 - Effective date: TBD

- **Lessee:**

Liability to make lease payments	=	Right-of-use asset	=	PV of lease payments
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- **Lessor:**

PO approach
Right to receive lease payments = Lease liability = PV of lease payments

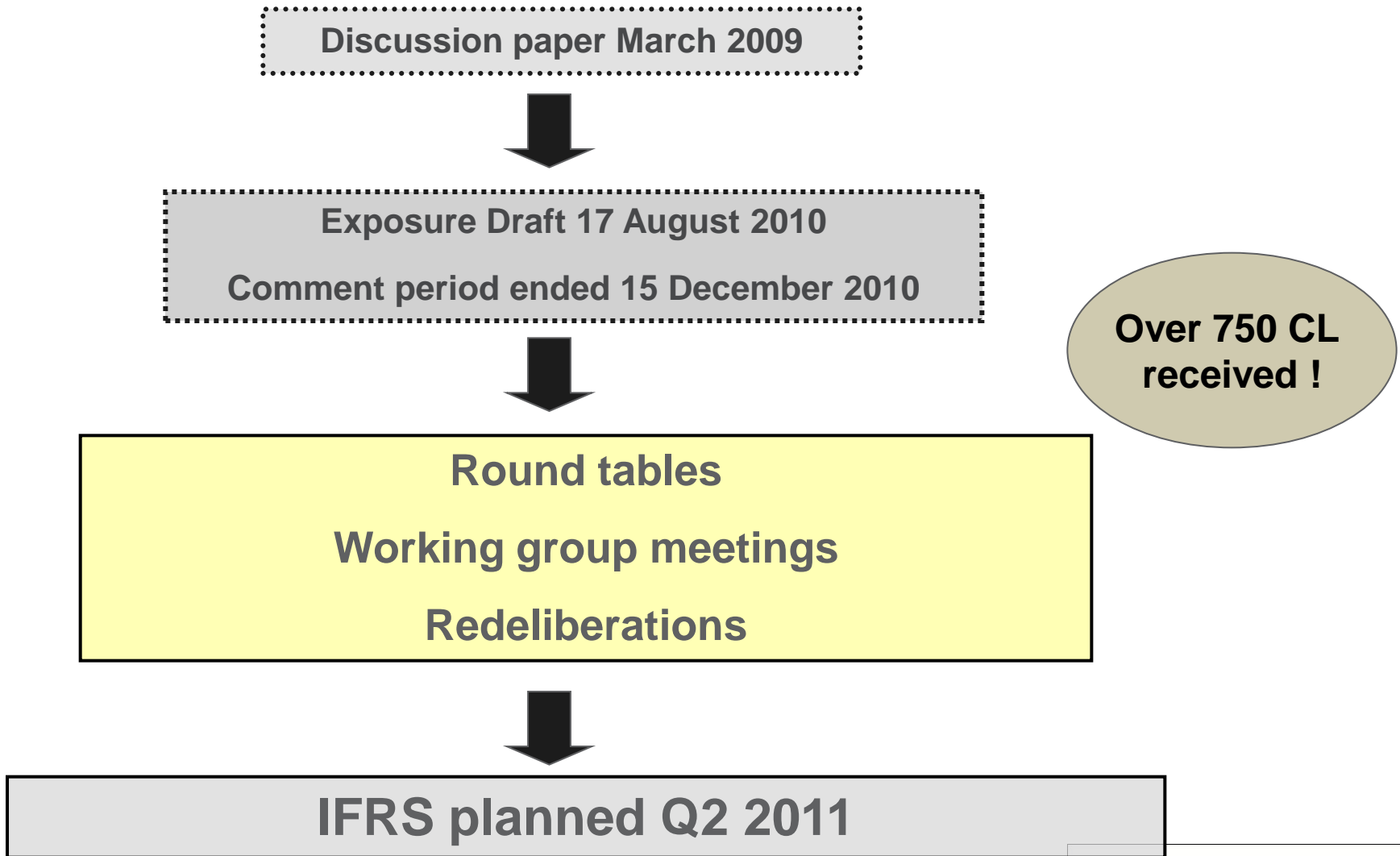
Derecognition approach
Right to receive lease payments = PV of lease payments
Residual asset = Fair value

Comment letters summary:

<http://www.ifrs.org/NR/rdonlyres/08B09F06-60A1-4C86-AFC1-3B97704A0D83/0/LeasesEDCommentletterSummary.pdf>

- Lessees:
 - Profit and loss effects (front-loading)
- Lessors:
 - Performance obligation approach (double counting?)
 - Subsequent measurement of residual asset under derecognition approach (cost or fair value?)
- General:
 - Treatment of options / contingent rentals (=Framework?)
 - Shorter term leases (not enough simplification)
 - Services versus leases – more tension put on criteria
 - Transition

What's next?



