

Meeting: International Public Sector Accounting Standards Board

Meeting Location: Toronto, Canada

Meeting Date: June 21-24, 2016

Agenda Item 7

For:

☒ Approval

☒ Discussion

☐ Information

Leases

Project summary	Develop revised requirements for lease accounting covering both lessees and lessors in order to maintain convergence with IFRS 16, <i>Leases</i> . The project will result in a new IPSAS that will replace IPSAS 13.	
Meeting objectives	Topic	Agenda Item
Decisions required at this meeting	1. Approval of Project Brief, <i>Leases</i>	7.1
	2. Lessee—Applicability of IFRS 16 recognition and measurement requirements to public sector financial reporting	7.2
	3. Lessee—"Peppercorn" leases	7.3
	4. Lessor—Applicability of IFRS 16 recognition requirements to public sector financial reporting	7.4
Other supporting items	Project Brief, <i>Leases</i> (marked-up version from March 2016 meeting)	7.5

PROJECT BRIEF, *LEASES*

1. Introduction

- 1.1 IPSAS 13, *Leases*, was issued in December 2001. It is a converged standard based on International Accounting Standard (IAS) 17, *Leases*.
- 1.2 In January 2016, the IASB issued International Financial Reporting Standard (IFRS) 16, *Leases*, which supersedes IAS 17. It also supersedes three interpretations: IFRIC 4, *Determining whether an Arrangement contains a Lease*, SIC-15, *Operating Leases-Incentives* and SIC-27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.
- 1.3 IFRS 16 introduces “a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value”¹. The lessor accounting in IFRS 16 remains substantially the same as in IAS 17. IFRS 16 retains the dual lessor accounting model that previously existed in IAS 17 in which leases are categorized as operating leases and finance leases.
- 1.4 IFRS 16 is effective for annual periods beginning on or after 1 January 2019 with earlier application permitted for entities that apply IFRS 15, *Revenue from Contracts with Customers* at or before the date of initial application of IFRS 16.
- 1.5 Many public sector entities use leasing arrangements for gaining access to assets, which they use in service delivery. Leasing is a means of obtaining finance, and of reducing an entity's exposure to the risks of asset ownership. The prevalence of leasing, therefore, means that it is important that users have a complete and understandable picture of an entity's leasing activities.
- 1.6 Like IAS 17, lease classification using IPSAS 13 has focused on the extent to which the risks and rewards incidental to ownership of a lease lie with the lessor or the lessee. IPSAS 13 classifies leases as either finance leases or operating leases. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership. For finance leases, the lessee recognizes assets and liabilities in the statement of financial position. For operating leases, the lessee accounts for lease payments as an expense on a straight-line basis over the lease term.
- 1.7 This model has been criticized for failing to meet the needs of users because:
 - (a) The resulting financial statements do not always provide a faithful representation of leasing transactions, because they omit resources and obligations that, conceptually, meet the definition of an asset and a liability particularly for operating leases; and
 - (b) The significant difference in recognition requirements for finance and operating leases has created incentives to structure some transactions as operating leases to achieve off-balance sheet accounting.
- 1.8 The IASB noted that, as a result, many users adjust the amounts reported in a lessee's financial statements to reflect the assets and liabilities arising from off-balance sheet leases, and make other consequential adjustments. However, because of the limited information available, such estimates may be inaccurate. In addition, many other users do not make adjustments. This creates asymmetry and leads to unreliable information in the market.

¹ Paragraph IN10 of IFRS 16

- 1.9 The objective of the project is to develop revised requirements for lease accounting covering both lessees and lessors in order to maintain alignment with the underlying IFRS. The project will result in a new IPSAS that will replace IPSAS 13.
- 1.10 Because this project is revising or replacing requirements in an existing IPSAS, the scope is clearly defined and it may be less resource intensive than “blue sky” projects.
- 1.11 Responses to the 2014 strategy consultation supported the ongoing alignment of existing IPSASs with underlying IFRSs. If a project to amend IPSAS 13 in order to align it with IFRS 16 is not undertaken, it will lead to a major divergence in lease accounting between the public sector and the private sector. Unless there are public sector specific reasons for such a divergence, the co-existence of different lessee accounting models for leases will also create additional burdens for consolidation where commercial public sector entities are reporting in accordance with IFRS.

2. Project Rationale and Objectives

(a) Project rationale

- 2.1 The project rationale is that IAS 17, from which IPSAS 13 was primarily drawn, has been replaced by IFRS 16. Not amending or replacing IPSAS 13 will result in the use of different models for accounting for leases in the public and private sectors.

(b) Objectives to be achieved

- 2.2 The objective is to issue a new IPSAS on Leases which will be converged with IFRS 16.
- 2.3 The intermediate objective is to produce an Exposure Draft (ED) of proposed new IPSAS on Leases.

(c) Link to IFAC and IPSASB Strategic Plans

i. Link to IPSASB Strategy

- 2.4 The project is consistent with the IPSASB's strategic objective of “strengthening public financial management and knowledge globally through increasing adoption of accrual-based IPSASs by developing high-quality public sector financial reporting standards”². IFRS convergence, where appropriate, is one of the factors the IPSASB considers in prioritizing the work plan³.

ii. Link to IFAC Strategic Plan

- 2.5 This project is aligned with the mission of IFAC, as stated in its Strategic Plan for 2016–2018, *Charting the Future of the Global Profession*, of serving the public interest and strengthen the accountancy profession by:
- (a) Supporting the development of high-quality international standards; and
 - (b) Promoting the adoption and implementation of these standards.

² Page 6 of *The IPSASB's Strategy for 2015 Forward*

³ See page 11 of *The IPSASB's Strategy for 2015 Forward*.

3. Outline of the Project

(a) Project Scope

- 3.1 The scope of this project is to develop accounting requirements for leases that are converged with IFRS 16.

(b) Key Issues

- 3.2 The key issues are listed below. The list is not exhaustive.

Key issue #1—Assumption that IFRS convergence is appropriate for leasing transactions in the public sector

- 3.3 When IPSAS 13 was developed the IPSASB decided that it should be converged with IAS 17 because the underlying accounting transactions are the same in the public sector and in the private sector – a lease is a lease – and that there were no public sector specific reasons to diverge from IAS 17. The project will assess whether a similar assumption can be made for IFRS 16, and, if so, develop proposals that are converged with the new IASB standard.
- 3.4 If the IPSASB decides to converge with IFRS 16, there will be implementation costs of the new IPSAS. If the IPSASB decides not to converge with IFRS 16, there are ongoing consolidation issues that needs to be addressed where commercial public sector entities that apply IFRS 16 or the national standard converged with IFRS 16 are consolidated by an entity that applies IPSASs.
- 3.5 Staff notes that in the first scenario the costs are mostly “one-off” in the first year of the application of the new lessee accounting model. These costs are associated with the recognition and measurement of the assets and the related liabilities.
- 3.6 In the latter scenario, the consolidation issues are not “one-off” and will recur in subsequent years.
- 3.7 By providing exemptions for short-term leases and leases for which the underlying asset is of low value, the IASB has sought to lower the costs of implementing IFRS 16.
- 3.8 The Board needs to consider whether in a public sector context the cost of introducing an IFRS 16 approach exceed the benefits.
- 3.9 The IPSASB’s policy paper⁴, *Process for Reviewing and Modifying IASB Documents* (also known as *Rules of the Road*), will guide the process.

Key Issue #2—Identification of a lease

- 3.10 As stated in paragraph 1.3, IFRS 16 has one single lessee accounting model in which all leases are accounted for in the same way, with the recognition of assets and liabilities for all leases (with limited exceptions). IFRS 16 provides optional recognition exemptions for short-term leases⁵ or leases for which the underlying asset is of low value⁶.
- 3.11 While the issue of identification of a lease is not new, IFRS 16 includes a considerable amount of new material on how leases are identified⁷. The requirements and guidance on lessee

⁴ See at <http://www.ifac.org/system/files/publications/files/IPSASB-Rules-of-the-Road-Oct2008.pdf>

⁵ A lease that, at the commencement date, has a lease term of 12 months or less. A lease that contains a purchase option is not a short-term lease.

⁶ The assessment of whether an underlying asset is of low value is performed on an absolute basis.

⁷ Staff notes that although the definition of a lease changed in IFRS 16, its meaning is basically the same.

accounting are no longer based on classifying a lease as a finance lease or an operating lease, dependent on the risks and rewards incidental to ownership. IFRS 16 provides requirements and guidance in distinguishing a lease from a service based on the following rationale⁸:

- Lease: the costumer (the lessee) has a right to control the use of the asset.
- Service: the supplier has a right to control the use of the asset.

- 3.12 The right to control the use of an asset approach is based on the right to obtain substantially all of the economic benefits from use of the identified asset (a “benefits” element) and the right to direct the use of the identified asset (a “power” element).
- 3.13 At an early stage the project will need to assess to what extent the right to control the use of an asset based on these two elements is applicable to the public sector.
- 3.14 The new IPSAS will have specific guidance to distinguish a lease from service concession arrangements (IPSAS 32, *Service Concession Arrangements: Grantor*) from the perspective of the grantor.

Key Issue #3—Impact of revised lessee accounting model

- 3.15 The new lessee accounting model will have an impact on the recognition, measurement, presentation and disclosure of assets, liabilities, revenue and expense. The recognition of assets and liabilities associated with a lease will have a major impact on the financial statements of public sector entities that use leases extensively in their operations.
- 3.16 Although the IPSASB’s literature does not include a standard on budget formulation and execution, the new lessee accounting model may have an impact in jurisdictions where entities base their budget accounting for leases on IPSAS.
- 3.17 In jurisdictions that apply “pure” accrual budgeting the impact on the budget will be the same as the impact on accrual accounting. In countries that do not apply “pure” accrual budgeting the impact will depend on the extent to which accrual information is used for budget purposes.
- 3.18 The change in the lessee accounting model will also affect fiscal targets set by governments when they use accrual-based IPSASs as the accounting bases. Staff notes that in many countries fiscal targets are based on Government Finance Statistics (GFS) reporting guidelines. As GFS is not changing its lease accounting guidance (or requirements), the new lessee accounting model will have no impact on performance against these fiscal targets.
- 3.19 The project will need to assess any consequential changes to existing IPSASs. These may be based on the consequential amendments made to other IFRSs made by IFRS 16, or may be specific to existing IPSASs (for example, the distinction between a lease and a service concession arrangement under IPSAS 32).
- 3.20 The project will also need to assess when the new IPSAS should become effective.
- 3.21 IFRS 16 will only be effective in 2019. The IPSASB convention is that an effective date is no less than eighteen months after publication.

IPSAS 13—A lease is an agreement whereby the lessor conveys to the lessee, in return for a payment or series of payments, the right to use an asset for an agreed period of time.

IFRS 16—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.

⁸ According to Paragraph BC140 of IFRS 16 “the new standard applies to contracts that convey the right to use an underlying asset for a period of time and does not apply to transactions that transfer control of the underlying asset to an entity—such transactions are sales or purchases within the scope of other Standards (for example, IFRS 15 or IAS 16).”

- 3.22 The IPSASB will also need to assess whether it will apply the same criteria as the IASB in determining an effective date for IFRS 16 or there are public sector reasons that warrant a different period to the effective date for the new IPSAS.

Key Issue #4—Sale and leaseback transactions

- 3.23 IFRS 16 introduced additional requirements to recognize revenue **only** to be applicable within the context of a sale and leaseback transaction. IFRS 16 now requires that a transfer of an asset is accounted for as a sale only if the transfer meets the requirements in IFRS 15, *Revenue from Contracts with Customers*. The IASB was of the view that this requirement “will be beneficial for both preparers and users of financial statements because it will increase comparability between sales entered into as part of a sale and leaseback transactions and all other sales.”⁹
- 3.24 IFRS 15 follows a *performance obligation* approach to recognize revenue from the transfer of goods and services to customers and is applicable to both lessee and lessor¹⁰.
- 3.25 According to IFRS 16, if the transfer of the underlying asset satisfies the requirements of IFRS 15 to be accounted for as a sale, the transaction will be accounted for as a sale (the seller-lessee derecognizes the underlying asset and the buyer-lessor recognizes the underlying asset) and a lease by both the lessee and the lessor. If not, the transaction is accounted for as a financing by both the seller-lessee and the buyer-lessor and both apply IFRS 9, *Financial Instruments*.
- 3.26 Currently IPSASB's literature does not have a performance obligation approach to the recognition of revenue from the sale of assets. Staff has identified two options to manage this new requirement in IFRS 16 in the future development of the Leases project:
- (a) Option 1—Do not include any requirement now and include the performance obligation approach later (as a consequential amendment of the new IPSAS on Revenue); and
 - (b) Option 2—Include current IPSASs requirements¹¹ now and include the performance obligation approach later (as a consequential amendment a new or revised IPSAS on Revenue).
- 3.27 As the effective date of the new IPSAS on revenue is still uncertain and the Revenue project is still in a Consultation Paper phase, staff is of the view that the Leases project cannot be linked to the Revenue project and, as a consequence, delay the Leases project, as the IPSASB always have the two above options.
- 3.28 During the development of the Leases project, the IPSASB will need to decide which of these two options will be applied in the new IPSAS on Leases.

