

## Exposure Draft (ED) 75 Summary—*Leases*

This summary provides an overview of [ED 75, \*Leases\*](#).

<b>Project Objective:</b>	This ED proposes new requirements for lease accounting aligned with IFRS 16, <i>Leases</i> to replace IPSAS 13, <i>Leases</i> . In developing ED 75, the IPSASB considered the public sector applicability of the principles drawn from IFRS 16, as well as the comments received on <a href="#">ED 64, <i>Leases</i></a> . ED 75 proposes an IFRS 16 aligned accounting model and principles for lessees and lessors.
<b>The Project Stage:</b>	The IPSASB issued ED 75 in January 2021.
<b>Next Steps:</b>	The IPSASB seeks feedback on ED 75 to guide it in developing a final International Public Sector Accounting Standard® (IPSAS®) that revises accounting requirements for leases.
<b>Comment Deadline:</b>	ED 75 is open for public comment until May 17, 2021.
<b>How to Respond:</b>	Respondents are asked to submit their comments electronically through the IPSASB website, using the " <a href="#">Submit a Comment</a> " link. Please submit comments in both a PDF and a Word file. All comments will be considered a matter of public record and will be posted on the website.

## Brief History of the IPSASB's Leases Project

### Why is IPSASB Undertaking the Leases Project?

IPSAS 13, *Leases* was drawn primarily from International Accounting Standard (IAS) 17, *Leases*, issued by the International Accounting Standards Board (IASB). In January 2016, the IASB issued International Financial Reporting Standard (IFRS) 16, *Leases*. IFRS 16 replaces IAS 17 and a number of related interpretations.

After consultation with constituents, the IPSASB decided to revise its leasing requirements. The IPSASB also decided to consider public sector issues, including concessionary leases, which are prevalent in the public sector.

### ED 64, *Leases*

In January 2018, the IPSASB published [ED 64, \*Leases\*](#) that proposed:

- (a) A single right-of-use model for lease accounting for lessees and lessors; and
- (b) Specific public sector accounting requirements for concessionary leases.

### Constituents' Feedback and Why the IPSASB Did Not Take Forward the ED 64 Lessor Accounting Proposals

Responses to ED 64 showed that constituents supported the proposed changes in lessee accounting, but:

- (a) Were divided on whether a departure from the IFRS 16 lessor accounting approach was justified; and
- (b) Lacked consensus on the economics of, and the proposed accounting for lessor accounting.

After careful consideration of the ED 64 feedback, the IPSASB identified three options to progress the project:

1. Retain IPSAS 13;
2. Develop a Standard aligned with IFRS 16; or
3. Continue with a Standard based on ED 64.

The IPSASB decided the public interest would be best served by proceeding with an IFRS 16–aligned Standard because:

- (a) It would address the key problem of 'off-balance sheet' leasing opportunities permitted by IPSAS 13 and be less costly to adopt;

- (b) Feedback to ED 64 made it clear that resolving the problems identified with the proposed lessor accounting model was unlikely to be achievable within a reasonable timeframe; and
- (c) Guidance on public sector specific issues, such as concessionary leases, would be better developed once the revised leasing model was agreed.

### ED 75, *Leases* and Request for Information

In light of constituents' feedback to ED 64, and the agreed approach, the IPSASB agreed to manage the project going forward as follows:

- (a) Phase One, to deal with lease accounting model(s) for both lessees and lessors based on IFRS 16, by issuing ED 75; and
- (b) Phase Two, to deal with public sector specific issues, such as concessionary leases, access rights, and other similar 'lease-like' arrangements in the public sector, informed by responses to a [Request for Information, \*Concessionary Leases and Other Arrangements Similar to Leases\*](#) issued together with ED 75.

## What Changes Does ED 75 Propose for Lessee Accounting?

ED 75 proposes a right-of-use model for lessees, which distinguishes the right to use an underlying asset (which the lessee controls) and the underlying asset itself (which the lessee does not control).

### **Recognition and Measurement of Leases— General Guidance**

ED 75 proposes that lessees recognize:

- (a) A right-of-use asset because they control the right to use the underlying asset, compared with IPSAS 13, where the lessee recognizes the underlying asset when the lease is classified as a finance lease, but not when it is classified as an operating lease.
- (b) A lease liability because they have a present obligation to make future lease payments in accordance with the lease contract (once the underlying asset has been made available, and the lessee has the right use it). Under IPSAS 13, a lease liability is not recognized when the lessee classifies the lease as operating lease.

