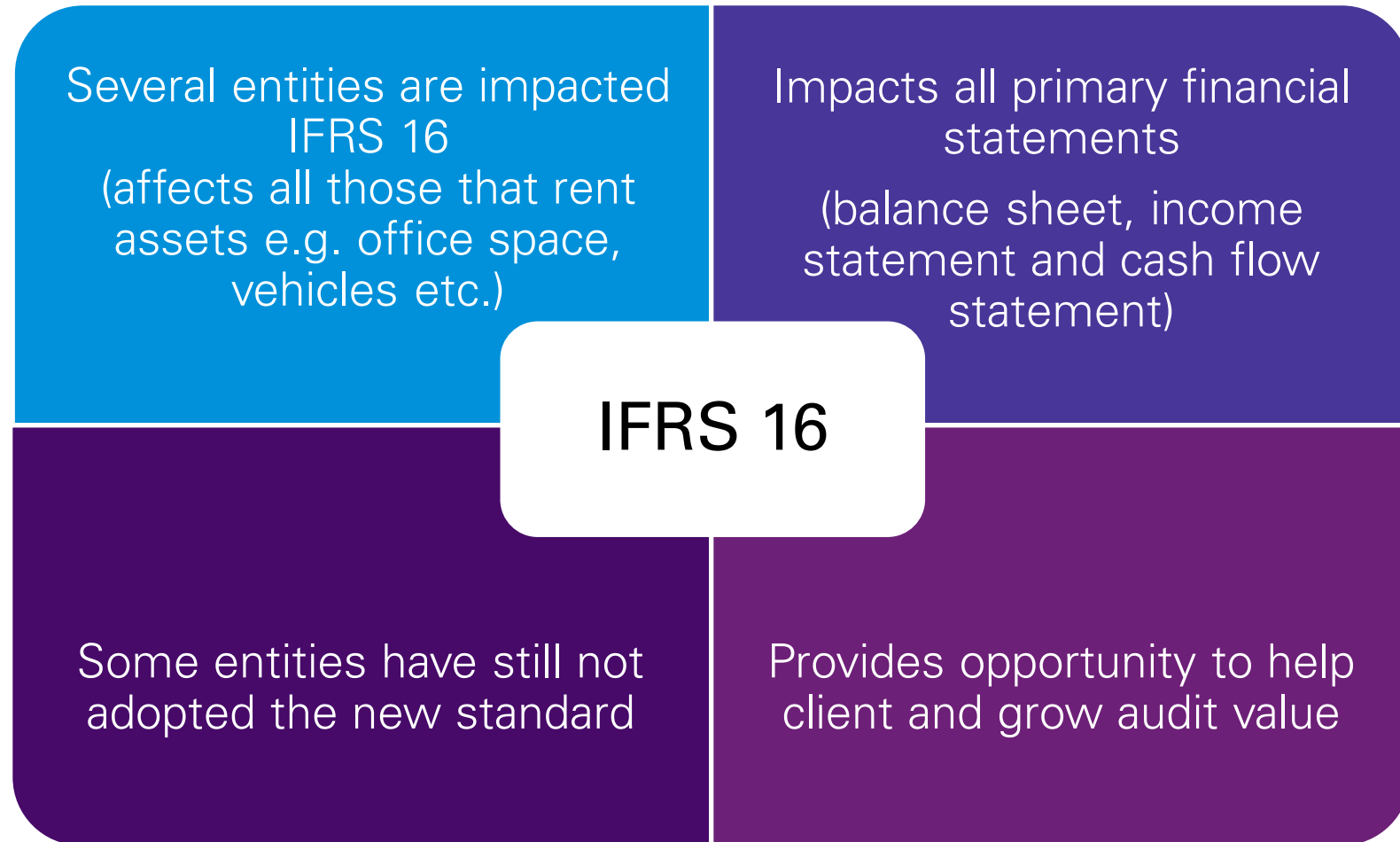


Spotlight on Auditing IFRS 16 Leases



Why is this important?