Key Issue #5—New disclosures in lessor accounting model

- 3.29 As stated in paragraph 1.3, lessor accounting remains substantially the same as in IFRS 16. However, IFRS 16 introduced enhanced disclosures for lessors providing information on:
- (a) The different components of lease revenue recognized during the reporting period;
 - (b) Residual asset risk;
 - (c) Assets subject to operating leases;

⁹ Paragraph BC261 of IFRS 16

¹⁰ See paragraphs BC262-BC265 of IFRS 16 for further details on IASB's rationale.

¹¹ IPSAS 9, *Revenue from Exchange Transactions* and IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*

- (d) Maturity analyses; and
 - (e) Changes in net investment in finance leases.
- 3.30 Staff notes that quite often public sector entities lease assets to other public sector entities (for example, to improve occupancy rate of unused buildings). In many jurisdictions, governments also establish public sector entities specializing in leasing assets to public sector entities. These “centralized lessors” have an important role in managing assets (mainly buildings) in the public sector. The IPSASB will need to assess to what extent these new disclosures are appropriate for public sector entities and whether further specific disclosures are required.

Key Issue #6—Lack of symmetry in lease accounting

- 3.31 IFRS 16 does not follow a symmetrical approach to lease accounting, i.e., while the lessee is required to recognize (almost) all leased assets (the right-of-use asset) and related liabilities, the lessor only recognizes a lease asset (the net investment in the lease) if the lease is classified as a finance lease.
- 3.32 One consequence of the lack of symmetry in IFRS 16 is that the underlying asset may not be recognized in either the lessee’s or the lessor’s statement of financial position. This might occur when the lessor classifies the lease as a finance lease.
- 3.33 The IASB explained the reason for the asymmetrical approach in paragraph BC61(b) of the Basis for Conclusions to IFRS 16:
- “most users of financial statements do not currently adjust lessors’ financial statements for the effects of leases—indicating that the lessor accounting model in IAS 17 already provides users of financial statements with the information that they need. In addition, investors generally analyse the financial statements of individual entities (and not a lessee and lessor of the same underlying asset). Accordingly, it is not essential that the lessee and lessor accounting models are symmetrical.”
- 3.34 Staff notes that this rationale is not related to the economics of a lease; rather it is related to the specific business environment and users’ needs in the for-profit sector.
- 3.35 Staff notes that the business environment and users’ needs in the for-profit sector may be different from the public sector. In fact, in the public sector very often the lessor and the lessee are both public sector entities and the same public sector entity can be simultaneously lessor and lessee in different lease contracts with other public sector entities or with private sector entities. These types of transactions can also occur within the same economic entity or between different levels of government not under common control.
- 3.36 The lack of symmetry in lease accounting would also create asymmetrical information in public sector financial reporting when governments do not publish consolidated financial statements and users have to rely on the separate financial statements of individual entities for accountability and decision-making purposes.
- 3.37 In this context, users of general purpose financial reports of public sector entities often analyze the financial statements of the lessee and lessor of the underlying asset in order to better assess the risks of lending resources and understand who controls the underlying asset. The underlying asset may be used as collateral for borrowing¹².

¹² For example: a public sector entity, which is a specialized lessor for the public sector, issues bonds in the capital markets to finance purchases of assets from other public sector entities that will be leased-back. As bonds are issued in the name of the public sector entity and not in the name of the State or guaranteed by the State, lenders may require the underlying asset to be used as collateral for borrowing, and understand who, in fact, controls the underlying assets.

- 3.38 The derecognition of the underlying asset by the lessor may mean that the financial information on leasing transactions does not meet the objectives of financial reporting because users are not provided with information that is useful for accountability and decision-making purposes.
- 3.39 Because of the introduction of the right-of-use model in lessee accounting, the IPSASB will need to assess the need of symmetry for lessor accounting in the light of the objectives and qualitative characteristics of public sector financial reporting.

Key Issue #7—"Peppercorn" leases

- 3.40 For the purpose of this project, staff will consider "peppercorn" leases all leases with nominal, reduced or rent-free, i.e., all leases that are not exchange transactions as defined in IPSASs glossary¹³.
- 3.41 Staff notes that the decision to add "peppercorn" leases will affect the scope of an Exposure Draft.
- 3.42 Quite often public sector entities and international organizations enter into a "peppercorn" lease for the whole period of use of the underlying asset that does not involve a sale and leaseback transaction. "Peppercorn" leases usually occur between public sector entities and between international organizations.
- 3.43 IFRS 16 requires that the lease asset and liability are measured at cost¹⁴. Applying IFRS 16 measurement requirements to "peppercorn" leases will lead to an understatement of the lease asset and a failure to recognize the subsidy from the lessor to the lessee in the financial statements of both the lessee and the lessor. Therefore, the accounting requirements for "peppercorn" leases will be developed for lessee and lessor.
- 3.44 Staff has identified two mutually exclusive options to address "peppercorn" leases in IPSASs:
- (a) Option 1—Include "peppercorn" leases within the scope of the new IPSAS on Leases; or
 - (b) Option 2—Include "peppercorn" leases explicitly within the scope of IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)* or in IPSASB's current projects on non-exchange expenses and revenue.
- 3.45 Staff has also identified two mutually exclusive options to measure leases, including "peppercorn leases":
- (a) Option 1—Measure all leases at fair value; or
 - (b) Option 2—Measure leases that are exchange transactions at cost and measure peppercorn leases (non-exchange transaction) at fair value.
- 3.46 During the development of the Leases project, the IPSASB will need to decide which of these options will be applied in the new IPSAS on Leases.

4. Describe the Implications for any Specific Persons or Groups

(a) Relationship to IASB

- 4.1 The project is primarily linked to IFRS 16. There are also links to IFRS 15.

¹³ Transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

¹⁴ Paragraphs 23, 24, 26 and 27 of IFRS 16

(b) Relationship to Other Standards, Projects in Process or Planned Projects

- 4.2 There are links to the Conceptual Framework, to other IPSASs, notably IPSAS 17, *Property Plant and Equipment* and IPSAS 32 and the IPSASB's Revenue project.
- 4.3 The recognition section of IPSAS 17 will need to be amended to reflect the new approach to lessee accounting.
- 4.4 There will be consequential amendments in IPSAS 32 a result of new IPSAS on Leases.

(c) Other—Government Finance Statistics (GFS)

- 4.5 The IPSASB supports the reduction of unnecessary differences between GFS and IPSAS in the development of new IPSASs and revisions to existing IPSASs. The IPSASB's policy paper *Process for Considering GFS Reporting Guidelines during Development of IPSASs* (2014) guides the process.
- 4.6 Government Finance Statistics Manual 2014 (GFSM 2014) classifies leases based on the distinction between legal and economic ownership. According to paragraph A4.4 of GFSM 2014, "the legal owner of resources is the institutional unit entitled by law and sustainable under the law to claim the benefits associated with the asset. By contrast, the economic owner of resources is entitled to claim the benefits associated with the use of the asset in the course of an economic activity by virtue of accepting the associated risks."
- 4.7 Based on this approach, GFSM 2014 identifies three types of leases¹⁵:
- (a) **Operating leases** – Are agreements for the use of nonfinancial assets, except natural resources. There is no change of economic ownership as the legal owner continues to be the economic owner.
 - (b) **Resource leases** – Are agreements for the use of natural resources, such as land and radio spectrum. Similar to operating leases, there is no change of economic ownership.
 - (c) **Financial leases** – Are agreements for the use of all non-financial assets, including natural resources under some circumstances.
- 4.8 Staff notes that, although GFSM 2014 has a different classification approach from IPSAS 13 and IAS 17, generally GFSM 2014 applies the same lease accounting as in IPSAS 13 and IAS 17 for recognition and measurement. Staff is of the view that adoption of the new lessee accounting model in IFRS 16 will increase the differences with GFSM 2014. These differences may be temporary, if the IFRS 16 lessee accounting model is adopted in the next revision of the GFS manuals¹⁶. If GFS does not apply the new lessee accounting model, then there may be a permanent difference between IPSAS and GFS.
- 4.9 Staff notes that IPSAS 13 is aligned with IAS 17 rather than with GFS. As IFRS 16 was published after GFSM 2014, staff recommends that the IPSASB does not consider GFS reporting guidelines in the development of this project further. However, when the new IPSAS on Leases is published, staff recommends that any differences related to the recognition and measurement of leases are should be included in the IPSAS/GFS Tracking Table.

¹⁵ Paragraphs A4.6–A4.17 of GFSM 2014 provides further guidance on how to classify a lease.

¹⁶ The revision of the GFS manuals are still some years away. The GFSM 2014 aims to be consistent with the *System of National Accounts, 2008 (SNA)*. Paragraph 13 of IPSASB Policy Paper *Process for Considering GFS Reporting Guidelines during Development of IPSASs* states that "Scope to reduce differences through changes to the GFS reporting guidelines largely depends on the changes identified not adversely affecting the guidelines' consistency with the SNA".

- 4.10 Staff is aware that the statistical community is following the recent IASB's developments in lease accounting very closely. In the context of revision of 2008 SNA, the statistical community will discuss in the near future, whether and, if so, the new lease accounting that the IASB has developed will be addressed.

5. Development Process, Project Timetable and Project Output

(a) Development Process

- 5.1 The development of outputs will be subject to the IPSASB's formal due process. The approval of the ED will be subject to the usual IPSASB voting rules. As the project progresses, regular assessments will be made to confirm the proposed path in the project timetable remains the most appropriate.
- 5.2 [Appendix A—Leases Project Timetable](#) shows a proposed project timetable (assuming initiation of the project in June 2016) and contingent on future decisions over the project. A first Issues Paper will be discussed at the June 2016 meeting after approval of the project brief.
- 5.3 Staff proposes to split the review of responses into two sessions (December 2017 and March 2018). Approval of a new IPSAS on Leases is projected for June 2018 with publication in July 2018.

(b) Project output

- 5.5 The initial output will be an ED converged with IFRS 16. Following analysis of the responses to the ED a new IPSAS on Leases will be issued.

6. Resources Required

(a) Task Based Group

- 6.1 A Task Based Group will advise staff in the development of this project.

(b) Staff

- 6.2 It is envisaged that 0.4 Full Time Equivalent (FTE) will be required to resource the project.

(c) Factors that might add to complexity and length

- 6.3 Factors that could add to the complexity and length of the project are the need to align with the Revenue project on sale and leaseback and identification of public sector specific reasons to depart from IFRS 16.

7. Important Sources of Information

- 7.1 The principal information sources will be IFRS 16 and the *Conceptual Framework*.

APPENDIX A – LEASES PROJECT TIMETABLE

Meeting		Objective
2016	June	<ol style="list-style-type: none"> 1. Review and approval of Project Brief 2. Lessee: applicability of IFRS 16 recognition and measurement requirements to public sector financial reporting (except reassessment of the lease liability and lease modifications) 3. “Peppercorn” leases 4. Lessor: applicability of IFRS 16 recognition requirements to public sector financial reporting
	September	<ol style="list-style-type: none"> 1. Objective, Scope and Definitions (including “peppercorn” leases) 2. Identifying a lease: Lease versus Service versus Service Concessions 3. Lessee: Measurement and reassessment of the lease liability and lease modifications 4. Lessor: Recognition and measurement (if the IPSASB agrees with symmetry in lease accounting) or only measurement (if the IPSASB agrees to retain the dual model) 5. Presentation: Lessee and lessor 6. Sale and Leaseback Transactions
	December	<ol style="list-style-type: none"> 1. Disclosures: Lessee and Lessor (including “peppercorn” leases) 2. Terminology: Conceptual Framework 3. Application Guidance 4. Effective date and transition 5. Review of first draft ED
2017	March	<ol style="list-style-type: none"> 1. Review of draft ED 2. Approval of ED
	December	<ol style="list-style-type: none"> 3. Review of Responses: Objective, Scope and Exemptions 4. Review of Responses: Identifying a lease 5. Review of Responses: Recognition and measurement—Lessee and lessor
2018	March	<ol style="list-style-type: none"> 1. Review of Responses: Presentation—Lessee and lessor (including peppercorn leases) 2. Review of Responses: Disclosures—Lessee and Lessor (including peppercorn leases) 3. Review of Responses: Sale and Leaseback Transactions 4. Review of Responses: Terminology—Conceptual Framework
	June	<ol style="list-style-type: none"> 1. Review of draft IPSAS 2. Approval of new IPSAS

Lessee – Applicability of IFRS 16 recognition and measurement requirements to public sector financial reporting

Question

1. Does IPSASB agree with staff's analysis on the applicability of IFRS 16 recognition and measurement requirements on lessee accounting to public sector financial reporting?

Detail

Rules of the Road—Step 1: Are there public sector issues that warrant departure?

