Date: May 03, 2023

Mr João Fonseca

Principal,

International Public Sector Accounting Standards Board

International Federation of Accountants

529 5th Avenue

New York, New York 10017

RE: Comments on ED 84, *Concessionary Leases and Right-of-Use Assets In-kind* (Amendments to IPSAS 43 and IPSAS 23)

Dear Mr. Fonseca,

We welcome the opportunity to comment on ED 84, *Concessionary Leases and Right-of-Use Assets In-kind* (Amendments to IPSAS 43 and IPSAS 23).

Our responses to the specific questions raised in the Exposure Draft as well as other comments are set out in Appendix 1.

Should you have any queries concerning the matters in this submission, or wish to discuss them in further detail, please contact Mr. Abdullah Alhomaida via email at:

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Yours sincerely,

Abdullah Al Mehthil

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Appendix 1 - Exposure Draft (ED) 84, *Concessionary Leases and Right-of-Use Assets In-kind* (Amendments to IPSAS 43 and IPSAS 23)

Specific Matter for Comment 1:

The IPSASB decided to propose new accounting guidance for concessionary leases for lessees (see paragraphs IPSAS 43.BC124–BC137) and right-of-use assets in-kind (see paragraphs IPSAS 23.BC28– BC30). Do you agree with the proposed amendments to IPSAS 43 and IPSAS 23? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

[Our Comments] We generally agree with the proposed guidance for concessionary leases for lessees and right-of-use assets in-kind, but have the following comments:

1. The proposed amendments to IPSAS 23 require an entity to identify a right-of-use asset in-kind by applying the principles in IPSAS 43. Specifically, IPSAS 23.28A states:

    > 28A. An entity identifies a right-of-use asset in-kind in accordance with the requirements of paragraphs 10–12 and AG10–AG34 of IPSAS 43, *Leases* for identifying a lease, <u>with the necessary adaptations in the absence of lease payments</u>.

    While it is clear from the proposed guidance that a lack of consideration is definitive of a right-of-use asset in-kind, it is not clear if the existence of a binding arrangement (contract or otherwise) and a specified term are conditions of a right-of-use asset in-Kind. We suggest that this should be clarified in IPSAS 23.28A. Our concern is that in the absence of a clear definition of what constitutes a right-of-use asset in-kind, preparers could apply IPSAS 43.10–12 and IPSAS43.AG10–AG34 differently to similar situations. Judging by those paragraphs alone an entity may conclude that a transaction does not give rise to a right-of-use asset in-kind due to lack of a binding arrangement and specified term, while another may, based on IPSAS 23.96, conclude that it does if the right to use the underlying asset has already been received.

2. IPSAS 23.83 states:

    > 83. As required by paragraph 42, transferred assets are measured at their fair value as at the date of acquisition. Entities develop accounting policies for the recognition and measurement of assets that are consistent with IPSASs. As noted previously, inventories, property, plant, equipment, or investment property acquired through non-exchange transactions are to be initially measured at their fair value as at the date of

> acquisition, in accordance with the requirements of IPSAS 12, IPSAS 16, and IPSAS 17. Right-of-use assets held by a lessee and right-of-use assets in-kind acquired through non-exchange transactions are to be initially measured at the present value of payments for the lease at market rates based on the current use of the underlying asset in accordance with IPSAS 43. Financial instruments, including cash and transfers receivable that satisfy the definition of a financial instrument, and other assets, will also be measured at fair value as at the date of acquisition in accordance with paragraph 42 and the appropriate accounting policy.

We suggest adding "under concessionary leases" after "Right-of-use assets held by a lessee" for the sake of completeness.

3. We note that no illustrative examples relating to rights-of-use assets in-kind are proposed to be added to the non-authoritative guidance accompanying IPSAS 23. We suggest that the IPSASB should add illustrative examples on the identification of and accounting for rights-of-use assets in-kind. We further suggest that such examples should cover scenarios in which a rights-of-use asset in-kind exists and does not exist (i.e. other type of asset or service in-kind exists).

