

NZ IAS 17 (Diff Rep)



NZ International Accounting Standard 17 (Diff Rep)

Leases (NZ IAS 17 (Diff Rep))

Issued November 2012

This Standard was issued by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 24(1)(a) of the Financial Reporting Act 1993.

This Standard is a Regulation for the purposes of the Regulations (Disallowance) Act 1989.

As at 1 December 2012, the requirements in this Standard are identical to the requirements in NZ IAS 17 *Leases* as applied by qualifying entities. Versions of NZ IAS 17 as applied by qualifying entities prior to adoption of this Standard are available on the Archived Standards page of the External Reporting Board (XRB) website at xrb.govt.nz

The following New Zealand Interpretations refer to NZ IAS 17 (Diff Rep):

- NZ SIC-15 (Diff Rep) *Operating Leases—Incentives*
- NZ SIC-27 (Diff Rep) *Evaluating the Substance of Transactions in the Legal Form of a Lease*
- NZ SIC-29 (Diff Rep) *Service Concession Arrangements: Disclosures*
- NZ SIC-32 (Diff Rep) *Intangible Assets—Web Site Costs*
- NZ IFRIC 4 (Diff Rep) *Determining whether an Arrangement contains a Lease*
- NZ IFRIC 12 (Diff Rep) *Service Concession Arrangements*

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ISBN 978-1-927237-49-6

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NZ International Accounting Standard 17 (Diff Rep) *Leases* (NZ IAS 17 (Diff Rep)) is set out in paragraphs 1–70 and the Appendix. NZ IAS 17 (Diff Rep) is based on International Accounting Standard 17 *Leases* (IAS 17) (2003) initially issued by the International Accounting Standards Committee (IASC) and subsequently revised by the International Accounting Standards Board (IASB). All the paragraphs have equal authority but retain the IASC format of the Standard when it was adopted by the IASB. NZ IAS 17 (Diff Rep) should be read in the context of its objective and the IASB’s Basis for Conclusions on IAS 17 and the New Zealand *Conceptual Framework for Financial Reporting (Diff Rep)* (NZ *Framework (Diff Rep)*). NZ IAS 8 (Diff Rep) *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Any additional material is shown with grey shading and the paragraphs are denoted with “NZ”.

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HISTORY OF AMENDMENTS

Table of Pronouncements – NZ IAS 17 (Diff Rep) *Leases*

This table lists the pronouncement establishing NZ IAS 17 (Diff Rep).

Pronouncements	Date approved	Early operative date	Effective date (annual reporting periods... on or after ...)
NZ IAS 17 (Diff Rep) <i>Leases</i>	Nov 2012	Early application permitted	1 Dec 2012

Table of Amended Paragraphs in NZ IAS 17 (Diff Rep)		
Paragraph affected	How affected	By ... [date]
Paragraph NZ 1.1	Inserted	NZ IAS 17 (Diff Rep) [Nov 2012]
Paragraph 67–68A	Deleted	NZ IAS 17 (Diff Rep) [Nov 2012]
Paragraph 69–69A	Deleted	NZ IAS 17 (Diff Rep) [Nov 2012]
Paragraph NZ 69.1	Inserted	NZ IAS 17 (Diff Rep) [Nov 2012]

The following tables list the pronouncements establishing and substantially amending NZ IAS 17 as applied by qualifying entities prior to the issue of this Standard as NZ IAS 17 (Diff Rep).

Pronouncements	Date approved	Early operative date	Effective date (annual reporting periods... on or after ...)
NZ IAS 17 <i>Leases</i>	Nov 2004	1 Jan 2005	1 Jan 2007
<i>Framework for Differential Reporting for Entities Applying the New Zealand Equivalents to IFRSs Financial Reporting Standards Reporting Regime (Framework for Differential Reporting)</i>	June 2005	1 Jan 2005	1 Jan 2007