ED 75 proposes measuring the right-of-use asset and the lease liability at cost (the present value of the future lease payments).

### **Recognition Exemptions**

ED 75 proposes two recognition exemptions for:

- (a) Short-term leases; and
- (b) Leases for which the underlying asset is of low value.

ED 75 proposes that leases, which qualify for the recognition exemptions, be accounted for consistent with how operating leases are treated in IPSAS 13 (expenses recognized on a straight-line basis over the lease term or another systematic basis). IPSAS 13 does not provide recognition exemptions.

## What Changes Does ED 75 Propose for Lessor Accounting?

ED 75 proposes to substantially carry forward the lessor accounting in IPSAS 13.

However, ED 75 also provides additional guidance and clarifications to help with applying the risks and rewards model incidental to ownership.

### Risks and Rewards Incidental to Ownership Model Substantially Carry Forward

ED 75 proposes to substantially carry forward the lessor accounting in IPSAS 13. However, ED 75 proposes specific changes to the model for consistency with the lessee accounting model.

### Initial Direct Costs Definition

ED 75 proposes to define initial direct costs consistently with the definition of incremental costs of obtaining a binding arrangement in [\[draft\] IPSAS \[X\] \(ED 70, Revenue with Performance Obligations\)](#). Therefore, the costs incurred by a lessor to obtain a lease are accounted for consistently with costs incurred in relation to other contracts with purchasers.

### Lease Modifications

ED 75 proposes to account for a modification to a finance lease as a separate lease if:

- (a) The modification increases the scope of the lease by adding the right for the lessee to use one or more underlying assets; and
- (b) The consideration received for the lease increases by an amount commensurate with the stand-alone price for the increase in scope.

ED 75 proposes to account for a modification to an operating lease as a new lease from the effective date of

the modification, considering any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease.

IPSAS 13 does not include specific requirements relating to lease modifications.

### Subleases

ED 75 proposes to classify subleases by intermediate lessors by reference to the right-of-use assets arising from the head lease and not by reference to the underlying asset, which differs from the current requirements in IPSAS 13.

### Disclosures

ED 75 proposes enhanced disclosures to better evaluate the amount, timing and uncertainty of cash flows arising from a lessor's leasing activities, such as:

- (a) Table of income;
- (b) Information about residual asset risk;
- (c) Information about assets subject to operating leases;
- (d) Maturity analysis; and
- (e) Changes in net investment in finance leases.

## What Changes Does ED 75 Propose for Sale and Leaseback Transactions?

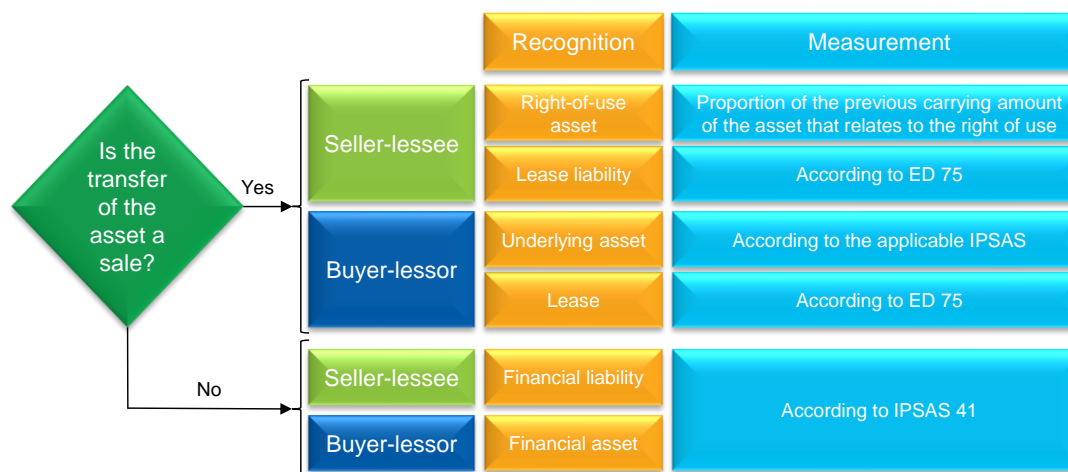
ED 75 proposes to recognize right-of-use assets and its related lease liabilities for all sale and leaseback transactions.