2. According to the *Rules of the Road* “the IPSASB develops accrual-based International Public Sector Accounting Standards (IPSASs) to address public sector financial reporting issues in two different ways:
 - By addressing public sector financial reporting issues (a) that have not been comprehensively or appropriately dealt with in existing International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB), or (b) for which there is no related IFRS; and
 - By developing IPSASs that are converged with IFRSs by adapting them to the public sector context.”
3. IAS 17, *Leases* is a converged standard with IPSAS 13, *Leases*. IFRS 16, *Leases* introduces a single lessee accounting model (the right-of-use model) with different recognition and measurement requirements that previously existed in IAS 17. Therefore, staff will analyze IFRS 16 accounting requirements by addressing public sector financial reporting issues (i) that have not been comprehensively or appropriately dealt with in IFRS 16 or (ii) by adapting IFRS 16 to the public sector context.
4. Staff analyzed the following sections and paragraphs of IFRS 16's requirements on lessee accounting
 - (a) Recognition exemptions: Paragraphs 5-8 and B3-B8; and
 - (b) Recognition and measurement: Paragraphs 22-38¹⁷.
5. Staff identified the following changes in lessee accounting in IFRS 16 in comparison with IPSAS 13:
 - (a) Recognition of the right-of-use of the underlying asset (the *right-of-use asset*), with optional exception for short-term leases and leases for which the underlying asset is of low value¹⁸;
 - (b) Recognition as a lease liability the obligation to make the lease payments (the *lease liability*)¹⁹;

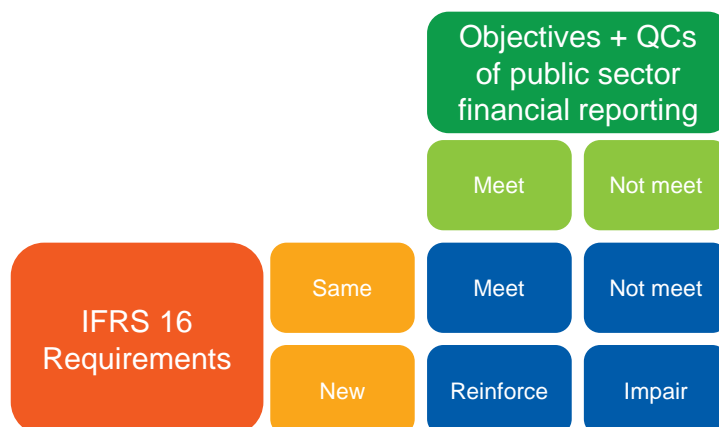
¹⁷ Paragraphs 39-46 of IFRS will be analyzed at a later meeting

¹⁸ According to IPSAS 13, if the lease is classified as a finance lease, then the lessee recognizes the underlying asset and not the right-of-use asset.

¹⁹ According to IPSAS 13, (i) if the lease is classified as a finance lease, then the lessee recognizes the lease liability; (ii) if the lease is classified as an operating lease, then the lessee does not recognize the lease liability.

- (c) Measurement of the right-of-use asset at cost²⁰; and
 - (d) Measurement of the lease liability at the present value of the lease payments that are not paid at the commencement date^{21 22}.
6. Table 1 below provides a summary of staff's methodology for analyzing the changes in lessee accounting in IFRS 16 in comparison with IPSAS 13.

Table 1 – Methodology Summary



7. Staff has evaluated the impact of IFRS 16 requirements against the current requirements in IPSAS 13 on the extent to which they reinforce or impair achievement of the objectives of financial reporting and meet the qualitative characteristics (QCs).
8. A positive evaluation means that the requirements of IFRS 16, where different from IPSAS 13, meet or reinforce the objectives or the QCs of public sector financial reporting. A negative evaluation means that the requirements do not meet or impair the objectives or the QCs of public sector financial reporting. Table 2 provides the staff's analysis.

Table 2 – Lessee—Applicability of IFRS 16 to public sector financial reporting

Criteria to meet public sector financial reporting	Recognition of the right-of-use asset	Recognition of the lease liability	Measurement base of the right-of-use asset	Measurement base of the lease liability ²³
I – Objectives				

²⁰ According to IPSAS 13, if the lease is classified as a finance lease, then the lessee recognizes the leased asset at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease.

²¹ According to IPSAS 13, if the lease is classified as a finance lease, then the lessee recognizes the lease liability at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease.

²² Staff notes that under IFRS 16 the initial measurement of the lease payments includes variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date. Under, IPSAS 13 contingent rents are recognized as expense of the lessee in the periods in which they occur. Staff considered contingent rents as a measurement issue in the lessee analysis. This also includes penalties.

²³ Staff if of the view that if the right-of-use asset is to be valued at fair value, then the lease liability should also be measured at fair value in order to measure and recognize the subsidized component of the lease in the case of "peppercorn" leases (see Agenda Item 7.3—Lessee—"Peppercorn" Leases for more details). Staff also notes that according to paragraph 13 of IPSAS 17 the lease liability is measured at the fair value of the leased property, or if lower, the present value of the minimum lease payments. Therefore, staff chose "meet" because IPSAS 13 also requires cost as a measurement base for leases.

Criteria to meet public sector financial reporting	Recognition of the right-of-use asset	Recognition of the lease liability	Measurement base of the right-of-use asset	Measurement base of the lease liability ²³
Accountability	Reinforces <i>accountability</i> because the public sector entity always recognizes the right-of-use of the underlying asset with material impact in the statement of financial position.	Reinforces <i>accountability</i> because the public sector entity always recognizes the liabilities related to the right-of-use of the underlying asset that is used in service delivery to constituents in the long-term with material impact in the statement of financial position.	Impairs <i>accountability</i> , unless fair value is used, because there are leases in the public sector that are at no cost or at nominal value In such case the value of the right-of-use asset is understated and the subsidized component not recognized.	Meets <i>accountability</i> because, as “the amount of the future payment is discounted so that, at the time a liability is first recognized, the present value of the lease payments that are not paid at the commencement date represents the value of the amount received ” ²⁴ . It also enables public sector entities to be accountable for the resources entrusted to them at the reporting date.
Decision-making	Reinforces <i>decision-making</i> because the approach facilitates increased focus on the management of public sector entity’s assets.	Reinforces <i>decision-making</i> because the recognition of lease liability enables a more focused <i>decision-making</i> in the management of public sector entity’s liabilities.	Impairs <i>decision-making</i> , unless fair value is used, because the historical cost of right-of-use asset does not provide information about operational ²⁵ and financial capacity ²⁶ of right-of-use asset at no cost or at nominal value and the amount of donation received.	Meets <i>decision-making</i> because the present value of the lease payments that are not paid at the commencement date informs users of general purpose financial reports (GPFs) about the liabilities that are “to be settled at stated terms” ²⁷ .
II – Qualitative characteristics				
Relevance	Reinforces <i>relevance</i> because the approach always provides confirmatory value about the economic nature of resources used and a predictive value about the “sources of the resources that are intended to be allocated to providing services in the future” ²⁸ .	Reinforces <i>relevance</i> because the recognition of the lease liability has a confirmatory value about the source of financing of the right-of-use asset.	Impairs <i>relevance</i> , unless fair value is used, because the historical cost has no confirmatory value about the market value of right-of-use asset acquired at no cost or at nominal cost and the donation component.	Meets <i>relevance</i> because the present value of the lease payments that are not paid at the commencement date has a confirmatory value about the amount of financing of the right-of-use asset.
Faithful Representation	Reinforces <i>faithful representation</i> because the approach provides a more faithful <i>representation</i> of the substance of the underlying transaction: based on control of a right-of-use asset and not the underlying asset.	Reinforces <i>faithful representation</i> because the recognition of the lease liability provides a more faithful <i>representation</i> of the substance of the underlying transaction: financing of the right-of-use asset and not of the underlying asset.	Impairs <i>faithful representation</i> , unless fair value is used, because the historical cost of the right-of-use asset fails to measure the right-of-use asset acquired at no cost or at nominal cost and the donation component.	Meets <i>faithful representation</i> because the present value of the lease payments that are not paid at the commencement date provides complete information about the financing of the right-of-use asset.

²⁴ Paragraph 7.72 of the *Conceptual Framework*

²⁵ See paragraphs 7.17 and 7.33 of the *Conceptual Framework*.

²⁶ See paragraphs 7.18 and 7.34 of the *Conceptual Framework*.

²⁷ Paragraph 7.73 of the *Conceptual Framework*

²⁸ Paragraph 3.8 of the *Conceptual Framework*

Criteria to meet public sector financial reporting	Recognition of the right-of-use asset	Recognition of the lease liability	Measurement base of the right-of-use asset	Measurement base of the lease liability ²³
Understandability	Reinforces <i>understandability</i> about the economic nature of the assets used in service delivery: the lessee has the control of the right-of-use asset and not control of the underlying asset.	Reinforces <i>understandability</i> about the financing activity of the lessee's assets used in service delivery: it is financing of the lessee's right-of-use asset and not of the underlying asset.	Impairs <i>understandability</i> , unless fair value is used, because the historical cost of the right-of-use asset fails to measure the right-of-use asset acquired at no cost or at nominal cost and the donation component.	Meets <i>understandability</i> because the present value of the lease payments that are not paid at the commencement date provides information about the financing of the right-of-use asset.
Timeliness	Public sector entities will have to provide financial information on leases as financing at the same time as other financing activities.			
Comparability	Reinforces <i>comparability</i> between public sector entities that lease assets and public sector entities that purchase assets.	Reinforces <i>comparability</i> between public sector entities that lease assets and public sector entities that obtain financing to purchase assets	Impairs <i>comparability</i> , unless fair value is used, because the historical cost of the right-of-use asset fails to compare public sector entities that purchase right-of-use asset at market value with public sector entities that purchase the right-of-use asset at no cost or at nominal cost and the donation component.	Meets <i>comparability</i> because the present value of the lease payments that are not paid at the commencement date enables to compare public sector entities that obtain financing of the right-of-use asset with public sector entities that obtain financing to purchase assets.
Verifiability	Reinforces <i>verifiability</i> because the recognition of the right-of-use asset enables to demonstrate and assure users the right-of-use assets that are used in service delivery.	Reinforces <i>verifiability</i> because the recognition of the lease liability enables to demonstrate and assure users the sources of financing of the right-of-use assets that are used in service delivery.	Impairs <i>verifiability</i> , unless fair value is used, because the historical cost of the right-of-use asset fails to measure the value of the right-of-use asset purchased at no cost or at nominal cost and the donation component.	Meets <i>verifiability</i> because the present value of the lease payments that are not paid at the commencement date can be directly verified through the lease contract.
III – Undue cost or effort				
	No foreseen undue cost or effort.			
IV – Consistency with the <i>Conceptual Framework</i>				
Elements	Consistent with the <i>Conceptual Framework</i> because the right-of-use item meets the definition of an asset ²⁹ .	Consistent with the <i>Conceptual Framework</i> because the lease liability meets the definition of a liability ³⁰ .	–	–
Recognition	Consistent with the <i>Conceptual Framework</i> because the right-of-use asset meets the recognition criteria ³¹ .		–	–
Measurement	–	–	Consistent with the <i>Conceptual Framework</i> because the measurement basis of historical cost for assets ³² is identified in the Framework. However, historical cost	Consistent with the <i>Conceptual Framework</i> because the measurement base of historical cost for

²⁹ See paragraphs 5.6-5.13 of the *Conceptual Framework*.

³⁰ See paragraphs 5.14-5.26 of the *Conceptual Framework*.

³¹ See paragraph 6.2 of the *Conceptual Framework*.

³² See paragraphs 7.13-7.21 of the *Conceptual Framework*.

Criteria to meet public sector financial reporting	Recognition of the right-of-use asset	Recognition of the lease liability	Measurement base of the right-of-use asset	Measurement base of the lease liability ²³
			is not an appropriate measurement basis to measure “peppercorn” leases.	liabilities ³³ is identified in the Framework.
V – Internal consistency with existing IPSASs				
	Staff did not identify inconsistencies with existing IPSAS			
VI – Consistency with statistical bases				
	N/A ³⁴			

Staff's conclusion

Recognition

9. Staff did not identify any public sector financial reporting reason that warrants departure from IFRS 16's recognition requirements on the applicability of the right-of-use model in lessee accounting.
10. Overall, staff is of the view that the lessee accounting recognition requirements of the right-of-use model better reflects the economics of a lease than the model of risks and rewards incidental to ownership because:
 - (a) The lessee **no longer** recognizes an underlying asset that it does not control, as in requirements in IPSAS 13 for finance lease;
 - (b) The lessee **always** recognizes an asset (the right-of-use asset), unlike in IPSAS 13 for operating leases;
 - (c) The lessee **always** recognizes the obligations resulting from the lease contract as liabilities, unlike in IPSAS 13 for operating leases; and
 - (d) The right-of-use model **prevents** arbitrage, gaming and information asymmetry, and improves comparability between public sector entities that lease assets and public sector entities that purchase assets.

Recognition exemptions

11. IFRS 16 permits a lessee to elect not to recognize the right-of-use asset of short-term leases³⁵ and leases for which the underlying asset is of low value³⁶. "The IASB concluded that the benefits of requiring a lessee to apply all of the requirements in IFRS 16 to short-term leases do not outweigh the associated costs."³⁷
12. Staff did not identify a public sector financial reporting reason that would warrant different recognition exemptions from IFRS 16. However, the IPSASB might consider requiring the recognition exemptions, instead of only permitting them, in order to increase comparability between public sector entities.

³³ See paragraphs 7.70-7.73 of the *Conceptual Framework*.

³⁴ See paragraphs 4.5-4.10 of the Project Brief, *Leases*

³⁵ A lease that, at the commencement date, has a lease term of 12 months or less. A lease that contains a purchase option is not a short-term lease.

³⁶ The assessment of whether an underlying asset is of low value is performed on an absolute basis when it is new regardless of the age of the asset being leased.

³⁷ Paragraph BC87 of IFRS 16

13. The following table provided the advantages and disadvantages of requiring instead of only permitting recognition exemptions.