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Pronouncements	Date approved	Early operative date	Effective date (annual reporting periods... on or after ...)
NZ IFRS 7 <i>Financial Instruments: Disclosures</i> and a complementary Amendment to IAS 1 <i>Presentation of Financial Statements–Capital Disclosures</i> .	Nov 2005	Early application encouraged	1 Jan 2007
Amendment to the <i>Framework for Differential Reporting</i>	Dec 2005	1 Jan 2005	1 Jan 2007
NZ IAS 1 <i>Presentation of Financial Statements</i> (revised 2007)	Nov 2007	Early application permitted	1 Jan 2009
<i>Omnibus amendments</i> (2007-1)	Nov 2007	Early application permitted	1 Jan 2008
Minor Amendments to NZ IFRSs (2008-1)	Apr 2008	Early application permitted	1 June 2008
<i>Improvements to NZ IFRSs</i>	May 2009	Early application permitted	1 Jan 2010
Minor Amendments to NZ IFRSs	July 2010	Immediate	Immediate

Table of Amended Paragraphs in NZ IAS 17		
Paragraph affected	How affected	By ... [date]
Paragraph NZ 3.1	Inserted	Amendment to the <i>Framework for Differential Reporting</i> [Dec 2005]
Paragraph NZ 3.2	Inserted	<i>Omnibus amendments</i> (2007-1) [Nov 2007]
Paragraph 14	Deleted	<i>Improvements to NZ IFRSs</i> [May 2009]
Paragraph 15	Deleted	<i>Improvements to NZ IFRSs</i> [May 2009]
Paragraph 15A	Inserted	<i>Improvements to NZ IFRSs</i> [May 2009]
Paragraph 31	Amended	NZ IFRS 7 [Nov 2005]
Paragraph 31(b)	Amended	<i>Omnibus amendments</i> (2007-1) [Nov 2007]
Paragraph 35	Amended	NZ IFRS 7 [Nov 2005]
Paragraph 47	Amended	NZ IFRS 7 [Nov 2005]
Paragraph 56	Amended	NZ IFRS 7 [Nov 2005]

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Table of Amended Paragraphs in NZ IAS 17		
Paragraph affected	How affected	By ... [date]
Paragraph 68A	Inserted	<i>Improvements to NZ IFRSs</i> [May 2009]
Paragraph 69A	Inserted	<i>Improvements to NZ IFRSs</i> [May 2009]

Introduction to NZ IAS 17 (Diff Rep)

NZ IAS 17 (Diff Rep) is identical to NZ IAS 17 applied by qualifying entities prior to the issuance of NZ IAS 17 (Diff Rep). That is, there is no change to the recognition, measurement, presentation and disclosure requirements of NZ IAS 17 on adoption of this Standard.

The Standard prescribes, for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases:

Differential Reporting

Qualifying entities are given several concessions to the requirements of this Standard (as identified in the Standard).

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Leases (NZ IAS 17 (Diff Rep))

Objective

- 1 The objective of this Standard is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases.

Scope

NZ 1.1 This Standard applies only to Tier 3 for-profit entities.

- 2 This Standard shall be applied in accounting for all leases other than:
- (a) leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources; and
 - (b) licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights.

However, this Standard shall not be applied as the basis of measurement for:

- (a) property held by lessees that is accounted for as investment property (see NZ IAS 40 (Diff Rep) *Investment Property*);
 - (b) investment property provided by lessors under operating leases (see NZ IAS 40 (Diff Rep));
 - (c) biological assets held by lessees under finance leases (see NZ IAS 41 (Diff Rep) *Agriculture*); or
 - (d) biological assets provided by lessors under operating leases (see NZ IAS 41 (Diff Rep)).
- 3 This Standard applies to agreements that transfer the right to use assets even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. This Standard does not apply to agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other.

NZ 3.1 Entities which qualify for differential reporting concessions in accordance with XRB A1 Accounting Standards Framework are not required to comply with the disclosure requirements in this Standard denoted with an asterisk (*).

NZ 3.2 Qualifying entities are not required to disclose a reconciliation between the total of future minimum lease payments at the end of the reporting period, and their present value as required by paragraph 31(b). Qualifying entities are still required to disclose a time period analysis of the total of future minimum lease payments, and their present value, at the end of the reporting period in accordance with the requirement in paragraph 31(b).

Definitions

4 The following terms are used in this Standard with the meanings specified:

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.

A *finance lease* is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred.

An *operating lease* is a lease other than a finance lease.

A *non-cancellable lease* is a lease that is cancellable only:

- (a) upon the occurrence of some remote contingency;
- (b) with the permission of the lessor;
- (c) if the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or
- (d) upon payment by the lessee of such an additional amount that, at inception of the lease, continuation of the lease is reasonably certain.