4. The proposed amendments to IPSAS 43's Basis for Conclusions provide a discussion in BC106-BC117 that is so focused on making the case that transactions conveying the right to use an underlying asset without consideration do not meet the definition of a lease, that it may be prove confusing or may be misunderstood as indicating that right-of-use assets in-kind fall all the way outside the scope of IPSAS 43. We suggest that the IPSASB should:

   A. include text in the scope section of IPSAS 43 explaining that a right-of-use asset in-kind is identified by applying the principles in IPSAS 43 and is measured by following the same principles in IPSAS 43 as for a right- of-use asset acquired through a concessionary lease; and

   B. include text in IPSAS 43's Basis for Conclusions explaining that notwithstanding the IPSASB's conclusion that transactions conveying the right to use an underlying asset without consideration do not meet the definition of a lease, the IPSASB has introduced additional guidance on a transitional basis in IPSAS 23 to:

      - Identify a right-of-use asset in-kind applying the principles in IPSAS 43; and
      - Measure a right-of-use asset in-kind by following the same principles as for a right- of-use asset in concessionary leases.

5. IPSAS 43.26B states:

> 26B. The payments for the lease at market rates based on the current use of the

> underlying asset shall be discounted using the interest rates identified in paragraph 27. The carrying value of the right-of- use asset shall also include the items identified in paragraphs 25(c) and 25(d).

It is not clear why only IPSAS 43.25(c) and 25(d) are referenced in this paragraph and not 25(b) too ("any lease payments made at or before the commencement date, less any lease incentives received;").

We also suggest replacing "carrying value" with "cost" for consistency with IPSAS 43.24 and 25 which refer to the "cost" of a right-of-use asset.

6. IPSAS 43.42 states:

> 42. In applying paragraph 41, a lessee shall determine the revised discount rate as the interest rate implicit in the lease for the remainder of the lease term, if that rate can be readily determined, or the lessee's incremental borrowing rate at the date of reassessment, if the interest rate implicit in the lease cannot be readily determined. In the case of a concessionary lease, a lessee shall apply the discount rate identified in paragraph 27.

It is not clear if the underlined text means the original discount rate used at initial measurement. This should be clarified. It is not clear though why for concessionary leases the IPSASB should depart from IPSAS 43's requirement to use a revised discount rate. This is not explained in the proposed amendments to IPSAS 43's Basis for Conclusions.

7. The proposed additions to IPSAS 43's authoritative guidance does not specifically address adjustments under the cost model to the right-of-use asset in a concessionary lease for any remeasurement of the lease liability specified in IPSAS 43.37(c). Notwithstanding IPSAS 43.BC122-BC123, the IPSASB has not provided an adequate discussion of why there should not be requirements specific to concessionary leases in this particular regard:

> Lease Modifications
>
> BC122. The IPSASB considered the role of lease modifications when identifying and classifying leases atmarket or at below-market terms.
>
> BC123. The IPSASB decided not to include additional guidance on lease modifications because an entity needs to apply professional judgment when assessing the conditions in IPSAS 43.

Lease liability reassessments / lease modifications may be such that they require a reassessment of whether the lease continues to be a concessionary lease and if so whether the carrying amount of the right-of-use asset should be adjusted to reflect the present value of updated payments at market rates based on the current use of the underlying asset (See also our comment #2 on SMC 3).

8. IPSAS 43.117A states:

> Leases Previously Classified as Operating Leases
>
> 117A. If a lessee elects to apply this Standard in accordance with paragraph 109(b), the lessee shall:
>
> (a) Recognize a lease liability at the date of initial application for concessionary leases previously classified as an operating lease applying IPSAS 13. The lessee shall measure that lease liability at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate at the date of initial application.
>
> (b) Recognize a right-of-use asset at the date of initial application for concessionary leases previously classified as an operating lease applying IPSAS 13. The lessee shall, on a lease- by-lease basis, measure that right-of-use asset at its carrying amount as if this Standard had been applied since the commencement date, but using the payments for the lease at market rates based on the current use of the underlying asset and discounted using the lessee's incremental borrowing rate at the date of initial application.