Table 2 – Advantages and disadvantages of requiring recognition exemptions

Advantages	Disadvantages
<ul style="list-style-type: none"> Increased comparability between public sector entities Increased cost relief in the application of the new IPSAS on Leases It is still within the <i>Rules of the Road</i> 	<ul style="list-style-type: none"> Divergence with IFRS 16 In low value leases that last a number of years may impact negatively reliability and accuracy of financial statements

14. Staff also notes that comparability between public sector entities and private sector entities will always depend on whether those entities elect the recognition exemptions.
15. Staff is of the view that making the above recognition exemptions requirements, rather than options, would enhance comparability between public sector entities and also provide cost relief to entities applying a new IPSAS on Leases. Such an approach does not impair comparability with private sector entities, as such entities have a choice of accounting policies for recognition under IFRS 16. This approach responds to the views of those who advocate limiting options and is consistent with paragraph i) of Step 3 of the *Rules of the Road*.
16. However, in the case of low value leases that lasts a number of years can requiring recognition exemption can impact negatively the reliability and accuracy of financial statements. The Task Based Group on Leases considered that for the recognition exemptions, the IPSASB will need to consider whether comparability or reliability and accuracy are more important than accuracy public sector financial reporting.

Measurement

17. IFRS 16 does not address appropriately the public sector financial reporting issues that arise with measurement of “peppercorn” leases. [Agenda Item 7.3—“Peppercorn” leases](#) addresses the geography of the issue, i.e., where it should be addressed peppercorn leases in IPSASB’s literature. At the September meeting, staff will address the measurement requirements of the right-of-use asset and lease liability, together with “peppercorn” leases.

Staff’s recommendation

18. Staff recommends that the IPSASB:
- Adopts the recognition requirements of IFRS 16’s right-of-use model in lessee accounting; and
 - Consider whether recognition exemptions should be a requirement or an option.

Rules of the Road—Step 2: Should a separate public sector project be initiated?

19. If the IPSASB agrees with staff’s recommendation to require rather than to permit the IFRS 16 recognition exemptions, the *Rules of the Road* requires an assessment of whether to amend an IASB document or to initiate a separate public sector specific project.
20. Staff did not identify a persuasive case for initiating a public sector specific project on recognition exemptions.

Staff's recommendation

21. Therefore, staff recommends that the IPSASB should not initiate a public sector specific project.

Rules of the Road—Step 3: Modify IASB documents

22. If the IPSASB decides to require recognition exemptions instead of permitting them, *Step 3: Modify IASB documents* of the *Rules of the Road* allows modifications “to be made to address the public sector issue that triggered the amendment”³⁸.

23. The elimination of the option on recognition exemption is covered by paragraph iii) of Step 3.

Decision required

Does the IPSASB agree with staff's recommendation to:

- Adopt the recognition requirements of the right-of-use model in lessee accounting in the new IPSAS on Leases?
- Consider whether recognition exemptions should be a requirement or an option in the new IPSAS on Leases for short-term leases and leases for which the underlying asset is of low value?

³⁸ Page 5 of *Process for Reviewing and Modifying IASB Documents*

Lessee—“Peppercorn” leases

Question

1. Does the IPSASB agree with staff’s analysis of “peppercorn” leases?

Detail

Introduction

2. Quite often public sector entities and international organizations enter into leases on nominal or subsidized terms (also called “peppercorn” leases) for the whole period of use of the underlying asset. “Peppercorn” leases usually occur between public sector entities and between international organizations. For the purpose of this project, staff will consider “peppercorn” leases all leases with nominal, reduced or rent-free terms, i.e., all leases that are not exchange transactions as defined in IPSASs Glossary of Defined Terms³⁹. IFRS 16 only addresses leases that are not at market values in the context of a sale and leaseback transaction.
3. IFRS 16 requires that the lease asset and liability are measured at cost⁴⁰. Applying IFRS 16 measurement requirements to “peppercorn” leases will lead to an understatement of the lease asset and fails to recognize the subsidy from the lessor to the lessee in the financial statements of the lessee and of the lessor.
4. Leases can be envisaged along a spectrum. At one end of the spectrum are leases with no consideration, i.e., no present obligation exists to make payments to the lessor. These types of leases are in substance a grant or a donation from the lessor to the lessee.
5. At the other end of the spectrum are leases that are exchange transactions, i.e., the lessee receives the lease asset and directly gives approximately equal value (in cash or other) to the lessor in exchange. IFRS 16 only covers these types of leases.
6. Between the two ends of the spectrum there are leases for a nominal value, i.e., such as one dollar/euro per year or month, to be exchanged for the right to use the underlying asset. It can be argued that this type of lease is in substance a grant or a donation, although it has an element of repayment the obligation.
7. There are also leases that are more than one dollar/euro but less than fair value. In this case there is consideration, but it is below fair value.

Where to “address” peppercorn leases in IPSASs?

8. Staff has identified two options for addressing “peppercorn” leases:
 - (a) **Option 1**—Include “peppercorn” leases within the scope of the new IPSAS on Leases; or
 - (b) **Option 2**—Include “peppercorn” leases explicitly within the scope of IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)* and in IPSASB’s current projects on non-exchange expenses and revenue.
9. Table 1 below provides an overview of arguments for each option:

³⁹ Transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

⁴⁰ Paragraphs 23, 24, 26 and 27 of IFRS 16

Table 1 – Preliminary Evaluation of Options for "Peppercorn" Leases

Criteria	Option 1	Option 2
Exchange transaction vs Non-exchange transaction	<ul style="list-style-type: none"> A "peppercorn" lease is still a lease even if it is for nil, nominal or reduced value and, therefore, it should be addressed in the lease standard 	<ul style="list-style-type: none"> A "peppercorn" lease is in substance a grant or donation and, therefore, it should be addressed only in IPSAS 23 and in IPSASB's current projects on non-exchange expenses and revenue
Sector neutral vs sector specific approach to the definition of a lease⁴¹	<ul style="list-style-type: none"> The public sector can have transactions that only occur in the public sector and, therefore, the definition of a lease should reflect a more neutral approach to lease accounting 	<ul style="list-style-type: none"> IFRS 16 is focused on leases that typically occur in the business sector, and, therefore, its definitions are sector specific and focused on exchange transactions. The new IPSAS on Leases should only address leases that are exchange transactions.
Explicit requirements vs professional judgment	<ul style="list-style-type: none"> IPSASs should explicitly address transactions that are typical in the public sector and in international organizations 	<ul style="list-style-type: none"> Leases are not explicitly addressed in IPSAS 23 and, therefore, professional judgment can be used to determine the appropriate accounting using the principles in IPSAS 23
Concentration vs dispersion of subject in IPSASs	<ul style="list-style-type: none"> The accounting treatment of all leases should be included in the new IPSAS on Leases and the subsidized component of "peppercorn" leases should be included in IPSAS 23 	<ul style="list-style-type: none"> IPSAS 23 already provides guidance on recognition⁴² and measurement⁴³ of assets acquired through non-exchange transactions. Such guidance can be applicable to "peppercorn" leases

3.47 Option 1 has the advantage of addressing all types of leases, including "peppercorn" leases, in the leases project but has the disadvantage of diverging with IFRS 16 in the definition of a lease (the term "in exchange for consideration" would have to be removed) and in the measurement requirements (from cost to fair value for all leases or only for "peppercorn" leases⁴⁴). Option 1 is also consistent with the approach taken by the IPSASB on concessionary loans in IPSAS 29, *Financial Instruments: Recognition and Measurement* and include specific requirements in IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)* to address the non-exchange component of concessionary loans⁴⁵.

3.48 Option 2 implies that this project would only address leases arising from exchange transactions. Such an approach has the advantage that the definition of a lease and the measurement requirements would be similar to IFRS 16. However, it has the disadvantage of not addressing a common public sector specific transaction in the same IPSAS on Leases.

⁴¹ The IFRS 16 definition of a lease is: "A contract, or part of a contract, that conveys the right to use an asset (the **underlying asset**) for a period of time in exchange for consideration."

⁴² IPSAS 23 deals with initial recognition of assets and liabilities acquired in a non-exchange transaction. However, IPSAS 23 does not prescribe subsequent measurement or derecognition of assets and liabilities acquired in a non-exchange transaction.

⁴³ Under IPSAS 23 assets acquired in a non-exchange transaction are initially measured at fair value and liabilities arising from a non-exchange transaction are measured by the best estimate of the amount required to settle the present obligation at the reporting date.

⁴⁴ The measurement base of peppercorn leases will be discussed at the September meeting.

⁴⁵ See paragraphs 105A and 105B of IPSAS 23.

- 3.49 On balance, staff is of the view that the arguments in Option 1 outweigh those in Option 2 and recommends that the IPSASB proceeds with Option 1.
- 3.50 Staff notes that if the IPSASB decides to include "peppercorn" leases within the scope of this project, then the IPSASB will need to change the measurement basis of leases from cost to fair value. If this is the IPSASB's decision, staff will bring proposals to address the change of measurement basis from cost to fair value to the September meeting.

Decision required

Does the IPSASB agree with staff's recommendation to:

- (a) Address "peppercorn" leases in this project (Option 1); and
- (b) Include specific requirements in IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)* to address the non-exchange component of the lease (similar to concessionary loans)?

Lessor – Applicability of IFRS 16 recognition requirements to public sector financial reporting

Questions

1. Does the IPSASB agree with staff's analysis of the non-applicability of IFRS 16 recognition requirements on lessor accounting to public sector financial reporting?
2. Does the IPSASB agree with staff's recommendation to apply the right-of-use model to lessor accounting, as the mirror of accounting for the IFRS 16 lessee's?

Detail

Rules of the Road—Step 1: Are there public sector issues that warrant departure?

3. According to the *Rules of the Road* “the IPSASB develops accrual-based International Public Sector Accounting Standards (IPSASs) to address public sector financial reporting issues in two different ways:
 - By addressing public sector financial reporting issues (a) that have not been comprehensively or appropriately dealt with in existing International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB), or (b) for which there is no related IFRS; and
 - By developing IPSASs that are converged with IFRSs by adapting them to the public sector context.”
4. IAS 17, *Leases* is a converged standard with IPSAS 13, *Leases*. IFRS 16, *Leases* retains the recognition and measurement⁴⁶ requirements that previously existed in IAS 17.
5. Staff notes that with the introduction of the right-of-use model in lessee accounting and the retention of the dual model in lessor accounting, there is a lack of symmetry in analyzing the economics of a lease from a conceptual point of view. As a consequence, the lack of symmetry is reflected in different recognition requirements in lessor accounting of IFRS 16 than in the hypothetical case of the lessor also applying the right-of-use model.
6. Therefore, staff is of the view that the recognition requirements of lessor accounting in IFRS 16 should be assessed on whether it is still applicable to public sector financial reporting and compatible with the right-of-use model in lessee accounting. If the answer is positive, then no adaption to public sector context is required in the development of the new IPSAS on *Leases*; if the answer is negative, then IFRS 16 needs to be adapted to the public sector context in the development of the new IPSAS on *Leases*.
7. In this process, staff will assess the requirements in lessor accounting in the light of the non-application of the right-of-use model to the lessor accounting. The process has two steps:
 - (a) Identify the requirements in IFRS 16 for lessor accounting that are not based on the right-of-use model; and
 - (b) Apply the *Rules of the Road* to the accounting requirements identified in (a).

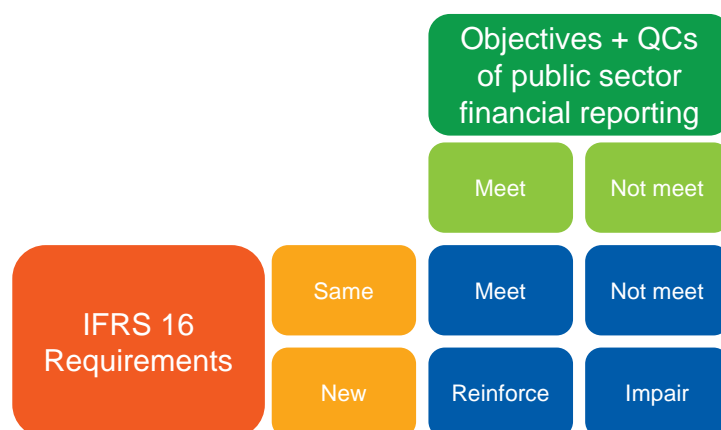
⁴⁶ Staff notes that under IFRS 16 the initial measurement of the lease payments includes variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date. Under, IPSAS 13 contingent rents are recognized as revenue of the lessor in the periods in which they occur. Staff considered contingent rents as a measurement issue in the lessor analysis.

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8. In this way, the lessor accounting model can be simultaneously assessed against the right-of-use model applied to the lessor and the *Rules of the Road*.
9. The lessor accounting model in IFRS 16 classifies leases as finance lease and operating lease and both have different recognition requirements.
10. Staff identified the following recognition differences in lessor accounting model in IFRS 16 in comparison with the right-of-use model applied to the lessor:
 - (a) **Finance lease**—derecognition of the underlying asset and non-recognition of the unearned revenue (liability)⁴⁷;
 - (b) **Operating lease**—non-recognition of the lease receivable and the finance revenue.
11. Staff analyzed the following sections and paragraphs of IFRS 16:
 - (a) Finance leases: Paragraphs 67-80;
 - (b) Operating leases: Paragraphs 81-86 and B53-B58.
12. Staff did not analyze the classification of leases in lessor accounting because this agenda item is only related to recognition requirements as a result of classification. However, staff acknowledges that the conclusions and recommendations on lessor accounting requirements will affect the IFRS 16 section on classification⁴⁸.
13. Staff did not identify any change in lessor accounting in IFRS 16 when comparing with IPSAS 13 regarding the recognition of the net investment in the lease and derecognition of the underlying asset.
14. Table 1 below provides a summary of staff's methodology to analyze the differences in lessor accounting in IFRS 16 when comparing with the right-of-use model applied to the lessor.