The *inception of the lease* is the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease. As at this date:

- (a) a lease is classified as either an operating or a finance lease; and
- (b) in the case of a finance lease, the amounts to be recognised at the commencement of the lease term are determined.

The *commencement of the lease term* is the date from which the lessee is entitled to exercise its right to use the leased asset. It is the date of initial recognition of the lease (ie the recognition of the assets, liabilities, income or expenses resulting from the lease, as appropriate).

The *lease term* is the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

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Minimum lease payments are the payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:

- (a) for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or
- (b) for a lessor, any residual value guaranteed to the lessor by:
 - (i) the lessee;
 - (ii) a party related to the lessee; or
 - (iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

However, if the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Economic life is either:

- (a) the period over which an asset is expected to be economically usable by one or more users; or
- (b) the number of production or similar units expected to be obtained from the asset by one or more users.

Useful life is the estimated remaining period, from the commencement of the lease term, without limitation by the lease term, over which the economic benefits embodied in the asset are expected to be consumed by the entity.

Guaranteed residual value is:

- (a) for a lessee, that part of the residual value that is guaranteed by the lessee or by a party related to the lessee (the amount of the guarantee being the maximum amount that could, in any event, become payable); and
- (b) for a lessor, that part of the residual value that is guaranteed by the lessee or by a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

Unguaranteed residual value is that portion of the residual value of the leased asset, the realisation of which by the lessor is not assured or is guaranteed solely by a party related to the lessor.

Initial direct costs are incremental costs that are directly attributable to negotiating and arranging a lease, except for such costs incurred by manufacturer or dealer lessors.

Gross investment in the lease is the aggregate of:

- (a) the minimum lease payments receivable by the lessor under a finance lease, and
- (b) any unguaranteed residual value accruing to the lessor.

Net investment in the lease is the gross investment in the lease discounted at the interest rate implicit in the lease.

Unearned finance income is the difference between:

- (a) the gross investment in the lease, and
- (b) the net investment in the lease.

The ***interest rate implicit in the lease*** is the discount rate that, at the inception of the lease, causes the aggregate present value of (a) the minimum lease payments and (b) the unguaranteed residual value to be equal to the sum of (i) the fair value of the leased asset and (ii) any initial direct costs of the lessor.

The ***lessee's incremental borrowing rate of interest*** is the rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.

Contingent rent is that portion of the lease payments that is not fixed in amount but is based on the future amount of a factor that changes other than with the passage of time (eg percentage of future sales, amount of future use, future price indices, future market rates of interest).

- 5 A lease agreement or commitment may include a provision to adjust the lease payments for changes in the construction or acquisition cost of the leased property or for changes in some other measure of cost or value, such as general price levels, or in the lessor's costs of financing the lease, during the period between the inception of the lease and the commencement of the lease term. If so, the effect of any such changes shall be deemed to have taken place at the inception of the lease for the purposes of this Standard.
- 6 The definition of a lease includes contracts for the hire of an asset that contain a provision giving the hirer an option to acquire title to the asset upon the fulfilment of agreed conditions. These contracts are sometimes known as hire purchase contracts.

Classification of leases

- 7 The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the

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lessor or the lessee. Risks include the possibilities of losses from idle capacity or technological obsolescence and of variations in return because of changing economic conditions. Rewards may be represented by the expectation of profitable operation over the asset's economic life and of gain from appreciation in value or realisation of a residual value.

8 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.

9 Because the transaction between a lessor and a lessee is based on a lease agreement between them, it is appropriate to use consistent definitions. The application of these definitions to the differing circumstances of the lessor and lessee may result in the same lease being classified differently by them. For example, this may be the case if the lessor benefits from a residual value guarantee provided by a party unrelated to the lessee.

10 Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract.* Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:

- (a) the lease transfers ownership of the asset to the lessee by the end of the lease term;
- (b) the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised;
- (c) the lease term is for the major part of the economic life of the asset even if title is not transferred;
- (d) at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and
- (e) the leased assets are of such a specialised nature that only the lessee can use them without major modifications.