Agenda

- Lease definition
- Lease Accounting
- Lessee Exceptions
- Audit considerations

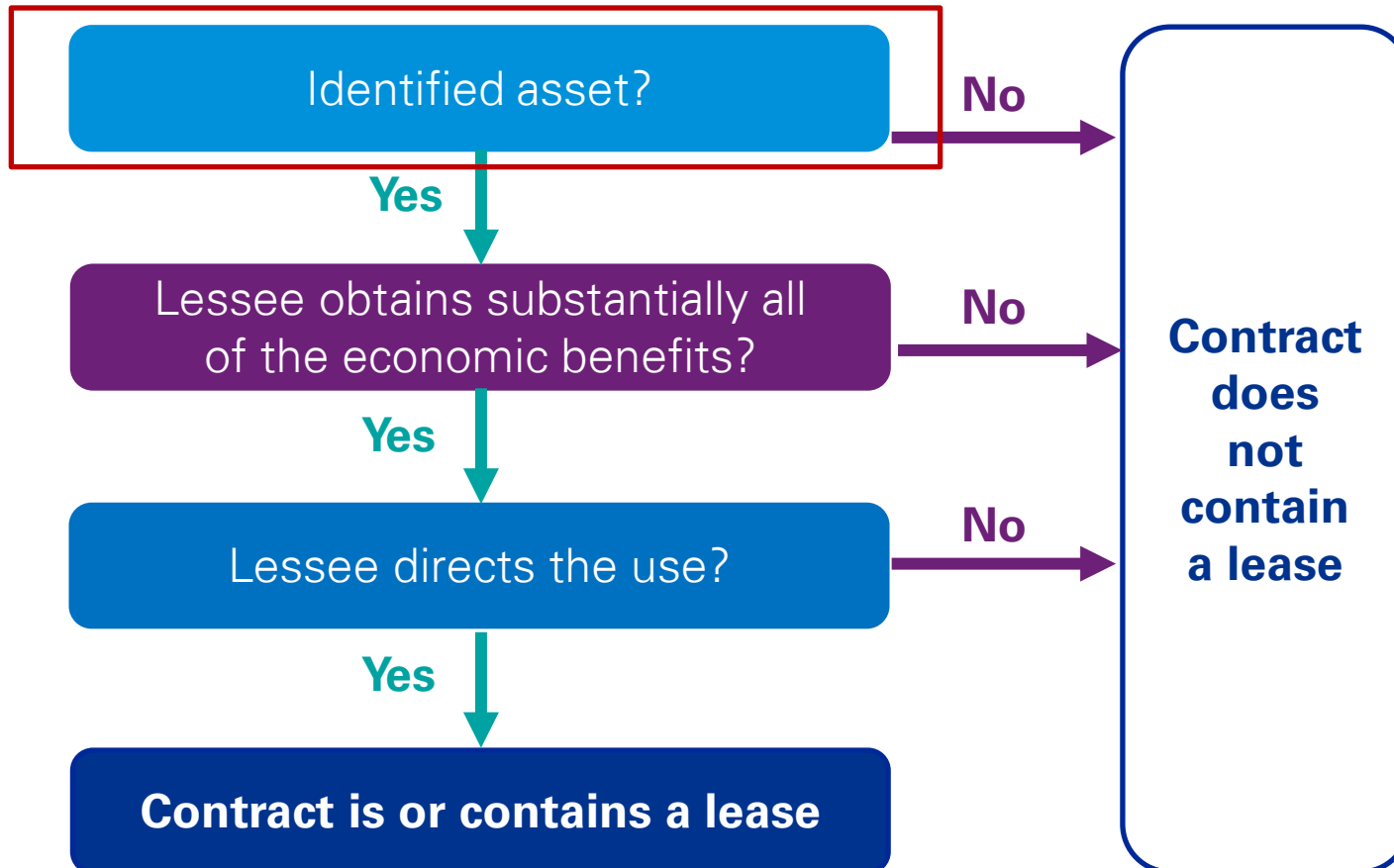




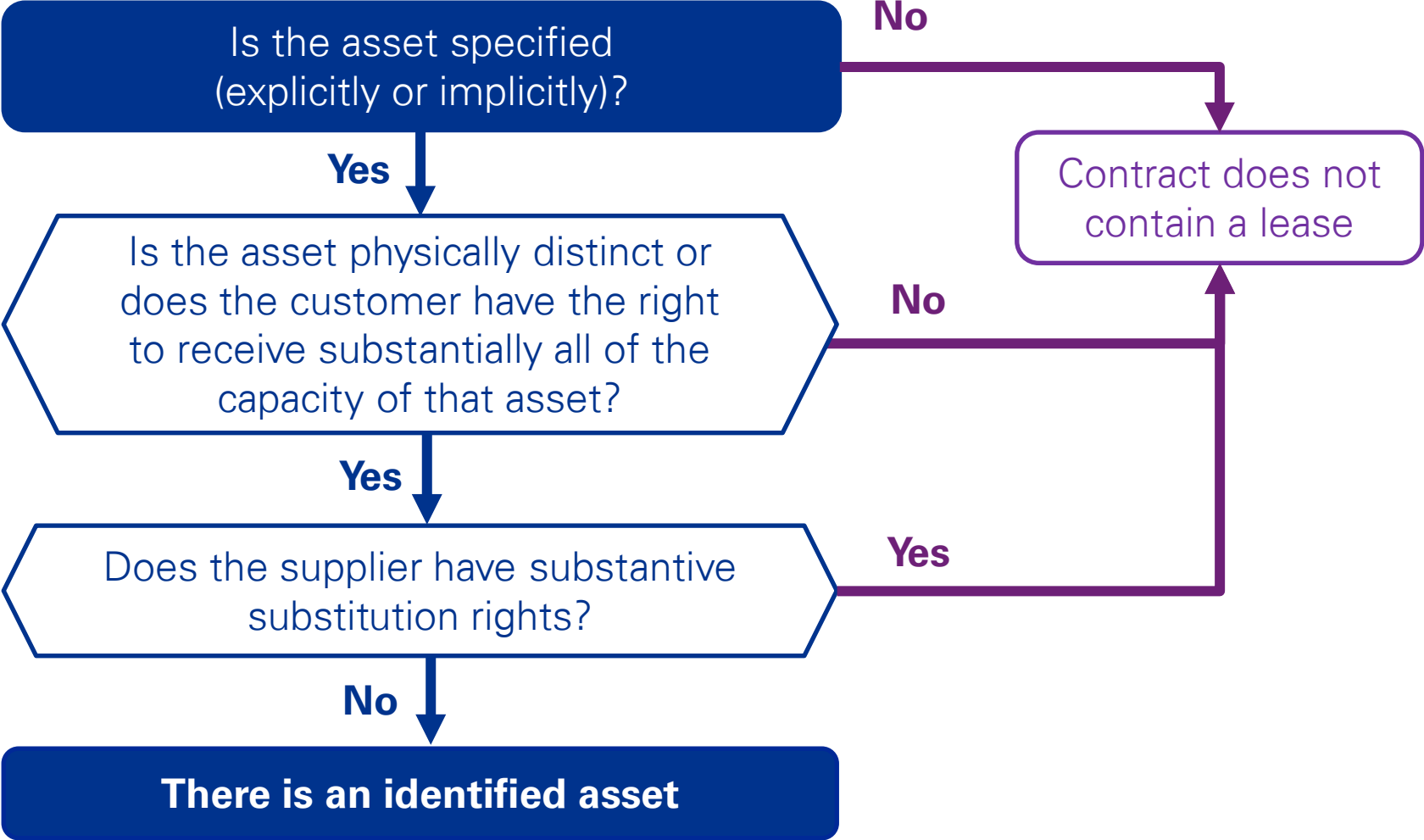
Lease Definition