Table 1 – Methodology Summary



15. Staff has evaluated the impact of IFRS 16 requirements against the current requirements in IPSAS 13 on the extent to which they reinforce or impair achievement of the objectives of financial reporting and meet the qualitative characteristics (QCs).

⁴⁷ The non-recognition of the unearned revenue (liability) is also be applicable to operating leases. For simplification purposes, staff only analyzed the non-recognition of the unearned revenue (liability) in finance leases, but the conclusions can be applicable in the context of operating leases.

⁴⁸ Paragraphs 61-66 of IFRS 16

16. A positive evaluation means that the requirements of IFRS 16, where different from IPSAS 13, meet or reinforce the objectives or the QCs of public sector financial reporting. A negative evaluation means that the requirements do not meet or impair the objectives or the QCs of public sector financial reporting. Table 2 provides the staff's analysis.

Table 2 – Lessor–Applicability of IFRS 16 to public sector financial reporting

Criteria to meet public sector financial reporting	Finance lease		Operating lease	
	Derecognition of the underlying asset ⁴⁹	Non recognition of unearned revenue as a liability ⁵⁰	Non-recognition of the lease receivable	Non-recognition of the finance revenue
I – Objectives				
Accountability	Impairs accountability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing in the statement of financial position the underlying asset that it controls, the public sector entity does not provide “information about the entity’s management of the resources entrusted to it for the delivery of services to constituents and others, and its compliance with legislation, regulation, or other authority that governs its service delivery and other operations.” ⁵¹	Impairs accountability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing in the statement of financial position the unearned revenue, the public sector entity fails to provide information about revenue that will be recognized in future periods which affects an “entity’s service delivery achievements during the reporting period, and its capacity to continue to provide services in future periods” ⁵² from an economic perspective.	Impairs accountability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the lease receivable, the public sector entity does not provide “information about the entity’s management of the resources entrusted to it for the delivery of services to constituents and others, and its compliance with legislation, regulation, or other authority that governs its service delivery and other operations.” ⁵³	Impairs accountability (unless the new IPSAS on Leases adopts symmetry) because it is not recognized the finance revenue component of granting financing to the lessee related to right-of-use an asset.
Decision-making	Impairs decision-making (unless the new IPSAS on Leases adopts symmetry) because users of the statement of financial position do not have information about the economic benefits embedded in the underlying asset from the cost, sale, re-lease or use of the underlying asset at the end of the lease term that would enable them to “make decisions about whether to provide resources to support the current and future activities of the	Impairs decision-making (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing in the statement of financial position the unearned revenue, users of the statement of financial position do not have information about revenue that will be recognized in future periods which affects “decisions about whether to provide resources to support the current and future activities of the government or other public sector entity.” ⁵⁵	Impairs decision-making (unless the new IPSAS on Leases adopts symmetry) because users of the statement of financial position do not have information about the economic benefits embedded in the lease receivable from the cost, sale, securitization and future payments from the lessee during the lease term that would enable them to “make decisions about whether to provide resources to support the current and future	Impairs decision-making (unless the new IPSAS on Leases adopts symmetry) because users of the statement of financial performance do not have information about the revenue obtained through financing transactions.

⁴⁹ At the same time, the lessor recognizes the net investment in the lease, which is the gross investment in the lease discounted at the interest rate implicit in the lease. The gross investment in the lease is the aggregate of: (a) the minimum lease payments receivable by the lessor under finance lease; and (b) any unguaranteed residual value accruing to the lessor.

⁵⁰ In IPSAS 13 the entry of the unearned revenue is presented together with the gross investment in the lease as a credit.

⁵¹ Paragraph 2.8 of the *Conceptual Framework*

⁵² Paragraph 2.8 of the *Conceptual Framework*

⁵³ Paragraph 2.8 of the *Conceptual Framework*

⁵⁵ Paragraph 2.9 of the *Conceptual Framework*

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Criteria to meet public sector financial reporting	Finance lease		Operating lease	
	Derecognition of the underlying asset ⁴⁹	Non recognition of unearned revenue as a liability ⁵⁰	Non-recognition of the lease receivable	Non-recognition of the finance revenue
	government or other public sector entity. ⁵⁴		activities of the government or other public sector entity. ⁵⁶	
II – Qualitative characteristics				
Relevance	Impairs relevance (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing in the statement of financial position the underlying asset that it controls, the public sector entity no longer provides a confirmatory value about the type of resources used and a predictive value about the “sources of the resources that are intended to be allocated to providing services in the future.” ⁵⁷	Impairs relevance (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing in the statement of financial position the unearned revenue, the public sector entity does not provide a confirmatory value about the type of resources used and a predictive value about the “sources of the resources that are intended to be allocated to providing services in the future.” ⁵⁸	Impairs relevance (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the lease receivable, the public sector entity does not provide a confirmatory or predictive value about the economic benefits embedded in the lease contract.	Impairs relevance (unless the new IPSAS on Leases adopts symmetry) because it does not distinguish revenue different predictive values: financing has a constant periodic rate of return and decreasing finance revenue during the lease term versus income from operating leases recognized on a straight-line basis.
Faithful Representation	Impairs faithful representation (unless the new IPSAS on Leases adopts symmetry) because, by derecognizing the underlying asset from the statement of financial position, the public sector entity fails to provide a complete depiction of the leasing phenomenon and does not “depict the substance of the underlying transaction” ⁵⁹ : granting the right-of-use of the underlying asset that it still controls.	Impairs faithful representation (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the unearned revenue in the statement of financial position, the public sector entity fails to provide a complete depiction of the leasing phenomenon and does not “depict the substance of the underlying transaction” ⁶⁰ : acquisition of resources that is related to future periods.	Impairs faithful representation (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the lease receivable, the public sector entity fails to provide a complete depiction of the leasing phenomenon and does not “depict the substance of the underlying transaction” ⁶¹ : the lessor has a right to receive economic benefits from the lessee.	Impairs faithful representation (unless the new IPSAS on Leases adopts symmetry) because it fails to provide a complete depiction of the leasing phenomenon and does not “depict the substance of the underlying transaction” ⁶² : a lease is a financing transaction.
Understandability	Impairs understandability (unless the new IPSAS on Leases adopts symmetry) because, by derecognizing the underlying asset from the statement of financial position, the public sector entity does not enable users to	Impairs understandability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the unearned revenue in the statement of financial position, the public sector entity does not enable users to assess	Impairs understandability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the lease receivable, the public sector entity prevents users to fully	Impairs understandability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the finance revenue component, prevents users to fully understand the economic impact of the

⁵⁴ Paragraph 2.9 of the *Conceptual Framework*

⁵⁶ Paragraph 2.9 of the *Conceptual Framework*

⁵⁷ Paragraph 3.8 of the *Conceptual Framework*

⁵⁸ Paragraph 3.8 of the *Conceptual Framework*

⁵⁹ Paragraph 3.10 of the *Conceptual Framework*

⁶⁰ Paragraph 3.10 of the *Conceptual Framework*

⁶¹ Paragraph 3.10 of the *Conceptual Framework*

⁶² Paragraph 3.10 of the *Conceptual Framework*

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7.4

Criteria to meet public sector financial reporting	Finance lease		Operating lease	
	Derecognition of the underlying asset ⁴⁹	Non recognition of unearned revenue as a liability ⁵⁰	Non-recognition of the lease receivable	Non-recognition of the finance revenue
	distinguish underlying assets that were granted the right-of-use from the assets used by the public sector entity itself in service delivery.	the amount of resources received by the public sector entity that are related to future periods.	understand the leasing activity.	leasing activity as a financing transaction.
Timeliness	-			
Comparability	Impairs comparability (unless the new IPSAS on Leases adopts symmetry) between public sector entities that grant right-of-use an asset and public sector entities that grant the right of access to assets in service concession arrangements and public sector entities that provide services with assets that all control.	Impairs comparability (unless the new IPSAS on Leases adopts symmetry) between public sector entities that grant right-of-use an asset and public sector entities that grant the right of access to assets in service concession arrangements.	Impairs comparability (unless the new IPSAS on Leases adopts symmetry), because, by not recognizing the lease receivable, the public sector entity prevents comparison between lessors that have more/less finance leases than operating leases while all lease contracts gives the right to receive economic benefits from the lessee.	Impairs comparability (unless the new IPSAS on Leases adopts symmetry), because it prevents comparison between lessors that have more/less finance leases than operating leases while all lease contracts are in substance a financing transaction.
Verifiability	Impairs verifiability (unless the new IPSAS on Leases adopts symmetry) because, by derecognizing the underlying asset from the statement of financial position, the public sector entity does not enable to demonstrate and assure users the right-of-use assets that are used in service delivery.	Impairs verifiability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing the unearned revenue in the statement of financial position, the public sector entity does not enable to demonstrate and assure users the unearned revenue that it will be recognized in future periods.	Impairs verifiability (unless the new IPSAS on Leases adopts symmetry), because, by not recognizing the lease receivable the public sector entity, the public sector entity does not “assure users that information in GPFRs faithfully represents the economic and other phenomena that it purports to represent” ⁶³ .	Impairs verifiability (unless the new IPSAS on Leases adopts symmetry) because, by not recognizing finance revenue the public sector entity, the public sector entity does not “assure users that information in GPFRs faithfully represents the economic and other phenomena that it purports to represent” ⁶⁴ .
III – Undue cost or effort				
	<p>There are on-going consolidation issues with public sector entities that account leasing contracts differently depending on whether they are lessee or lessor.</p> <p>Public sector entities that are lessors and lessees in different lease contracts need to interpret two different models for the same economic transaction.</p> <p>Many times public sector entities do not publish consolidated financial statements. In this context, users of financial statements of public sector entities have asymmetrical information about lenders and borrowers within the same economic entity because of the lack of symmetry in lease accounting. As a result, users will have to make adjustments to the financial statements.</p>			
IV – Consistency with the Conceptual Framework				
Elements	Inconsistent with the <i>Conceptual Framework</i> (unless the new IPSAS on Leases adopts symmetry) because the underlying item meets the definition of an asset ⁶⁵ .	Unearned revenue is not a defined element in the <i>Conceptual Framework</i> . During the finalization of the elements chapter of the <i>Conceptual Framework</i> , the IPSASB	Inconsistent with the <i>Conceptual Framework</i> (unless the new IPSAS on Leases adopts symmetry) because the lease receivable meets	Inconsistent with the <i>Conceptual Framework</i> (unless the new IPSAS on Leases adopts symmetry) because the finance revenue meets

⁶³ Paragraph 3.26 of the *Conceptual Framework*

⁶⁴ Paragraph 3.26 of the *Conceptual Framework*

⁶⁵ See paragraphs 5.6-5.13 of the *Conceptual Framework*. Staff is of the view that the rationale provided in paragraphs BC37-BC39 of IFRS 16 is applicable to public sector financial reporting.

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7.4

Criteria to meet public sector financial reporting	Finance lease		Operating lease	
	Derecognition of the underlying asset ⁴⁹	Non recognition of unearned revenue as a liability ⁵⁰	Non-recognition of the lease receivable	Non-recognition of the finance revenue
		accepted "that certain economic phenomena that do not meet the definition of any element may need to be recognized in financial statements in order to meet the objectives of financial reporting" ⁶⁶ and concluded that this "provides the most transparent approach" ⁶⁷ .	the definition of an asset ⁶⁸ .	the definition of revenue ⁶⁹ .
Recognition	Inconsistent with the <i>Conceptual Framework</i> (unless the new IPSAS on Leases adopts symmetry) because the underlying asset meets the recognition criteria ⁷⁰ , and, therefore, it should not be derecognized.	In paragraph BC5.56 of the <i>Conceptual Framework</i> the IPSASB stated that "the circumstances under which other obligations and other resources will be recognized will be determined at standards level and explained in the Bases for Conclusions of specific standards". Staff did not identify an economic reason for not recognizing the unearned revenue in the same way that it is recognized in IPSAS 32 for the grant of a right to the operator model.	Inconsistent with the <i>Conceptual Framework</i> (unless the new IPSAS on Leases adopts symmetry) because the lease receivable meets the recognition criteria ⁷¹ , and, therefore, it should be recognized.	Inconsistent with the <i>Conceptual Framework</i> (unless the new IPSAS on Leases adopts symmetry) because the finance revenue meets the recognition criteria ⁷² , and, therefore, it should be recognized.
Measurement⁷³	–	–	–	–
V – Internal consistency with existing IPSASs				
	Inconsistent with IPSAS 32 (unless the new IPSAS on Leases adopts symmetry) because the grantor never derecognizes the underlying asset in both the liability model and the grant of the right to access model. IPSAS 32 is the mirror accounting of IFRIC 12, <i>Service</i>	Inconsistent with IPSAS 32 (unless the new IPSAS on Leases adopts symmetry) because the grantor always recognizes the unearned revenue (liability) in the grant of the right to access model.	Inconsistent with IPSAS 29 (unless the new IPSAS on Leases adopts symmetry) because leases are in substance financing transactions.	