Financial Crisis related projects	2011 Q1	2011 Q2	2011 H2+	MeU	Joint
Financial instruments (IAS 39 replacement)					
Impairment	RV			✓	✓
Hedge accounting [ED, comments due 9 March 2011]		IFRS		✓	✓
Asset and liability offsetting	ED			✓	✓
Consolidation					
Replacement of IAS 27	IFRS			✓	✓
Disclosures unconsolidated entities	IFRS				
Investment companies		ED			✓
Fair value measurement	IFRS			✓	✓

Memorandum of Understanding projects	2011 Q1	2011 Q2	2011 H2+	MeU	Joint
Financial statement presentation (Presentation of OCI)	IFRS				
Leases	RT 5 and 6 Jan	IFRS		✓	✓
Revenue recognition		IFRS		✓	✓
Joint ventures	IFRS			✓	
Post-employment benefits	IFRS			✓	
Effective dates and transition [Request for Views, comments due 31 January 2011]					✓

Other projects	2011 Q1	2011 Q2	2011 H2+	MeU	Joint
Insurance contracts		IFRS			✓
Annual improvements 2009-2011		ED			

Agenda consultation	2011 Q1	2011 Q2	2011 H2+
Three-yearly public consultation	RV		

Abbreviations	
AD Agenda Decision (to add the topic to the active agenda)	PS IFRS Practice Statement
DP Discussion Paper	ED Exposure Draft
IFRS International Financial Reporting Standard	RT Roundtables
RV Request for Views	TBD To be determined

Boards Re-deliberations Plan (January to May 2011)

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- 5 main issues:
 - Definition of a lease (vs Service contract)
 - Lessor accounting model (keep IAS17?)
 - Assessment of lease term
 - Variable lease payments (contingent rent)
 - Profit & Loss recognition pattern (front loading of interest expense vs straight line expense pattern)
- Other issues
 - Scope of project – Intangible assets?
 - Separating lease elements from service elements of complex lease contracts
 - Simplifications for short term leases
 - Fully retrospective application? Effective date? Early adoption?

- Request For Views published in October 2010 by IASB and FASB to assess whether the 4 new standards* should become effective one at a time or all at the same time
 - Also need input on delay necessary to adapt information systems
 - Take into consideration the required restatement of (two) comparative periods
- ➔ Effective date could be no earlier than 2014, possibly 2015

(*) *Leases, Revenue, Financial Instruments, Insurance*

PRESS RELEASE

19 October 2010

IASB and FASB consult on effective dates for accounting standards

The International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) today published documents seeking views on when new financial reporting standards resulting primarily from their work to improve and achieve convergence of International Financial Reporting Standards (IFRSs) and US generally accepted accounting principles (GAAP) should become effective.

When finalising an IFRS, the IASB will identify a date from which entities will be required to start applying the new requirements (known as the effective date). This date is often 12-18 months after the date the IFRS is published, allowing time for entities to prepare for the change and for jurisdictions to implement the IFRS into their legal or regulatory regime.

With a number of major projects planned to be completed in 2011, the boards are seeking views on whether or how to sequence effective dates in order to reduce the burden to interested parties. In deciding how to proceed, the IASB will consider the needs of jurisdictions already using IFRSs as well as those planning to do so. Feedback from the consultation will inform the boards as they jointly develop an implementation plan for those new standards that helps stakeholders to manage both the pace and cost of change.

The projects covered by the request for views include the second and third phases of *Financial Instruments*, *Revenue from contracts with customers*, *Insurance contracts* and *Leases*. Comments are requested by 31 January 2011.

Commenting on the request for views, Sir David Tweedie, Chairman of the IASB, said:

“The next six to eight months will see a number of new IFRSs being published. Whilst each of these standards will provide more decision-useful information to investors, we want to know if users and preparers prefer the effective dates to be batched together or sequenced over a period of time.”

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Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged. The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.