11 Indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease are:

- (a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
- (b) gains or losses from the fluctuation in the fair value of the residual accrue to the lessee (for example, in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and

* See also NZ SIC-27 (Diff Rep) *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

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- (c) the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.
- 12 The examples and indicators in paragraphs 10 and 11 are not always conclusive. If it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease. For example, this may be the case if ownership of the asset transfers at the end of the lease for a variable payment equal to its then fair value, or if there are contingent rents, as a result of which the lessee does not have substantially all such risks and rewards.
- 13 Lease classification is made at the inception of the lease. If at any time the lessee and the lessor agree to change the provisions of the lease, other than by renewing the lease, in a manner that would have resulted in a different classification of the lease under the criteria in paragraphs 7–12 if the changed terms had been in effect at the inception of the lease, the revised agreement is regarded as a new agreement over its term. However, changes in estimates (for example, changes in estimates of the economic life or of the residual value of the leased property), or changes in circumstances (for example, default by the lessee), do not give rise to a new classification of a lease for accounting purposes.
- 14 [Deleted by IASB]
- 15 [Deleted by IASB]
- 15A When a lease includes both land and buildings elements, an entity assesses the classification of each element as a finance or an operating lease separately in accordance with paragraphs 7–13. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life.
- 16 Whenever necessary in order to classify and account for a lease of land and buildings, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the buildings elements in proportion to the relative fair values of the leasehold interests in the land element and buildings element of the lease at the inception of the lease. If the lease payments cannot be allocated reliably between these two elements, the entire lease is classified as a finance lease, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease.
- 17 For a lease of land and buildings in which the amount that would initially be recognised for the land element, in accordance with paragraph 20, is immaterial, the land and buildings may be treated as a single unit for the purpose of lease classification and classified as a finance or operating lease in accordance with paragraphs 7–13. In such a case, the economic life of the buildings is regarded as the economic life of the entire leased asset.
- 18 Separate measurement of the land and buildings elements is not required when the lessee's interest in both land and buildings is classified as an investment property in accordance with NZ IAS 40 (Diff Rep) and the fair value model is adopted. Detailed calculations are required for this assessment only if the classification of one or both elements is otherwise uncertain.

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- 19 In accordance with NZ IAS 40 (Diff Rep), it is possible for a lessee to classify a property interest held under an operating lease as an investment property. If it does, the property interest is accounted for as if it were a finance lease and, in addition, the fair value model is used for the asset recognised. The lessee shall continue to account for the lease as a finance lease, even if a subsequent event changes the nature of the lessee's property interest so that it is no longer classified as investment property. This will be the case if, for example, the lessee:
- (a) occupies the property, which is then transferred to owner-occupied property at a deemed cost equal to its fair value at the date of change in use; or
 - (b) grants a sublease that transfers substantially all of the risks and rewards incidental to ownership of the interest to an unrelated third party. Such a sublease is accounted for by the lessee as a finance lease to the third party, although it may be accounted for as an operating lease by the third party.

Leases in the financial statements of lessees

Finance leases

Initial recognition

- 20 **At the commencement of the lease term, lessees shall recognise finance leases as assets and liabilities in their statements of financial position 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. The discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate shall be used. Any initial direct costs of the lessee are added to the amount recognised as an asset.**
- 21 Transactions and other events are accounted for and presented in accordance with their substance and financial reality and not merely with legal form. Although the legal form of a lease agreement is that the lessee may acquire no legal title to the leased asset, in the case of finance leases the substance and financial reality are that the lessee acquires the economic benefits of the use of the leased asset for the major part of its economic life in return for entering into an obligation to pay for that right an amount approximating, at the inception of the lease, the fair value of the asset and the related finance charge.
- 22 If such lease transactions are not reflected in the lessee's statement of financial position, the economic resources and the level of obligations of an entity are understated, thereby distorting financial ratios. Therefore, it is appropriate for a finance lease to be recognised in the lessee's statement of financial position both as an asset and as an obligation to pay future lease payments. At the

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commencement of the lease term, the asset and the liability for the future lease payments are recognised in the statement of financial position at the same amounts except for any initial direct costs of the lessee that are added to the amount recognised as an asset.