### Less Opportunity for 'Off-Balance Sheet' Accounting and Improved Comparability of Financial Information

IPSAS 13 provides an opportunity for an entity selling the assets that it owns and lease those assets back through operating leases because it would report less assets and less financial debt—thus improving its financial indicators. However, in substance the entity was neither changing its operations nor the use of the assets that it leased back.

ED 75 proposes recognizing the rights to use those same assets and related liabilities for all sale and leaseback transactions and restricts the amount of any gain recognized on the sale of an asset.

As a result, the proposals in ED 75 provide less opportunity for entities to enter into sale and leaseback transactions and more comparability of financial information reported in the statement of financial position between entities that lease assets and entities that buy assets.



## What Other Changes Does ED 75 Propose for Lease Accounting?

ED 75 proposes additional guidance in several areas of lease accounting.

### Definition of a Lease

ED 75 proposes a definition of a lease which is consistent with IPSAS 13. However, ED 75 proposes changes to the guidance on how to apply the definition. The changes are based on the concept of control within the definition of a lease.

### Identifying a Lease

ED 75 proposes guidance to help in determining whether a contract conveys the right to control the use of an identified asset over a period of time. The proposed guidance requires an entity to assess whether, throughout the period of use, the customer has both of the following:

- (a) The right to obtain substantially all of the economic benefits or service potential from use of the identified asset; and
- (b) The right to direct the use of the identified asset.

The IPSASB decided to refer to both “economic benefits” and “service potential” when identifying a lease because it is consistent with *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* in referring to assets in terms of both economic benefits and service potential.

### Combination of Contracts

ED 75 proposes that an entity shall combine two or more contracts entered into at or near the same time with the same counterparty (or related parties of the counterparty), and account for the contracts as a single contract if one or more of the following criteria are met:

- (a) The contracts are negotiated as a package with an overall commercial objective that cannot be understood without considering the contracts together;
- (b) The amount of consideration to be paid in one contract depends on the price or performance of the other contract; or
- (c) The rights to use underlying assets conveyed in the contracts (or some rights to use underlying assets conveyed in each of the contracts) form a single lease component.

### Variable Lease Payments

ED 75 proposes measurement of lease liabilities includes variable lease payments, such as:

- (a) In-substance fixed lease payments; and
- (b) That depend on an index or a rate.

## Next Steps:

The deadline for comments is May 17, 2021.

During the comment period, the IPSASB members are available to discuss the proposals with a wide range of parties.



### How Can I Comment on the Proposals?

The ED includes Specific Matters for Comment (SMCs) on which the IPSASB is seeking views.

Respondents may choose to answer all SMCs or just a selected few. The IPSASB welcomes comments on any other matters respondents think it should consider in forming its views.

Respondents are asked to submit their comments electronically through the IPSASB website, using the [“Submit a Comment”](#) link. Please submit comments in both a PDF and a Word file.

All comments will be considered a matter of public record and will be posted on the IPSASB website.

The IPSASB will carefully consider all feedback and discuss responses at its public meetings after the comment period has ended.

### Stay Informed

The IPSASB’s website will indicate the meetings at which feedback on the ED will be discussed. The dates and the locations of 2021 meetings are available at:

<http://www.ipsasb.org/meetings>

To stay up to date about the project, please visit:

<http://www.ipsasb.org/projects/leases>

### Specific Matters for Comment

ED 75 includes three Specific Matters for Comment, which cover the following issues:

**SMC 1:** The proposed modifications to IFRS 16 for the public sector.

**SMC 2:** The proposed retention of the fair value definition from IPSAS 13 and IFRS 16.

**SMC 3:** The proposed addition of the term “service potential”, where appropriate, together with “economic benefits” in the application guidance of ED 75 on identifying a lease.

### Request for Information

The IPSASB issued the [Request for Information, Concessionary Leases and Other Arrangements Similar to Leases](#) together with ED 75.

This information will inform the IPSASB on what guidance, if any, is required.

Issues identified during the Request for Information process will be considered in the context of the finalization of a Standard based on ED 75.