Lease definition

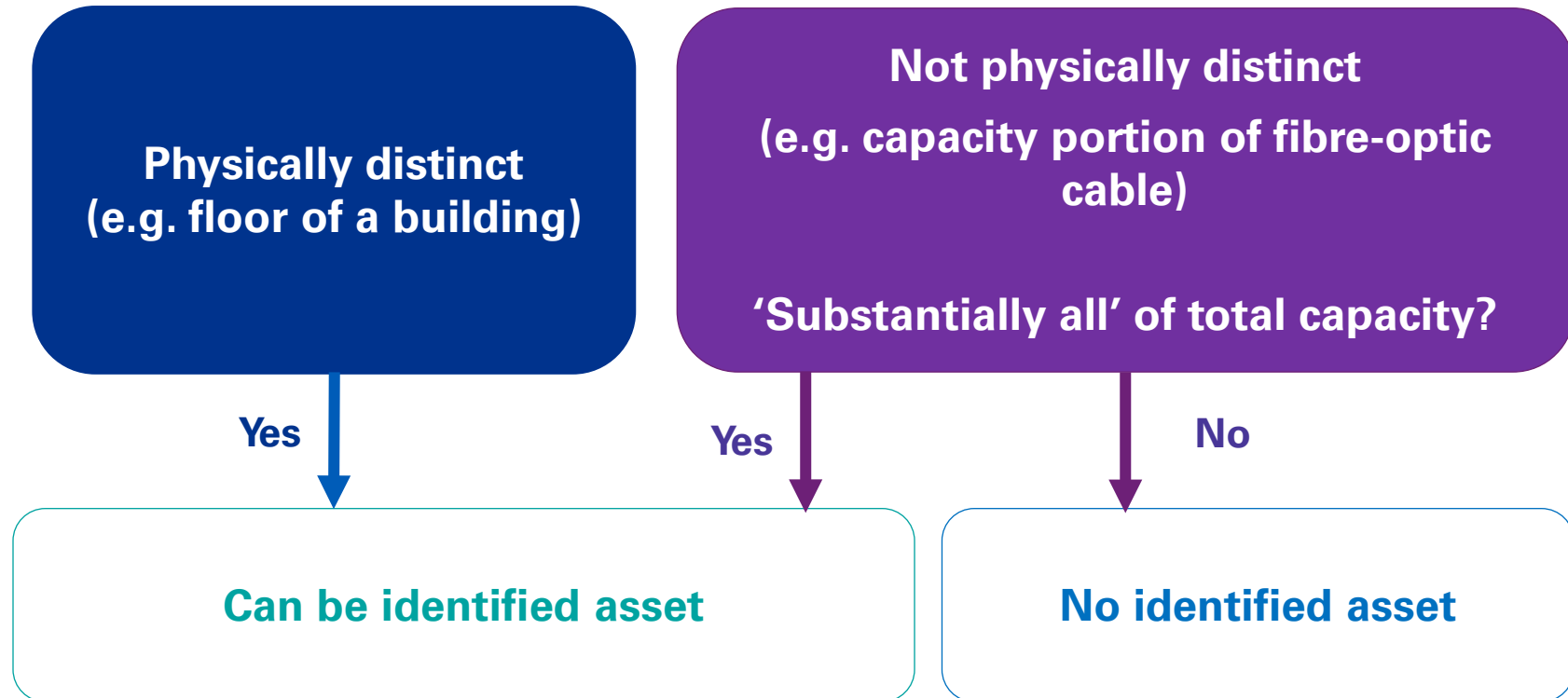
Contract, or part of a contract, that conveys the **right to use** an **asset** for a **period of time** in exchange for **consideration**