- 23 It is not appropriate for the liabilities for leased assets to be presented in the financial statements as a deduction from the leased assets. If for the presentation of liabilities in the statement of financial position a distinction is made between current and non-current liabilities, the same distinction is made for lease liabilities.
- 24 Initial direct costs are often incurred in connection with specific leasing activities, such as negotiating and securing leasing arrangements. The costs identified as directly attributable to activities performed by the lessee for a finance lease are added to the amount recognised as an asset.

Subsequent measurement

- 25 **Minimum lease payments shall be apportioned between the finance charge and the reduction of the outstanding liability. The finance charge shall be allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents shall be charged as expenses in the periods in which they are incurred.**
- 26 In practice, in allocating the finance charge to periods during the lease term, a lessee may use some form of approximation to simplify the calculation.
- 27 **A finance lease gives rise to depreciation expense for depreciable assets as well as finance expense for each accounting period. The depreciation policy for depreciable leased assets shall be consistent with that for depreciable assets that are owned, and the depreciation recognised shall be calculated in accordance with NZ IAS 16 (Diff Rep) *Property, Plant and Equipment* and NZ IAS 38 (Diff Rep) *Intangible Assets*. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life.**
- 28 The depreciable amount of a leased asset is allocated to each accounting period during the period of expected use on a systematic basis consistent with the depreciation policy the lessee adopts for depreciable assets that are owned. If there is reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset; otherwise the asset is depreciated over the shorter of the lease term and its useful life.
- 29 The sum of the depreciation expense for the asset and the finance expense for the period is rarely the same as the lease payments payable for the period, and it is, therefore, inappropriate simply to recognise the lease payments payable as an expense. Accordingly, the asset and the related liability are unlikely to be equal in amount after the commencement of the lease term.
- 30 To determine whether a leased asset has become impaired, an entity applies NZ IAS 36 (Diff Rep) *Impairment of Assets*.

Disclosures

- 31 Lessees shall, in addition to meeting the requirements of NZ IFRS 7 (Diff Rep) *Financial Instruments: Disclosures*, make the following disclosures for finance leases:
- (a) for each class of asset, the net carrying amount at the end of the reporting period.
 - (b) a reconciliation between the total of future minimum lease payments at the end of the reporting period, and their present value.* In addition, an entity shall disclose the total of future minimum lease payments at the end of the reporting period, and their present value, for each of the following periods:
 - (i) not later than one year;
 - (ii) later than one year and not later than five years;
 - (iii) later than five years.
 - * (c) contingent rents recognised as an expense in the period.
 - (d) the total of future minimum sublease payments expected to be received under non-cancellable subleases at the end of the reporting period.
 - * (e) a general description of the lessee's material leasing arrangements including, but not limited to, the following:
 - (i) the basis on which contingent rent payable is determined;
 - (ii) the existence and terms of renewal or purchase options and escalation clauses; and
 - (iii) restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing.
- 32 In addition, the requirements for disclosure in accordance with NZ IAS 16 (Diff Rep), NZ IAS 36 (Diff Rep), NZ IAS 38 (Diff Rep), NZ IAS 40 (Diff Rep) and NZ IAS 41 (Diff Rep) apply to lessees for assets leased under finance leases.

Operating leases

- 33 Lease payments under an operating lease shall be recognised as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.†
- 34 For operating leases, lease payments (excluding costs for services such as insurance and maintenance) are recognised as an expense on a straight-line basis unless another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis.

* Qualifying entities are not required to prepare this reconciliation.

† See also NZ SIC-15 (Diff Rep) *Operating Leases—Incentives*.

Disclosures

- 35 Lessees shall, in addition to meeting the requirements of NZ IFRS 7 (Diff Rep), make the following disclosures for operating leases:
- (a) the total of future minimum lease payments under non-cancellable operating leases for each of the following periods:
 - (i) not later than one year;
 - (ii) later than one year and not later than five years;
 - (iii) later than five years.
 - (b) the total of future minimum sublease payments expected to be received under non-cancellable subleases at the end of the reporting period.
 - (c) lease and sublease payments recognised as an expense in the period, with separate amounts for minimum lease payments, contingent rents, and sublease payments.
 - *(d) a general description of the lessee's significant leasing arrangements including, but not limited to, the following:
 - (i) the basis on which contingent rent payable is determined;
 - (ii) the existence and terms of renewal or purchase options and escalation clauses; and
 - (iii) restrictions imposed by lease arrangements, such as those concerning dividends, additional debt and further leasing.