⁶⁶ Option D in paragraph BC5.49 of the *Conceptual Framework*

⁶⁷ Paragraph BC5.56 of the *Conceptual Framework*

⁶⁸ See paragraphs 5.6-5.13 of the *Conceptual Framework*. Staff is of the view that the rationale provided in paragraphs BC37-BC39 of IFRS 16 is applicable to public sector financial reporting.

⁶⁹ Paragraph 5.29 of the *Conceptual Framework*

⁷⁰ See paragraph 6.2 of the *Conceptual Framework*.

⁷¹ See paragraph 6.2 of the *Conceptual Framework*.

⁷² See paragraph 6.2 of the *Conceptual Framework*.

⁷³ The measurement requirements will be analyzed in the September meeting.

Criteria to meet public sector financial reporting	Finance lease		Operating lease	
	Derecognition of the underlying asset ⁴⁹	Non recognition of unearned revenue as a liability ⁵⁰	Non-recognition of the lease receivable	Non-recognition of the finance revenue
	<i>Concession Arrangements.</i> ⁷⁴			
VI – Consistency with statistical bases				
	N/A ⁷⁵			

Staff's conclusion

17. Staff concludes that the different recognition requirements of the lessor's dual accounting model in IFRS 16 in comparison to the possible application of the right-of-use model to the lessor:
 - (a) **Does not meet** the objectives and QCs of public sector financial reporting;
 - (b) **Are inconsistent** with the *Conceptual Framework*; and
 - (c) **Are inconsistent** with IPSAS 32 and IPSAS 29.
18. Staff notes that the accountability differences identified above is one of the items identified by the *Rules of the Road* that could affect public sector financial reporting.
19. Having reached these conclusions, staff considered the reasons that led the IASB to retain the dual accounting model for lessor accounting in IFRS 16.

IASB's rationale for retaining the dual model in lessor accounting

20. The IASB also "concluded that the lessor's lease receivable and rights retained in the underlying asset both meet the definition of an asset"⁷⁶. However, the IASB stated that "stakeholders observed that:
 - (a) the lessor accounting model in IAS 17 is well understood.
 - (b) most users of financial statements do not currently adjust lessors' financial statements for the effects of leases—indicating that the lessor accounting model in IAS 17 already provides users of financial statements with the information that they need. In addition, investors generally analyse the financial statements of individual entities (and not a lessee and lessor of the same underlying asset). Accordingly, it is not essential that the lessee and lessor accounting models are symmetrical.

⁷⁴ Staff notes that according to BC2 of IPSAS 32 "the IPSASB concluded that the scope of this Standard should be the **mirror of IFRIC 12**, in particular, the criteria under which the grantor recognizes a service concession asset (see paragraphs BC11–BC16). The rationale for this decision is that this approach would require both parties to the same arrangement to apply the same principles in determining which party should **recognize the asset** used in a service concession arrangement. Thus, arrangements in which the criteria for recognition of a service concession asset in paragraph 9 (or paragraph 10 for a whole-of-life asset) are not satisfied, are outside the scope of this IPSAS. The IPSASB considers that this approach minimizes the possibility for an asset to be accounted for by both of the parties, **or by neither party**" [emphasis added]. Staff did not identify an economic reason why these conclusions are not applied to lease accounting.

⁷⁵ See paragraphs 4.5-4.10 of the Project Brief, *Leases* (Agenda Item 7.1)

⁷⁶ Paragraph BC57 of IFRS 16. Paragraphs BC35-BC40 of IFRS 16 explain why the lease receivable and the rights retained in the underlying asset meet the definition of an asset.

- (c) in contrast to lessee accounting, lessor accounting in IAS 17 is not fundamentally flawed and should not be changed solely because lessee accounting is changing.”⁷⁷
21. The IASB also noted that:
- “Some stakeholders also acknowledged that their views on lessor accounting had changed over the life of the Leases project. These stakeholders noted that they had originally suggested that the IASB should address lessor accounting at the same time as lessee accounting. However, in response to the 2013 Exposure Draft, they suggested that no changes should be made to lessor accounting. These stakeholders had changed their views primarily for cost-benefit reasons.”⁷⁸
- “In the light of this feedback, the IASB concluded that requiring a lessor to recognise a lease receivable for all leases would not improve financial reporting to the extent that the benefits from the improvements would outweigh the costs associated with that change.”⁷⁹
22. The IASB had “proposed changes to lessor accounting in the 2010 and 2013 Exposure Drafts that were more symmetrical with the lessee accounting model ultimately included in IFRS 16, because these proposals would have required a lessor to recognise a lease receivable for all (or many) leases.”⁸⁰
23. Staff notes that the IASB published three consultation documents in its project on:
- (a) *Leases—Preliminary Views*⁸¹ issued in March 2009—Only included “some of the issues that will need to be resolved in developing any proposed new standard for lessors”⁸² without any preliminary views because “the IASB decided to defer consideration of lessor accounting and concentrate on developing an improved lessee accounting model”⁸³;
 - (b) Exposure Draft—Leases issued in August 2010⁸⁴—Included proposals for lessor accounting because “Although many of the problems associated with existing lease standards relate to the treatment of operating leases in the financial statements of lessees, keeping the existing lease standards for lessors would be inconsistent with the proposed approach to lessee accounting. It would also be inconsistent with the boards’ proposed approach to revenue recognition, described in their exposure draft *Revenue from Contracts with Customers*”⁸⁵.
 - (c) Exposure Draft—Leases issued in May 2013—Included proposals for lessor accounting because “Although many of the problems associated with existing leases requirements relate to the accounting for operating leases in the financial statements of lessees, retaining the existing lease accounting models for lessors would be inconsistent with the proposed approach to lessee accounting and would result in additional complexity in financial reporting. In addition, the boards decided that it would be beneficial to consider lessor accounting at the same time they are developing proposals on revenue recognition.”⁸⁶

⁷⁷ Paragraph BC61 of IFRS 16

⁷⁸ Paragraph BC62 of IFRS 16

⁷⁹ Paragraph BC63 of IFRS 16

⁸⁰ Paragraph BC60 of IFRS 16

⁸¹ <http://www.ifrs.org/Current-Projects/IASB-Projects/Leases/DPMar09/Documents/DPLLeasesPreliminaryViews.pdf>

⁸² Paragraph 10.1 of Leases—Preliminary Views

⁸³ Paragraph 10.1 of Leases—Preliminary Views

⁸⁴ <http://www.ifrs.org/Current-Projects/IASB-Projects/Leases/ed10/Documents/EDLeasesStandard0810.pdf>

⁸⁵ Page 5 of Exposure Draft—Leases (ED/2010/9)

⁸⁶ Page 5 of Exposure Draft—Leases (ED/2013/6)

Staff's comments on IFRS 16 lessor accounting

24. Staff notes that the reasons provided by the IASB's stakeholders are not related to the economics of a lease nor to any identified fundamental or conceptual flaw in the application of recognition requirements of the right-of-use model to the lessor.
25. Staff also notes that the reasons provided by the IASB's stakeholders are specific to the business environment in which they operate and specific to users' needs in the for-profit sector. The economic environment and users' needs in the for-profit sector may be different from the public sector. For example, it might be difficult for public sector stakeholders to understand different accounting principles for the same transaction.
26. The lack of symmetry in lease accounting also creates asymmetrical information in public sector financial reporting when governments do not publish consolidated financial statements and users have to rely on separate financial statements of individual entities for accountability and decision-making purposes.
27. In this context, users of general purpose financial reports of public sector entities many times do analyze the financial statements of the lessee and lessor of the underlying asset in order to better assess the risks of lending capital and in order to understand who controls the underlying asset for accountability and decision-making purposes. The underlying asset may be used as collateral for borrowing.⁸⁷
28. Staff notes that under IFRS 16, the underlying asset might not be recognized in either the lessor's or the lessee's statement of financial position, if the lessor classifies the lease as a finance lease.
29. Staff also notes that the non-recognition of the underlying asset in either party's statement of financial position could occur under IPSAS 13/IAS 17. However, this would be because of different interpretations by preparers (lessee and lessor) of the same model rather because there are different models for lessee and lessor accounting.
30. The diversity of situations where leasing transactions can be used within the public sector, the frequent existence of lessees and lessors within the public sector (many times the same public sector entity is a lessor and a lessee in different lease contracts), the existence of centralized lessors that managed assets of other public sector entities (under common control or not), and decreasing understandability of the leasing phenomena can be compelling reasons to adopt symmetry in lease accounting. These reasons are reinforced by the economics of the transaction: leases are financings and, therefore, the lessor accounting should mirror the lessee accounting.
31. Recently the Governmental Accounting Standards Board (GASB)⁸⁸ published an Exposure Draft⁸⁹ on lease accounting that proposes the right-of-use model to be applicable to both the lessee and the lessor (symmetry in lease accounting). According to GASB "governmental lessees and lessors should account for the same transaction in a way that mirrors how the other party

⁸⁷ For example: a public sector entity, which is a specialized lessor for the public sector, issues bonds in the capital markets to finance purchases of assets from other public sector entities that will be leased-back. As bonds are issued in the name of the public sector entity and not in the name of the State or guaranteed by the State, lenders may require the underlying asset to be used as collateral for borrowing and understand who, in fact, controls the underlying assets..

⁸⁸ GASB is the independent, private-sector organization based in Norwalk, Connecticut, that establishes accounting and financial reporting standards for U.S. state and local governments that follow Generally Accepted Accounting Principles (GAAP).

⁸⁹ See Exposure Draft, *Leases* at http://www.gasb.org/jsp/GASB/Document_C/GASBDocumentPage?cid=1176167852776&acceptedDisclaimer=true

accounts for it”⁹⁰ and “when the lessor and lessee are both part of the same reporting entity, symmetry in accounting prevents distortion of the total government’s financial position”⁹¹.

32. As the IASB’s stakeholders “changed their views primarily for cost-benefit reasons”⁹² and the IASB decided to retain the lessor dual model that existed in IAS 17 because the improvements to financial reporting “would outweigh the costs associated with such a change”, staff has analyzed the costs and benefits of applying a single model (the right-of-use model) to lease accounting in the public sector:

Table 3 – Costs and benefits of applying symmetry to lessor accounting in the public sector

Costs	Benefits
<ul style="list-style-type: none"> • One-off implementation costs for lessors as for lessees (review of existing lease agreements; staff training; information technology systems changes) • On-going costs of monitoring all leases in the statement of financial position • On-going consolidation issues with commercial public sector entities that apply IFRS (no convergence with IFRS in lessor accounting) 	<ul style="list-style-type: none"> • Represents faithfully the economics of a lease • Achieves the objectives of financial reporting • Provides more transparent, relevant and verifiable information on lease accounting • Provides a better understanding of financing activities within the public sector and between the public sector and the private sector • Improves comparability between public sector entities • Increases simplicity in lease accounting • Improves on-going consolidation of public sector entities that apply IPSASs • Better understandability of leasing arrangements by users of general purpose financial reports based on IPSASs

33. The IPSASB will need to consider whether the benefits of applying symmetry in lease accounting in public sector outweigh its costs.
34. The adoption of symmetrical lease accounting requirements will involve divergence from IFRS 16 for lessor accounting, whereas current lessor accounting requirements in IPSAS 13 are fully converged with those in IAS 17. Therefore, the IPSASB will need to consider whether it is more important to achieve a symmetrical accounting treatment between public sector entities for which IPSASs are designed (if that better meets the objectives and QCs of public sector financial reporting), than maintaining convergence with IFRSs.

Decision required

35. Does the IPSASB agree to adopt the right-of-use model for lessor accounting, as the mirror accounting of IFRS 16 lessee’s right-of-use model, or, conversely, to adopt the IFRS 16’s lessor accounting?