Identified asset



Capacity portions

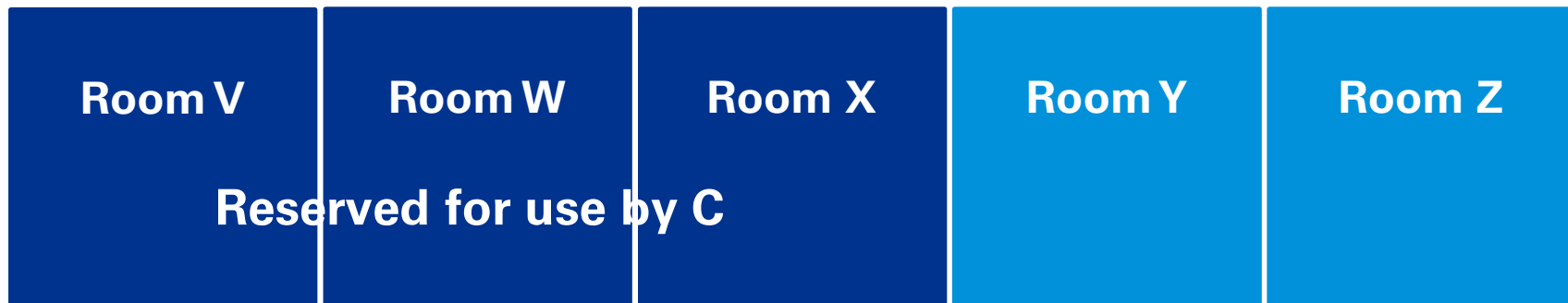


Question: Capacity portions

Customer C enters into an arrangement with Supplier S for the right to store its products in a specified storage warehouse.

Within this warehouse, rooms V, W and X are contractually allocated to C for its exclusive use.

S has no substitution rights. Rooms V, W and X represent 60% of the warehouse's total storage capacity.



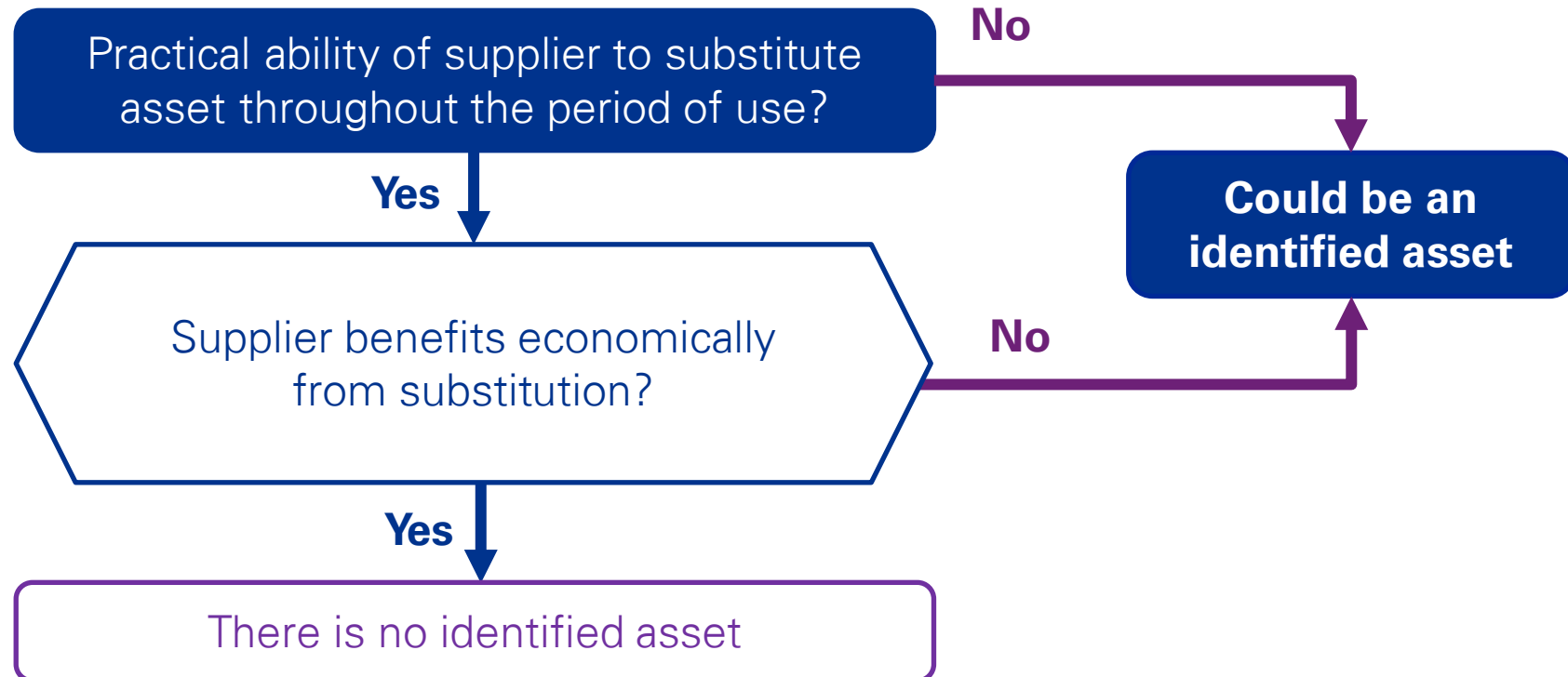
Is there an identified asset?