Unlike IPSAS 43.112(b) which offers two measurement options, IPSAS 43. 117A(b) prescribes a single way to measure the right-of-use asset on transition from a lease previously classified as an operating lease applying IPSAS 13. We therefore suggest that latter paragraph should be revised to read, "..... The lessee shall measure that right-of-use asset at its carrying amount as if this Standard had been applied since the commencement date, but using payments for the lease at market rates based on the current use of the underlying asset, discounted using the lessee's incremental borrowing rate at the date of initial application."

9. IPSAS 43.117D states:

> 117D. A lessee may elect not to apply the requirements in paragraph 117A to concessionary leases for which the lease term ends within 12 months of the date of initial application. In this case, the lessee shall include the cost associated with

> those concessionary leases within the disclosure of short- term lease expense in the annual reporting period that includes the date of initial application.

This paragraph omits IPSAS 43.114(c)(i) reading "Account for those leases in the same way as short-term leases as described in paragraph 7; and". We note that a lessee will still apply IPSAS 43.7 if it makes the election in IPSAS 43.117D, so we cannot see why IPSAS 43.114(c)(i) is not reflected in IPSAS 43.117D.

10. IPSAS 43.117E states:

> Leases Previously Classified as Finance Leases
>
> 117E. If a lessee elects to apply this Standard in accordance with paragraph 109(b), for concessionary leases that were classified as finance leases applying IPSAS 13, at the date of initial application the lessee shall:
>
> (a) Measure the lease liability at the carrying amount of the lease liability immediately before that date measured applying IPSAS 13; and
>
> (b) Recognize a right-of-use asset and measure in accordance with paragraph 117A(b).
>
> For those concessionary leases, a lessee shall account for the right-of-use asset and the lease liability applying this Standard from the date of initial application.

We suggest revising IPSAS 43.117E(b) to read, "Recognize, in place of the leased asset, a right-of-use asset measured in accordance with paragraph 117A(b)" for the sake of clarity and completeness.

Specific Matter for Comment 2:

For lessors, the IPSASB decided to propose accounting for leases at below-market terms in the same way as for leases at market terms (see paragraphs IPSAS 43.BC138–BC149). Do you agree with the proposed amendments to IPSAS 43? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

[Our Comments]

1. While we agree that the proposed lessor accounting for concessionary operating leases is consistent with (a) the fact that no economic benefits or service potential associated with the transaction will flow to the entity higher than the cash received by the lessor in the form of lease payments made by the lessee, and with (b) revenue recognition principles in IPSAS 9, *Revenue from Exchange Transactions*; the IPSASB's proposal (in IPSAS 43.BC148 and the

diagram below IPSAS43.AG32B) that the cost of the concession component would be the difference between the expenses associated with the underlying asset and lease revenue based on contractual payments seems to be conceptually at odds with the IPSASB's description of a "concessionary lease" in IPSAS 43. 18A-18D and AG60–AG62 which indicates that the concessionary component is the difference between "market terms" and "below market terms", not between cost and "below market terms".

We suggest that the IPSASB should first consider the relevance to financial statement users and costs of reporting information on the concession component of leases in the financial statements of lessors given that a large part of the entities for which IPSAS are intended operate at subsidized rates or at cost recovery and do not normally, and are not required by IPSAS to, report information on the subsidized component ("forgone revenue"). If the IPSASB concludes that lessors should not be required to report such information, we suggest that the IPSASB should withdraw its proposal that the cost of the concession component would be the difference between the expenses associated with the underlying asset and lease revenue based on contractual payments (IPSAS 43.BC148 and the diagram below IPSAS43.AG32B). If, however, the IPSASB concludes that lessors should report such information, we suggest that the IPSASB should either:

A. withdraw its proposal that the cost of the concession component would be the difference between the expenses associated with the underlying asset and lease revenue based on contractual payments (IPSAS 43.BC148 and the diagram below IPSAS43.AG32B), and should instead require reporting by way of note disclosure information that is representative of the concept of the lease component as it now stands in ED 84---that is, information that is based on the difference "market terms" and "below market terms"; or

B. develop a concept of "concessionary leases" for lessors that is based on the difference between costs and contractual payments---that is, a public sector specific concept.