⁹⁰ Paragraph BC58 of GASB’s Exposure Draft, *Leases*

⁹¹ Paragraph BC67 of GASB’s Exposure Draft, *Leases*

⁹² Paragraph BC62 of IFRS 16

PROJECT BRIEF, *LEASES*

(Marked-up version from March 2016 meeting)

1. Introduction

- 1.12 IPSAS 13, *Leases*, was issued in December 2001. It is a converged standard based on International Accounting Standard (IAS) 17, *Leases*.
- 1.13 In January 2016, the IASB issued International Financial Reporting Standard (IFRS) 16, *Leases*, which supersedes IAS 17. It also supersedes three interpretations: IFRIC 4, *Determining whether an Arrangement contains a Lease*, SIC-15, *Operating Leases-Incentives* and SIC-27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.
- 1.14 IFRS 16 introduces “a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value”⁹³. The lessor accounting in IFRS 16 remains substantially the same as in IAS 17. IFRS 16 retains the dual lessor accounting model that previously existed in IAS 17 in which leases are categorized as operating leases and finance leases.
- 1.15 IFRS 16 is effective for annual periods beginning on or after 1 January 2019 with earlier application permitted for entities that apply IFRS 15, *Revenue from Contracts with Customers* at or before the date of initial application of IFRS 16.
- 1.16 Many public sector entities use leasing arrangements for gaining access to ~~the~~ assets, which they use in service delivery. Leasing is a means of obtaining finance, and of reducing an entity's exposure to the risks of asset ownership. The prevalence of leasing, therefore, means that it is important that users have a complete and understandable picture of an entity's leasing activities.
- 1.17 Like IAS 17, lease classification using IPSAS 13 has focused on the extent to which the risks and rewards incidental to ownership of a lease lie with the lessor or the lessee. IPSAS 13 classifies leases as either finance leases or operating leases. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership. For finance leases, the lessee recognizes assets and liabilities in the statement of financial position. For operating leases, the lessee accounts for lease payments as an expense on a straight-line basis over the lease term.
- 1.18 This model has been criticized for failing to meet the needs of users because:
- (a) The resulting financial statements do not always provide a faithful representation of leasing transactions, because they omit resources and obligations that, conceptually, meet the definition of an asset and a liability particularly for operating leases; and
 - (b) The significant difference in recognition ~~of~~[requirements for](#) finance and operating leases has created incentives to structure some transactions as operating leases to achieve off-balance sheet accounting.
- 1.19 The IASB noted that, as a result, many users adjust the amounts reported in a lessee's financial statements to reflect the assets and liabilities arising from off-balance sheet leases, and make other consequential adjustments. However, because of the limited information available, such estimates may be inaccurate. In addition, many other users do not make adjustments. This creates asymmetry and leads to unreliable information in the market.

⁹³ Paragraph IN10 of IFRS 16

1.20 The objective of the project is to develop revised requirements for lease accounting covering both lessees and lessors in order to maintain alignment with the underlying IFRS. The project will result in a ~~revised IPSAS 13 or a~~ new IPSAS that will replace IPSAS 13.

1.21 Because this project is revising or replacing requirements in an existing IPSAS, the scope is clearly defined and it may be less resource intensive than “blue sky” projects.

~~1.21~~ 1.22 Responses to the 2014 strategy consultation supported the ongoing alignment of existing IPSASs with underlying IFRSs. If a project to amend IPSAS 13 in order to align it with IFRS 16 is not undertaken, it will lead to a major divergence in lease accounting between the public sector and the private sector. Unless there are public sector specific reasons for such a divergence, the co-existence of different lessee accounting models for leases will also create additional burdens for consolidation where commercial public sector entities are reporting in accordance with IFRS.

2. Project Rationale and Objectives

(a) Project rationale

2.6 The project rationale is that IAS 17, from which IPSAS 13 was primarily drawn, has been replaced by IFRS 16. Not amending or replacing IPSAS 13 will result in the use of different models for accounting for leases in the public and private sectors.

(b) Objectives to be achieved

2.7 The objective is to issue a ~~revised IPSAS 13 or a~~ new IPSAS on Leases which will be converged with ~~the new~~ IFRS 16.

2.8 The intermediate objective is to produce an Exposure Draft (ED) of proposed revisions to IPSAS 13 (or a new IPSAS) on Leases.

(c) Link to IFAC and IPSASB Strategic Plans

i. Link to IPSASB Strategy

2.9 The project is consistent with the IPSASB's strategic objective of “strengthening public financial management and knowledge globally through increasing adoption of accrual-based IPSASs by developing high-quality public sector financial reporting standards”⁹⁴. –IFRS convergence, where appropriate, is one of the factors the IPSASB considers in prioritizing the work plan⁹⁵.

ii. Link to IFAC Strategic Plan

2.10 This project is aligned with the mission of IFAC, as stated in its Strategic Plan for 2016–2018, *Charting the Future of the Global Profession*, of serving the public interest and strengthen the accountancy profession by:

- (a) Supporting the development of high-quality international standards; and
- (b) Promoting the adoption and implementation of these standards.

⁹⁴ Page 6 of *The IPSASB's Strategy for 2015 Forward*

⁹⁵ See page 11 of *The IPSASB's Strategy for 2015 Forward*.

3. Outline of the Project

(a) Project Scope

- 3.51 The scope of this project is to develop accounting requirements for leases that are converged with IFRS 16.

(b) Key Issues

- 3.52 The key issues are listed below. The list is not exhaustive.

Key issue #1—Assumption that IFRS convergence is appropriate for leasing transactions in the public sector

- 3.53 When IPSAS 13 was developed the IPSASB decided that it should be converged with IAS 17 because the underlying accounting transactions are the same in the public sector and in the private sector – a lease is a lease – and that there were no public sector specific reasons to diverge from IAS 17. The project will assess whether a similar assumption can be made for IFRS 16, and, if so, develop proposals that are converged with the new IASB standard.
- 3.54 If the IPSASB decides to converge with IFRS 16, there ~~are~~will be implementation costs of the ~~revised IPSAS 13 or a~~ new IPSAS. If the IPSASB decides not to converge with IFRS 16, there are ongoing consolidation issues that needs to be addressed where commercial public sector entities that apply IFRS 16 or the national standard converged with IFRS 16 are consolidated by an entity that applies IPSASs.
- 3.55 Staff notes that in the first scenario the costs are mostly “one-off” in the first year of the application of the new lessee accounting model. These costs are associated with the recognition and measurement of the assets and the related liabilities.
- 3.56 In the latter scenario, the consolidation issues are not “one-off” and will recur in subsequent years.
- 3.57 By providing exemptions for short-term leases and leases for which the underlying asset is of low value, the IASB has sought to lower the costs of implementing IFRS 16.
- 3.58 The Board needs to consider whether in a public sector context the benefits~~cost~~ of introducing an IFRS 16 approach ~~are commensurate with~~exceed the ~~costs~~benefits.
- 3.59 The IPSASB’s policy paper⁹⁶, *Process for Reviewing and Modifying IASB Documents* (also known as *Rules of the Road*), will guide the process.

Key Issue #2—Identification of a lease

- 3.60 As stated in paragraph 1.3, IFRS 16 has one single lessee accounting model in which all leases are accounted for in the same way, with the recognition of assets and liabilities for all leases (with limited exceptions). IFRS 16 provides optional recognition exemptions for short-term leases⁹⁷ or leases for which the underlying asset is of low value⁹⁸.

⁹⁶ See at <http://www.ifac.org/system/files/publications/files/IPSASB-Rules-of-the-Road-Oct2008.pdf>

⁹⁷ A lease that, at the commencement date, has a lease term of 12 months or less. A lease that contains a purchase option is not a short-term lease.

⁹⁸ The assessment of whether an underlying asset is of low value is performed on an absolute basis.

- 3.61 While the issue of identification of a lease is not new, IFRS 16 includes a considerable amount of new material on how leases are identified⁹⁹. The requirements and guidance on lessee accounting are no longer based on classifying a lease as a finance lease or an operating lease, dependent on the risks and rewards incidental to ownership. IFRS 16 provides requirements and guidance in distinguishing a lease from a service based on the following rationale¹⁰⁰:
- Lease: the costumer (the lessee) has a right to control the use of the asset.
 - Service: the supplier has a right to control the use of the asset.
- 3.62 The right to control the use of an asset approach is based on the right to obtain substantially all of the economic benefits from use of the identified asset (a “benefits” element) and the right to direct the use of the identified asset (a “power” element).
- 3.63 At an early stage the project will need to assess to what extent the right to control the use of an asset based on these two elements is applicable to the public sector.
- 3.64 ~~The revised IPSAS 13 or the~~The new IPSAS will have specific guidance to distinguish a lease from service concession arrangements (IPSAS 32, *Service Concession Arrangements: Grantor*) from the perspective of the grantor.

Key Issue #3—Impact of revised lessee accounting model

- 3.65 The new lessee accounting model will have an impact on the recognition, measurement, presentation and disclosure of assets, liabilities, revenue and expense. The recognition of assets and liabilities associated with a lease will have a major impact on the financial statements of public sector entities that use leases extensively in their operations.
- 3.66 Although the IPSASB’s literature does not include a standard on budget formulation and execution, the new lessee accounting model may have an impact in jurisdictions where entities base their budget accounting for leases on IPSAS.
- 3.67 In jurisdictions that apply “pure” accrual budgeting the impact on the budget will be the same as the impact on accrual accounting. In countries that do not apply “pure” accrual budgeting the impact will depend on the extent to which accrual information is used for budget purposes.
- 3.68 The change in the lessee accounting model will also affect fiscal targets set by governments when they use accrual-~~basisbased~~ IPSASs as the accounting ~~basisbases~~. Staff notes that in many countries fiscal targets are based on Government Finance Statistics (GFS) reporting guidelines. As GFS is not changing its lease accounting guidance (or requirements), the new lessee accounting model will have no impact on performance against these fiscal targets.
- 3.69 The project will need to assess any consequential changes to existing IPSASs. These may be based on the consequential amendments made to other IFRSs made by IFRS 16, or may be specific to existing IPSASs (for example, the distinction between a lease and a service concession arrangement under IPSAS 32).

⁹⁹ Staff notes that although the definition of a lease changed in IFRS 16, its meaning is basically the same.

IPSAS 13—A lease is an agreement whereby the lessor conveys to the lessee, in return for a payment or series of payments, the right to use an asset for an agreed period of time.

IFRS 16—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.

¹⁰⁰ According to Paragraph BC140 of IFRS 16 “the new standard applies to contracts that convey the right to use an underlying asset for a period of time and does not apply to transactions that transfer control of the underlying asset to an entity—such transactions are sales or purchases within the scope of other Standards (for example, IFRS 15 or IAS 16).”

- 3.70 The project will also need to assess when the ~~revised IPSAS 13~~ or new IPSAS will~~should~~ become effective.
- 3.71 IFRS 16 will only be effective in 2019. The IPSASB convention is that an effective date is no less than eighteen months after publication.
- 3.72 The IPSASB will also need to assess whether it will apply the same criteria as the IASB in determining an effective date for IFRS 16 or there are public sector reasons that warrant a different period to the effective date for the ~~revised or~~ new IPSAS.

Key Issue #4—Sale and leaseback transactions

- 3.73 IFRS 16 introduced additional requirements to recognize revenue only to be applicable within the context of a sale and leaseback transaction. IFRS 16 now requires that a transfer of an asset is accounted for as a sale only if the transfer meets the requirements in IFRS 15, *Revenue from Contracts with Customers*. The IASB was of the view that this requirement “will be beneficial for both preparers and users of financial statements because it will increase comparability between sales entered into as part of a sale and leaseback transactions and all other sales.”¹⁰¹
- 3.74 IFRS 15 follows a *performance obligation* approach to recognize revenue from the transfer of goods and services to customers ~~and is applicable to both lessee and lessor~~¹⁰².
- 3.75 The IPSASB has a project on Revenue According to update IFRS 16, if the transfer of the underlying asset satisfies the requirements of IFRS 15 to be accounted for as a sale, the transaction will be accounted for as a sale (the seller-lessee derecognizes the underlying asset and guidance on IPSAS 9, *Revenue from Exchange Transactions*, the buyer-lessor recognizes the underlying asset) and IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)* the lessor. If not, the transaction is accounted for as a financing by both the seller-lessee and the buyer-lessor and both apply IFRS 9, *Financial Instruments*.
- 3.753.76 Currently, IPSAS 23 follows a present IPSASB’s literature does not have a performance obligation approach to recognize the recognition of revenue from the sale of assets, liabilities and revenue. Staff has identified two options to manage this new requirement in IFRS 16 in the future development of the Leases project:
- (c) Decisions taken by the IPSASB when considering Option 1—Do not include any requirement now and include the performance obligation approach in its Revenue project may impact on this aspect of the Leases project. Therefore, the IPSASB needs to consider the impact of any decision to adopt later (as a consequential amendment of the new IPSAS on Revenue); and
- (e)(d) Option 2—Include current IPSASs requirements¹⁰³ now and include the performance obligation approach in the Revenue project and the extent of such adoption on the development of the Leases project later (as a consequential amendment a new or revised IPSAS on Revenue).
- 3.77 Staff notes that according to the project timetable in paragraph 5(b), staff expects an ED to be approved in September 2016. The As the effective date of the new IPSAS on revenue is still uncertain and the Revenue project has is still in a Consultation Paper phase and is not expected

¹⁰¹ Paragraph BC261 of IFRS 16

¹⁰² See paragraphs BC262-BC265 of IFRS 16 for further details on IASB’s rationale.

¹⁰³ IPSAS 9, *Revenue from Exchange Transactions* and IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*

to, staff is of the view that the Leases project cannot be linked to the Revenue project and, as a consequence, delay the Leases project, as the IPSASB always have the two above options.

3.763.78 During the development of the Leases project, the IPSASB will need to decide which of these two options will be completed before 2018 applied in the new IPSAS on Leases.

Key Issue #5—New disclosures in lessor accounting model

3.773.79 As stated in paragraph 1.3, the lessor accounting remains substantially the same as in IFRS 16. However, IFRS 16 introduced enhanced disclosures for lessors providing information on:

- (f) The different components of lease revenue recognized during the reporting period;
- (g) Residual asset risk;
- (h) Assets subject to operating leases;
- (i) Maturity analyses; and
- (j) Changes in net investment in finance leases.

3.783.80 Staff notes that public sector entities are usually the lessees and not the lessors, so the impact of changes to disclosure requirements may be limited. Nevertheless, the quite often public sector entities lease assets to other public sector entities (for example, to improve occupancy rate of unused buildings). In many jurisdictions, governments also establish public sector entities specializing in leasing assets to public sector entities. These “centralized lessors” have an important role in managing assets (mainly buildings) in the public sector. The IPSASB will need to assess to what extent these new disclosures are appropriate for public sector entities and whether further specific disclosures are required.