Question: Capacity portions

Is there an identified asset?

- A. Yes
- B. No

Substantive substitution rights



Example : Practical ability to substitute

Customer L enters into a five-year contract with a freight carrier Supplier M to transport a specified quantity of goods.

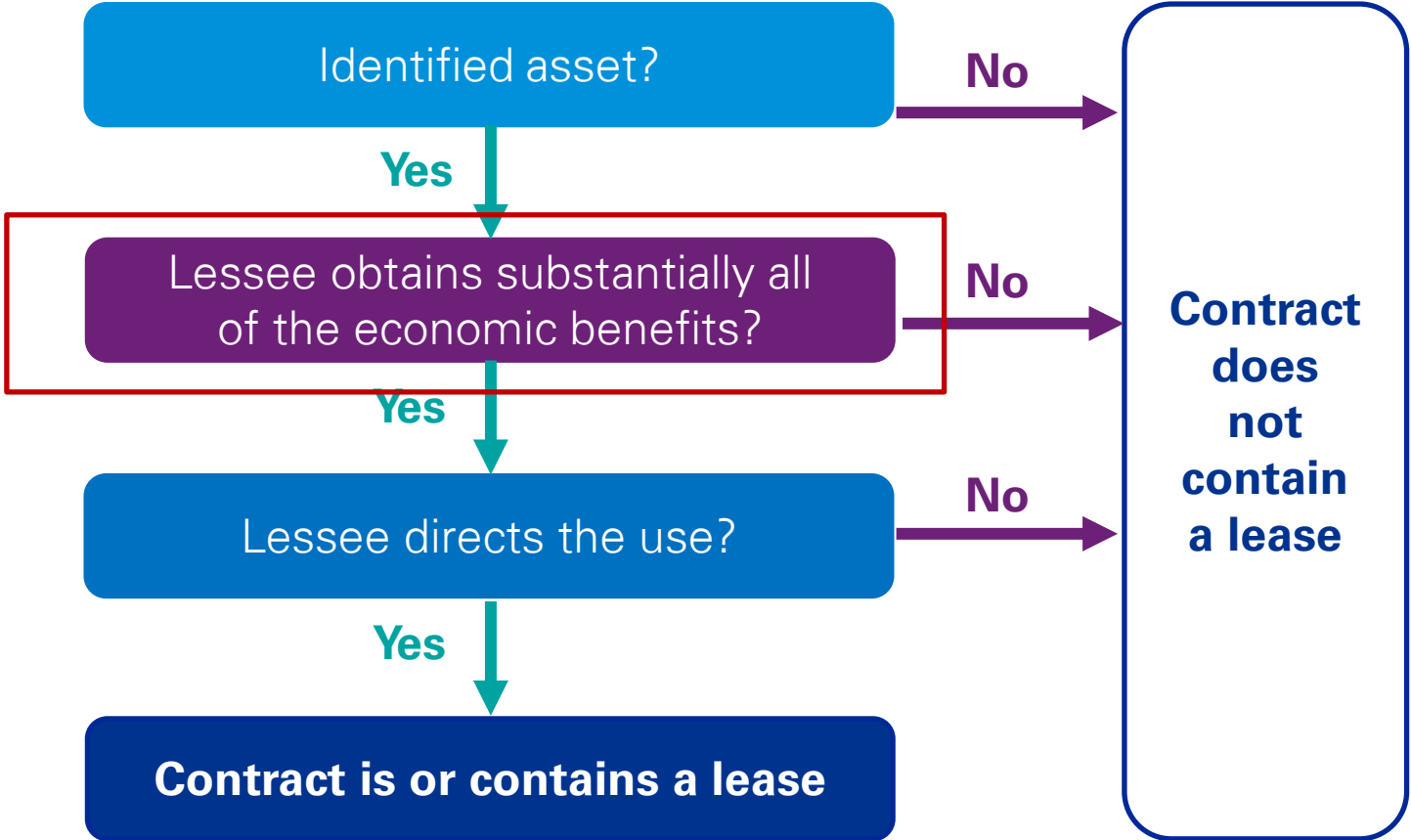
M uses rail cars of a particular specification that are stored at its premises and has a large pool of similar rail cars that can be used to fulfil the requirements of the contract.