Leases in the financial statements of lessors

Finance leases

Initial recognition

- 36 Lessors shall recognise assets held under a finance lease in their statements of financial position and present them as a receivable at an amount equal to the net investment in the lease.
- 37 Under a finance lease substantially all the risks and rewards incidental to legal ownership are transferred by the lessor, and thus the lease payment receivable is treated by the lessor as repayment of principal and finance income to reimburse and reward the lessor for its investment and services.
- 38 Initial direct costs are often incurred by lessors and include amounts such as commissions, legal fees and internal costs that are incremental and directly attributable to negotiating and arranging a lease. They exclude general overheads such as those incurred by a sales and marketing team. For finance leases other than

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those involving manufacturer or dealer lessors, initial direct costs are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term. The interest rate implicit in the lease is defined in such a way that the initial direct costs are included automatically in the finance lease receivable; there is no need to add them separately. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease are excluded from the definition of initial direct costs. As a result, they are excluded from the net investment in the lease and are recognised as an expense when the selling profit is recognised, which for a finance lease is normally at the commencement of the lease term.

Subsequent measurement

- 39 The recognition of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.**
- 40 A lessor aims to allocate finance income over the lease term on a systematic and rational basis. This income allocation is based on a pattern reflecting a constant periodic return on the lessor's net investment in the finance lease. Lease payments relating to the period, excluding costs for services, are applied against the gross investment in the lease to reduce both the principal and the unearned finance income.
- 41 Estimated unguaranteed residual values used in computing the lessor's gross investment in a lease are reviewed regularly. If there has been a reduction in the estimated unguaranteed residual value, the income allocation over the lease term is revised and any reduction in respect of amounts accrued is recognised immediately.
- 41A An asset under a finance lease that is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with NZ IFRS 5 (Diff Rep) *Non-current Assets Held for Sale and Discontinued Operations* shall be accounted for in accordance with that Standard.
- 42 Manufacturer or dealer lessors shall recognise selling profit or loss in the period, in accordance with the policy followed by the entity for outright sales. If artificially low rates of interest are quoted, selling profit shall be restricted to that which would apply if a market rate of interest were charged. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease shall be recognised as an expense when the selling profit is recognised.**
- 43 Manufacturers or dealers often offer to customers the choice of either buying or leasing an asset. A finance lease of an asset by a manufacturer or dealer lessor gives rise to two types of income:
- (a) profit or loss equivalent to the profit or loss resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and
 - (b) finance income over the lease term.

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- 44 The sales revenue recognised at the commencement of the lease term by a manufacturer or dealer lessor is the fair value of the asset, or, if lower, the present value of the minimum lease payments accruing to the lessor, computed at a market rate of interest. The cost of sale recognised at the commencement of the lease term is the cost, or carrying amount if different, of the leased property less the present value of the unguaranteed residual value. The difference between the sales revenue and the cost of sale is the selling profit, which is recognised in accordance with the entity's policy for outright sales.
- 45 Manufacturer or dealer lessors sometimes quote artificially low rates of interest in order to attract customers. The use of such a rate would result in an excessive portion of the total income from the transaction being recognised at the time of sale. If artificially low rates of interest are quoted, selling profit is restricted to that which would apply if a market rate of interest were charged.
- 46 Costs incurred by a manufacturer or dealer lessor in connection with negotiating and arranging a finance lease are recognised as an expense at the commencement of the lease term because they are mainly related to earning the manufacturer's or dealer's selling profit.

Disclosures

- 47 Lessors shall, in addition to meeting the requirements in NZ IFRS 7 (Diff Rep), disclose the following for finance leases:
- ***(a) a reconciliation between the gross investment in the lease at the end of the reporting period, and the present value of minimum lease payments receivable at the end of the reporting period. In addition, an entity shall disclose the gross investment in the lease and the present value of minimum lease payments receivable at the end of the reporting period, for each of the following periods:**
 - (i) not later than one year;**
 - (ii) later than one year and not later than five years;**
 - (iii) later than five years.**
 - (b) unearned finance income.**
 - (c) the unguaranteed residual values accruing to the benefit of the lessor.**
 - ***(d) the accumulated allowance for uncollectible minimum lease payments receivable.**
 - ***(e) contingent rents recognised as income in the period.**
 - ***(f) a general description of the lessor's material leasing arrangements.**
- 48 As an indicator of growth it is often useful also to disclose the gross investment less unearned income in new business added during the period, after deducting the relevant amounts for cancelled leases.