2. As for the proposed accounting for concessionary finance leases, the requirement that a lessor should measure the net investment in a concessionary lease at the present value of contractual payments obviously mirrors the requirement that a lessee should measure the liability for a concessionary lease at the present value of contractual payments, but is inconsistent with both IPSAS 41's approach to creditor accounting for concessionary loans and the requirement that a lessee should account for the concession component in a concessionary lease following the principles applicable to concessionary loans in IPSAS 23, with the effect that the lessor and lessee would measure the concession component of the transaction in their surplus or deficit differently. Again, here too the IPSASB's proposal (in IPSAS 43.BC146, the diagram below IPSAS43.AG32B and IPSAS 43.96A(c)) that the cost of

the concession component would be the difference between the carrying amount of the underlying asset and the net investment in the lease based on contractual payments seems to be conceptually at odds with the IPSASB's description of a concessionary lease which indicates that the concessionary component is the difference between "market terms" and "below market terms", not between cost and "below market terms".

We suggest that the IPSASB should first consider the relevance to financial statement users and costs of reporting information on the concession component of leases in the financial statements of lessors given that a large part of the entities for which IPSAS are intended operate at subsidized rates or at cost recovery and do not normally report information on the subsidized component (except in creditor's accounting for concessionary loans). If the IPSASB concludes that lessors should not be required to report such information, we suggest that the IPSASB should withdraw its proposal that the cost of the concession component would be the difference between the carrying amount of the underlying asset and the net investment in the lease based on contractual payments (IPSAS 43.BC146, the diagram below IPSAS43.AG32B and IPSAS 43.96A(c)). If, however, the IPSASB concludes that lessors should report such information, we suggest that the IPSASB should either:

A. withdraw its proposal that the cost of the concession component would be the difference between the carrying amount of the underlying asset and the net investment in the lease based on contractual payments (IPSAS 43.BC146 and the diagram below IPSAS43.AG32B), and should instead develop an approach for lessor accounting for concessionary finance leases that is similar to creditor accounting for concessionary loans under IPSAS 41. The reasons cited in IPSAS 43. BC134 in support of the proposed lessee accounting for concessionary leases seem relevant to lessor accounting for concessionary finance leases too:

> BC134. The IPSASB also decided to account for the concession component in a concessionary lease following the principles applicable to concessionary loans in IPSAS 23 because:
>
> (a) Both transactions are at below-market terms at inception;
>
> (b) Have a concession to the price of the resource being transferred;
>
> (c) Have the objective to provide/receive resources with a price at below-market terms;
>
> (d) Whether transferring a resource in cash or in-kind it should not modify the accounting forthe concession component as non-exchange revenue in both transactions, as concessionary leases are in substance a financing transaction; and

(e) It prevents preparers choosing between concessionary leases and concessionary loans to achieve desired accounting outcomes.

Or:

B. develop a concept of "concessionary leases" for lessors that is based on the difference between costs and contractual payments---that is, a public sector specific concept.

3. The proposed amendments do not cover grantor accounting for transactions that convey the right to use an underlying asset without consideration. We suggest that the IPSASB should develop guidance to fill this gap.

4. IPSAS 43.96B states:

Concessionary Operating Leases

96B. For concessionary operating leases granted, a lessor shall disclose:

(a) Contractual value of the lease payments received during the period; and

(b) The purpose and terms of the various types of concessionary operating leases, including the nature of the concession.

We suggest revising the IPSAS 43.96B(a) to read, "The amount of lease revenue accrued during the period; and" for comparability with the costs associated with the underlying asset incurred on the accrual basis during the period.