Does M have the practical ability to substitute the assets?

Yes, M has the practical ability to substitute the assets because the rail cars are stored at M's premises, it has a large pool of similar rail cars and substitution costs are minimal.

Lease definition

Contract, or part of a contract, that conveys the **right to use** an **asset** for a **period of time** in exchange for **consideration**



Case study



25-year contract for customised solar panel output. Supplier receives renewable energy credits related to use.



Contract to use office. Tenant sublets 25% of space.

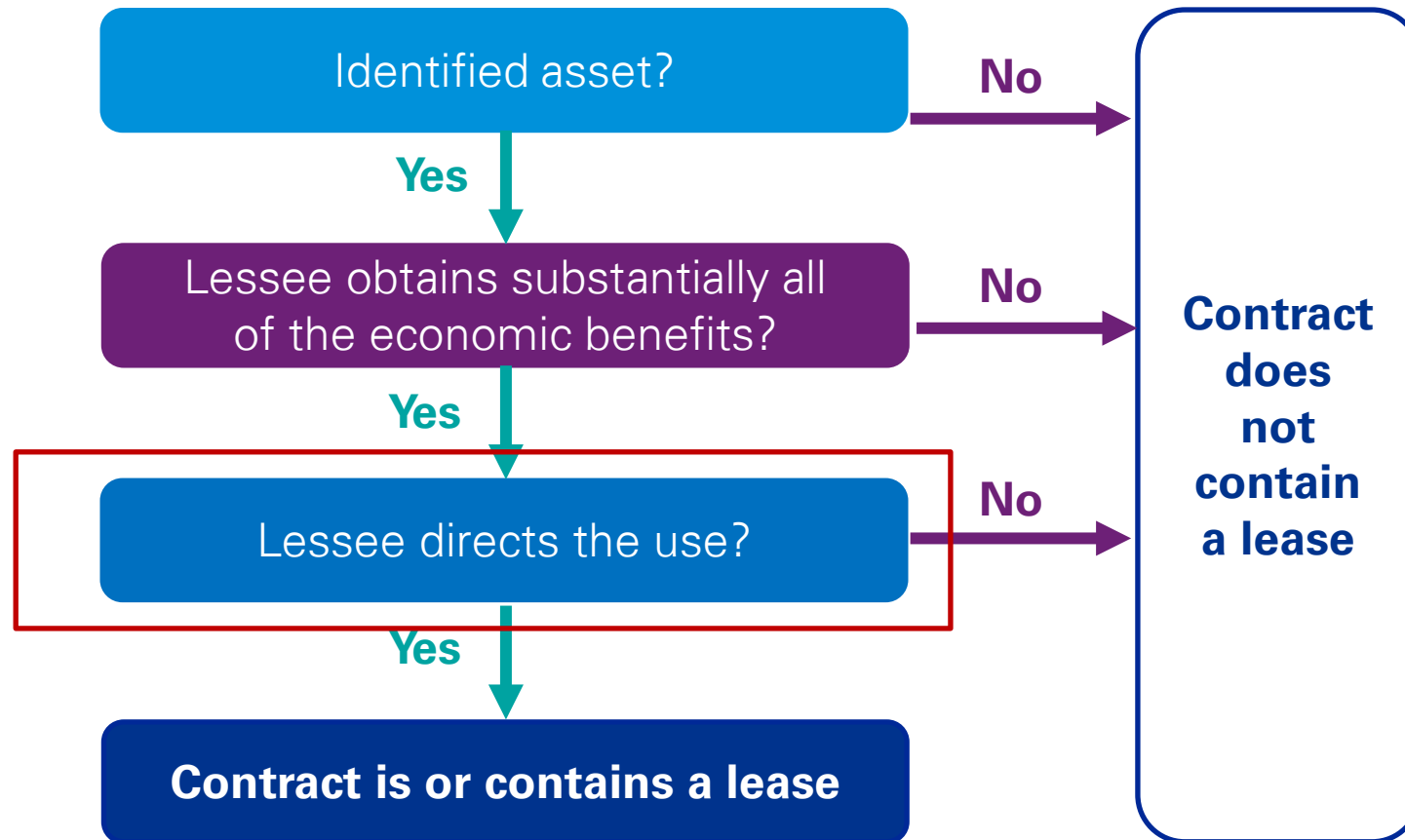


Contract to use a retail store within a mall. Rental = fixed amount + 20% of revenue.