Operating leases

- 49 Lessors shall present assets subject to operating leases in their statements of financial position according to the nature of the asset.
- 50 Lease income from operating leases shall be recognised in income on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished.*
- 51 Costs, including depreciation, incurred in earning the lease income are recognised as an expense. Lease income (excluding receipts for services provided such as insurance and maintenance) is recognised on a straight-line basis over the lease term even if the receipts are not on such a basis, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished.
- 52 Initial direct costs incurred by lessors in negotiating and arranging an operating lease shall be added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease income.
- 53 The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets, and depreciation shall be calculated in accordance with NZ IAS 16 (Diff Rep) and NZ IAS 38 (Diff Rep).
- 54 To determine whether a leased asset has become impaired, an entity applies NZ IAS 36 (Diff Rep).
- 55 A manufacturer or dealer lessor does not recognise any selling profit on entering into an operating lease because it is not the equivalent of a sale.

Disclosures

- *56 Lessors shall, in addition to meeting the requirements of NZ IFRS 7 (Diff Rep), disclose the following for operating leases:
- (a) the future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods:
 - (i) not later than one year;
 - (ii) later than one year and not later than five years;
 - (iii) later than five years.
 - (b) total contingent rents recognised as income in the period.
 - (c) a general description of the lessor's leasing arrangements.

* See also NZ SIC-15 (Diff Rep) *Operating Leases-Incentives*.

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- 57 In addition, the disclosure requirements in NZ IAS 16 (Diff Rep), NZ IAS 36 (Diff Rep), NZ IAS 38 (Diff Rep), NZ IAS 40 (Diff Rep) and NZ IAS 41 (Diff Rep) apply to lessors for assets provided under operating leases.

Sale and leaseback transactions

- 58 A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent because they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.
- 59 **If a sale and leaseback transaction results in a finance lease, any excess of sales proceeds over the carrying amount shall not be immediately recognised as income by a seller-lessee. Instead, it shall be deferred and amortised over the lease term.**
- 60 If the leaseback is a finance lease, the transaction is a means whereby the lessor provides finance to the lessee, with the asset as security. For this reason it is not appropriate to regard an excess of sales proceeds over the carrying amount as income. Such excess is deferred and amortised over the lease term.
- 61 **If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, any profit or loss shall be recognised immediately. If the sale price is below fair value, any profit or loss shall be recognised immediately except that, if the loss is compensated for by future lease payments at below market price, it shall be deferred and amortised in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the excess over fair value shall be deferred and amortised over the period for which the asset is expected to be used.**
- 62 If the leaseback is an operating lease, and the lease payments and the sale price are at fair value, there has in effect been a normal sale transaction and any profit or loss is recognised immediately.
- 63 **For operating leases, if the fair value at the time of a sale and leaseback transaction is less than the carrying amount of the asset, a loss equal to the amount of the difference between the carrying amount and fair value shall be recognised immediately.**
- 64 For finance leases, no such adjustment is necessary unless there has been an impairment in value, in which case the carrying amount is reduced to recoverable amount in accordance with NZ IAS 36 (Diff Rep).
- 65 Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of material leasing arrangements leads to disclosure of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.
- 66 Sale and leaseback transactions may trigger the separate disclosure criteria in NZ IAS 1 (Diff Rep) *Presentation of Financial Statements*.

Transitional provisions

67–68A [Deleted]

Effective date

69–69A [Deleted]

NZ 69.1 This Standard applies to annual periods beginning on or after 1 December 2012. Early application is permitted. This Standard replaces NZ IAS 17 as applied by qualifying entities prior to the issuance of this Standard. There are no changes to the requirements of NZ IAS 17 as it applied to qualifying entities.

Withdrawal of IAS 17 (revised 1997)

70 [Paragraph 70 is not reproduced. The withdrawal of previous IASB pronouncements is not relevant to this Standard.]