Key Issue #6—Lack of symmetry in lease accounting

3.81 IFRS 16 does not follow a symmetrical approach to lease accounting, i.e., while the lessee is required to recognize (almost) all leased assets (the right-of-use asset) and related liabilities, the lessor only recognizes a lease asset (the net investment in the lease) if the lease is classified as a finance lease.

3.82 One consequence of the lack of symmetry in IFRS 16 is that the underlying asset may not be recognized in either the lessee’s or the lessor’s statement of financial position. This might occur when the lessor classifies the lease as a finance lease.

3.83 The IASB explained the reason for the asymmetrical approach in paragraph BC61(b) of the Basis for Conclusions to IFRS 16:

“most users of financial statements do not currently adjust lessors’ financial statements for the effects of leases—indicating that the lessor accounting model in IAS 17 already provides users of financial statements with the information that they need. In addition, investors generally analyse the financial statements of individual entities (and not a lessee and lessor of the same underlying asset). Accordingly, it is not essential that the lessee and lessor accounting models are symmetrical.”

3.84 Staff notes that this rationale is not related to the economics of a lease; rather it is related to the specific business environment and users’ needs in the for-profit sector.

3.85 Staff notes that the business environment and users’ needs in the for-profit sector may be different from the public sector. In fact, in the public sector very often the lessor and the lessee are both public sector entities and the same public sector entity can be simultaneously lessor and

lessee in different lease contracts with other public sector entities or with private sector entities. These types of transactions can also occur within the same economic entity or between different levels of government not under common control.

- 3.86 The lack of symmetry in lease accounting would also create asymmetrical information in public sector financial reporting when governments do not publish consolidated financial statements and users have to rely on the separate financial statements of individual entities for accountability and decision-making purposes.
- 3.87 In this context, users of general purpose financial reports of public sector entities often analyze the financial statements of the lessee and lessor of the underlying asset in order to better assess the risks of lending resources and understand who controls the underlying asset. The underlying asset may be used as collateral for borrowing¹⁰⁴.
- 3.88 The derecognition of the underlying asset by the lessor may mean that the financial information on leasing transactions does not meet the objectives of financial reporting because users are not provided with information that is useful for accountability and decision-making purposes.
- 3.89 Because of the introduction of the right-of-use model in lessee accounting, the IPSASB will need to assess the need of symmetry for lessor accounting in the light of the objectives and qualitative characteristics of public sector financial reporting.

Key Issue #7—"Peppercorn" leases

- 3.90 For the purpose of this project, staff will consider "peppercorn" leases all leases with nominal, reduced or rent-free, i.e., all leases that are not exchange transactions as defined in IPSASs glossary¹⁰⁵.
- 3.91 Staff notes that the decision to add "peppercorn" leases will affect the scope of an Exposure Draft.
- 3.92 Quite often public sector entities and international organizations enter into a "peppercorn" lease for the whole period of use of the underlying asset that does not involve a sale and leaseback transaction. "Peppercorn" leases usually occur between public sector entities and between international organizations.
- 3.93 IFRS 16 requires that the lease asset and liability are measured at cost¹⁰⁶. Applying IFRS 16 measurement requirements to "peppercorn" leases will lead to an understatement of the lease asset and a failure to recognize the subsidy from the lessor to the lessee in the financial statements of both the lessee and the lessor. Therefore, the accounting requirements for "peppercorn" leases will be developed for lessee and lessor.
- 3.94 Staff has identified two mutually exclusive options to address "peppercorn" leases in IPSASs:
- (a) Option 1—Include "peppercorn" leases within the scope of the new IPSAS on Leases; or
 - (b) Option 2—Include "peppercorn" leases explicitly within the scope of IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)* or in IPSASB's current projects on non-exchange expenses and revenue.

¹⁰⁴ For example: a public sector entity, which is a specialized lessor for the public sector, issues bonds in the capital markets to finance purchases of assets from other public sector entities that will be leased-back. As bonds are issued in the name of the public sector entity and not in the name of the State or guaranteed by the State, lenders may require the underlying asset to be used as collateral for borrowing, and understand who, in fact, controls the underlying assets.

¹⁰⁵ Transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

¹⁰⁶ Paragraphs 23, 24, 26 and 27 of IFRS 16

[3.95 Staff has also identified two mutually exclusive options to measure leases, including “peppercorn leases”:](#)

[\(a\) Option 1—Measure all leases at fair value; or](#)

[\(b\) Option 2—Measure leases that are exchange transactions at cost and measure peppercorn leases \(non-exchange transaction\) at fair value.](#)

[3.96 During the development of the Leases project, the IPSASB will need to decide which of these options will be applied in the new IPSAS on Leases.](#)

4. Describe the Implications for any Specific Persons or Groups

(a) Relationship to IASB

4.1 The project is primarily linked to IFRS 16. There are also links to IFRS 15.

(b) Relationship to Other Standards, Projects in Process or Planned Projects

4.2 There are links to the Conceptual Framework, to other IPSASs, notably IPSAS 17, *Property Plant and Equipment* and IPSAS 32 and the IPSASB’s Revenue project.

4.3 The recognition section of IPSAS 17 will need to be amended to reflect the new approach to lessee accounting.

4.4 There will be consequential amendments in IPSAS 32 a result of ~~the revised IPSAS 13 or~~ new IPSAS [on Leases](#).

(c) Other—Government Finance Statistics (GFS)

4.5 The IPSASB supports the reduction of unnecessary differences between GFS and IPSAS in the development of new IPSASs and revisions to existing IPSASs. The IPSASB’s policy paper *Process for Considering GFS Reporting Guidelines during Development of IPSASs* (2014) guides the process.

4.6 Government Finance Statistics Manual 2014 (GFSM 2014) classifies leases based on the distinction between legal and economic ownership. According to paragraph A4.4 of GFSM 2014, “the legal owner of resources is the institutional unit entitled by law and sustainable under the law to claim the benefits associated with the asset. By contrast, the economic owner of resources is entitled to claim the benefits associated with the use of the asset in the course of an economic activity by virtue of accepting the associated risks.”

4.7 Based on this approach, GFSM 2014 identifies three types of leases¹⁰⁷:

(d) **Operating leases** – Are agreements for the use of nonfinancial assets, except natural resources. There is no change of economic ownership as the legal owner continues to be the economic owner.

(e) **Resource leases** – Are agreements for the use of natural resources, such as land and radio spectrum. Similar to operating leases, there is no change of economic ownership.

(f) **Financial leases** – Are agreements for the use of all ~~nonfinancial~~[non-financial](#) assets, including natural resources under some circumstances.

¹⁰⁷ Paragraphs A4.6–A4.17 of GFSM 2014 provides further guidance on how to classify a lease.

- 4.8 Staff notes that, although GFSM 2014 has a different classification approach from IPSAS 13 and IAS 17, generally GFSM 2014 applies the same lease accounting as in IPSAS 13 and IAS 17 for recognition and measurement. Staff is of the view that adoption of the new lessee accounting model in IFRS 16 will increase the differences with GFSM 2014. These differences may be temporary, if the IFRS 16 lessee accounting model is adopted in the next revision of the GFS manuals¹⁰⁸. If GFS does not apply the new lessee accounting model, then there ~~will~~may be a permanent difference between IPSAS and GFS.
- 4.9 Staff notes that IPSAS 13 is aligned with IAS 17 rather than with GFS. As IFRS 16 was published after GFSM 2014, staff recommends that the IPSASB does not consider GFS reporting guidelines in the development of this project further. However, when the ~~revised IPSAS 13 or~~ new IPSAS on Leases is published, staff recommends that any differences related to the recognition and measurement of leases are should be included in the IPSAS/GFS Tracking Table.
- 4.10 Staff is aware that the statistical community is following the recent IASB's developments in lease accounting very closely. In the context of revision of 2008 SNA, the statistical community will discuss in the near future, whether and, if so, the new lease accounting that the IASB has developed will be addressed.

5. Development Process, Project Timetable and Project Output

(a) Development Process

- 5.1 The development of outputs will be subject to the IPSASB's formal due process. The approval of the ED will be subject to the usual IPSASB voting rules. As the project progresses, regular assessments will be made to confirm the proposed path in the project timetable remains the most appropriate. ~~As this is a convergence project, staff is of the view that it could be completed quite quickly.~~
- 5.2 ~~If Appendix A—Leases Project Timetable shows a proposed project timetable (assuming initiation of the IPSASB approves project in June 2016) and contingent on future decisions over the project brief in March 2016, staff proposes to bring a. A first Issues Paper to will be discussed at the June 2016 meeting. The timetable projects after approval of an ED in September 2016 with publication at the end of October 2016 and an exposure period of 3-4 months. the project brief.~~
- 5.3 Staff proposes to split the review of responses into two sessions in (December 2017 with the approval and March 2018). Approval of a revised IPSAS 13 or a new IPSAS at the end of 2017 on Leases is projected for June 2018 with publication in July 2018.

(b) ~~Detailed project timetable (assuming approved to commence in 2016)~~

Meeting		Objective
2016	March	5. Review of Project Brief 6. Approval of Project Brief

¹⁰⁸ The revision of the GFS manuals are still some years away. The GFSM 2014 aims to be consistent with the *System of National Accounts, 2008 (SNA)*. Paragraph 13 of IPSASB Policy Paper *Process for Considering GFS Reporting Guidelines during Development of IPSASs* states that "Scope to reduce differences through changes to the GFS reporting guidelines largely depends on the changes identified not adversely affecting the guidelines' consistency with the SNA".

Meeting		Objective
	June	7. Objective, Scope and Exemptions—Short-term and low-value leases 8. Identifying a lease—Lease versus Service versus Service Concessions 9. Lessee accounting: Recognition, Measurement and Presentation 10.——Lessor accounting: Classification of leases 11.——Lessor accounting: Recognition, Measurement and Presentation 12.——Sale and Leaseback Transactions 13.——Other issues: Revised IPSAS 13 versus New IPSAS
	September	6. Disclosures: Lessee and Lessor 7. Terminology—Conceptual Framework 8. Review of draft ED 9. Approval of ED
2017	June	6. Review of Responses: Objective, Scope and Exemptions 7. Review of Responses: Identifying a lease 8. Review of Responses: Lessee accounting—Recognition, Measurement and Presentation
	September	5. Review of Responses: Lessor accounting—Recognition, Measurement and Presentation 6. Review of Responses: Disclosures—Lessee and Lessor 7. Review of Responses: Sale and Leaseback Transactions 8. Review of Responses: Terminology—Conceptual Framework
	December	3. Review of draft IPSAS 4. Approval of revised IPSAS 13 or new IPSAS

(c) Project output

5.35 The initial output will be an ED converged with IFRS 16. Following analysis of the responses to the ED a [revised IPSAS 13 or a new IPSAS on Leases](#) will be issued.

6. Resources Required

(a) Task Based Group

6.1 A Task Based Group will advise staff in the development of this project.

(b) Staff

6.2 It is envisaged that 0.34 Full Time Equivalent (FTE) will be required to resource the project.

(c) Factors that might add to complexity and length

6.3 Factors that could add to the complexity and length of the project are the need to align with the Revenue project on sale and leaseback and identification of public sector specific reasons to depart from IFRS 16.

7. Important Sources of Information

7.1 The principal information sources will be IFRS 16 and the *Conceptual Framework*.

APPENDIX A – LEASES PROJECT TIMETABLE

<u>Meeting</u>		<u>Objective</u>
<u>2016</u>	<u>June</u>	5. Review and approval of Project Brief 6. Lessee: applicability of IFRS 16 recognition and measurement requirements to public sector financial reporting (except reassessment of the lease liability and lease modifications) 7. “Peppercorn” leases 8. Lessor: applicability of IFRS 16 recognition requirements to public sector financial reporting
	<u>September</u>	7. Objective, Scope and Definitions (including “peppercorn” leases) 8. Identifying a lease: Lease versus Service versus Service Concessions 9. Lessee: Measurement and reassessment of the lease liability and lease modifications 10. Lessor: Recognition and measurement (if the IPSASB agrees with symmetry in lease accounting) or only measurement (if the IPSASB agrees to retain the dual model) 11. Presentation: Lessee and lessor 12. Sale and Leaseback Transactions
	<u>December</u>	6. Disclosures: Lessee and Lessor (including “peppercorn” leases) 7. Terminology: Conceptual Framework 8. Application Guidance 9. Effective date and transition 10. Review of first draft ED
<u>2017</u>	<u>March</u>	6. Review of draft ED 7. Approval of ED
	<u>December</u>	8. Review of Responses: Objective, Scope and Exemptions 9. Review of Responses: Identifying a lease 10. Review of Responses: Recognition and measurement—Lessee and lessor
<u>2018</u>	<u>March</u>	5. Review of Responses: Presentation—Lessee and lessor (including peppercorn leases) 6. Review of Responses: Disclosures—Lessee and Lessor (including peppercorn leases) 7. Review of Responses: Sale and Leaseback Transactions 8. Review of Responses: Terminology—Conceptual Framework
	<u>June</u>	3. Review of draft IPSAS 4. Approval of new IPSAS