Primary output	✓	✓	✓
+ Other benefits	✗	✓	None
= Substantially all economic benefits	✗	✓	✓

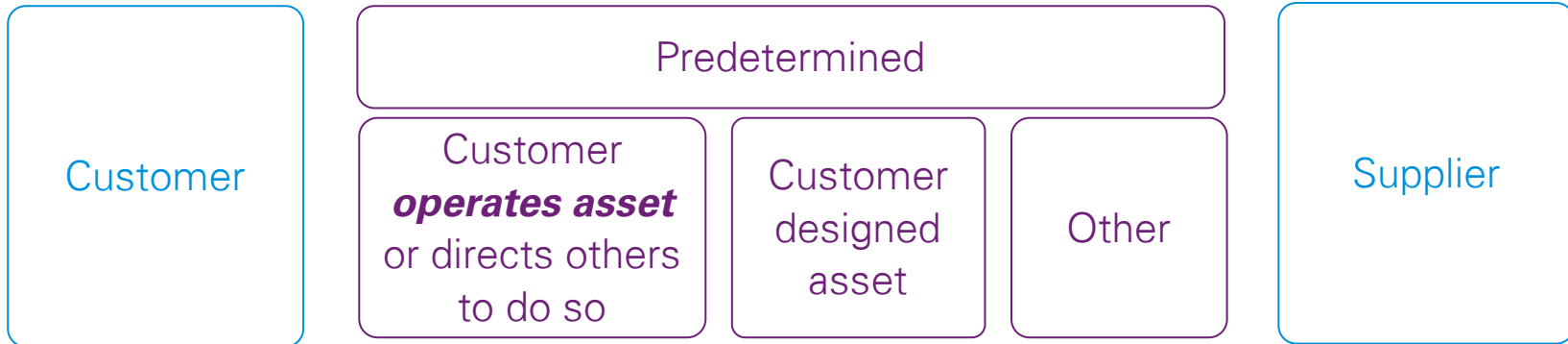
Lease definition

Contract, or part of a contract, that conveys the **right to use** an **asset** for a **period of time** in exchange for **consideration**



Right to direct use

Who takes the **'how and what purpose' decisions** throughout the **period of use**?



Contract is or contains a lease*

Contract does not contain a lease

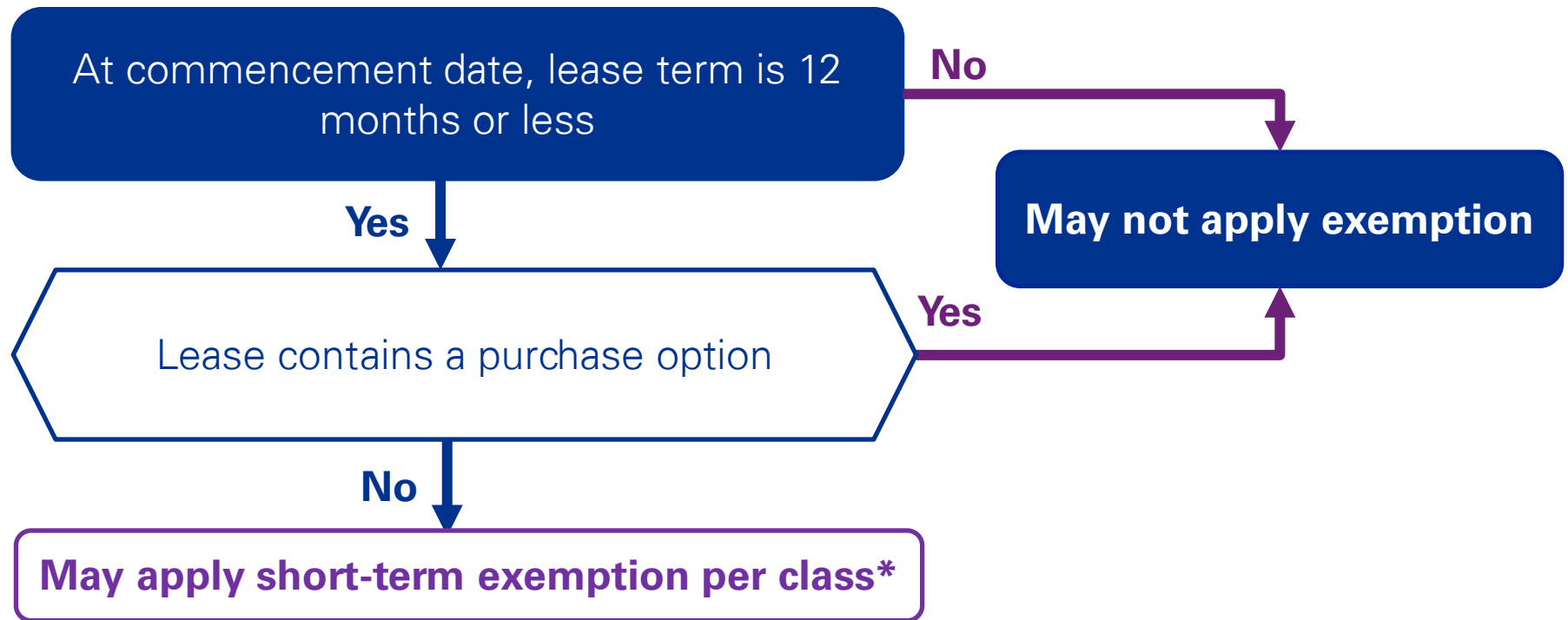
Protective rights of the supplier

* If other criteria are met.