Subject to our comment #1 on this SMC, we also suggest adding the following disclosures immediately after IPSAS 43.96B(a) to report the "amount of the concession" for concessionary operating leases similar to the disclosures in IPSAS 43.96A for concessionary finance leases:

"(b) The aggregate of the costs incurred in earning the lease revenue during the period broken down by nature of expense;

(c) The difference between (a) and (b); and"

5. We note that the IPSASB has proposed in IPSAS 43 to address the interaction between lessee accounting for concessionary leases and IPSAS 23, and the interaction between lessor accounting for concessionary operating leases and IPSAS 21 and 26. Subject to our comments #1 and 2 on this SMC, we suggest that the IPSASB should also consider any interaction between lessor accounting for concessionary finance and operating leases and the IPSAS on transfer expenses.

Specific Matter for Comment 3:

The IPSASB decided to propose initially measuring right-of-use assets in concessionary leases (see paragraphs IPSAS 43.BC124–BC131) and right-of-use assets in-kind (see paragraphs IPSAS 23.BC28– BC30) at the present value of payments for the lease at market rates based on the current use of the underlying asset as at the commencement date of the lease. Do you agree with IPSASB's decision? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

[Our Comments]

We generally agree with the proposed guidance for the initial measurement of right-of-use assets in concessionary leases and right-of-use assets in-kind, but have the following comments:

1. We suggest that the IPSASB should define what is meant by "current use of the underlying asset as at the commencement date". The commencement date of the lease is the date on which a lessor makes an underlying asset available for use by a lessee. At the commencement date the underlying asset may not be in use at all if the lessor has stopped using it and the lessee has yet to start using it. So, does "current use" refer to "final use by the lessor before it turns over the underlying asset" or "intended use by the lessee as provided by the lease"? Also, the aspects of "current use" should be clarified. Does this include the purpose for which the underlying asset is used, the level of use, and/or something else?
2. We suggest that the IPSASB should address how subsequent measurement of the right-of-use asset in a concessionary lease should be impacted (if at all) if there has been a change in the agreed use of the underlying asset (See our comment #7 on SMC 1).
3. We suggest that the IPSASB should consider the applicability of current operational value to the initial measurement of right-of-use assets in-kind.

Specific Matter for Comment 4:

When the payments for the lease at market rates based on the current use of the underlying asset are not readily available, the IPSASB decided to propose initially measuring right-of-use assets in concessionary leases (see paragraphs IPSAS 43.BC132–BC133) at the present value of contractual payments for the lease. Do you agree with IPSASB's decision? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

[Our Comment] We agree. However, we note that the proposed additional guidance in IPSAS 23 is silent regarding such a scenario in respect of a right-of-use asset in-kind. We suggest that the IPSASB should clarify how the acquirer of a right-of-use asset in-kind should, if at all, measure that asset when information about payments at market rates based on the current use of the underlying asset is not readily available.

Other Comments

1. IPSAS 43. 18C states:

   > 18C. As concessionary leases are granted or received at below-market terms, the present value of contractual payments (consideration) on initial recognition of the lease will be lower than the present value of payments for the lease at market rates based on the current use of the underlying asset. At initial recognition, an entity, therefore, analyzes the substance of the lease granted or received into its component parts, and accounts for those components using the principles in paragraphs AG60–AG62.

   Given the dichotomy between how a lessee and a lessor should respectively account for concessionary leases (i.e. the present value of payments for the lease at market rates based on the current use of the underlying asset is only applicable to lessee accounting), it may not be clear to preparers that the test indicated by the underlined text is applicable to both lessees and lessors. This should be clarified.

2. We suggest the following editorial corrections to the diagram below IPSAS 43.AG32B:

The lease contains both an exchange component and a non-exchange component.	The lease contains both exchange and non-exchange components.
Difference between lease revenue and the expenses with the underlying asset.	Difference between lease revenue and the expenses associated with the underlying asset.

3. We suggest that the IPSASB should address how entities that continue to apply IPSAS 13 until the effective date of IPSAS 43 should handle concessionary leases and free rights to use in the interim under the operating / finance lease accounting models in IPSAS 13.