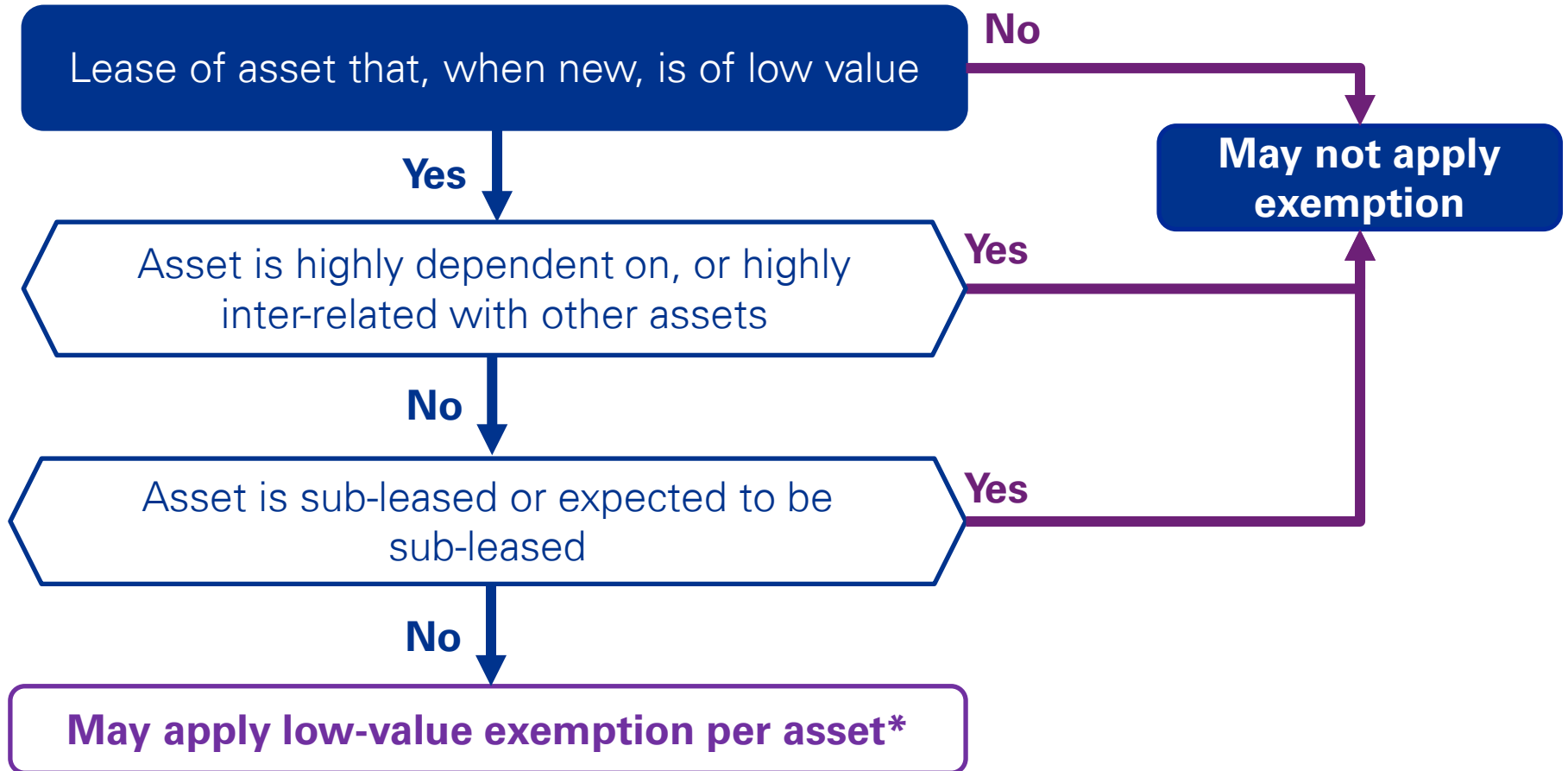
Lessee exemptions

Short-term leases



***Treat as a new lease if there are subsequent changes in lease term**

Low-value items



***Treat as a new lease if asset is subsequently sub-leased**

Example: Low-value items exemption



Lessee B is in the pharmaceutical manufacturing and distribution industry and has the following leases:

Lease	Eligible for low-value exemption?
Real estate: both office building and warehouse	No
Inexpensive office furniture	Yes
Company cars: both for sales personnel and senior management; of varying quality, specification and value	No
Trucks and vans used for delivery	No
Inexpensive IT equipment – e.g. laptops	Yes



Lessee Accounting

Overview

Single lease accounting model

Balance sheet

Asset

= 'Right-of-use' (ROU) of
underlying asset

Liability

= Obligation to make lease
payments

P&L

Lease expense

Depreciation

+ Interest

= Total lease expense



Audit Considerations

Other Audit Considerations

Auditing
judgement areas

Increased
audit scope –
New
lease/Change
in lease term

Correct
application
of practical
expedients

Lease register
Completeness


Re-
measurement
of leases

Lease
modification

Other Audit Considerations

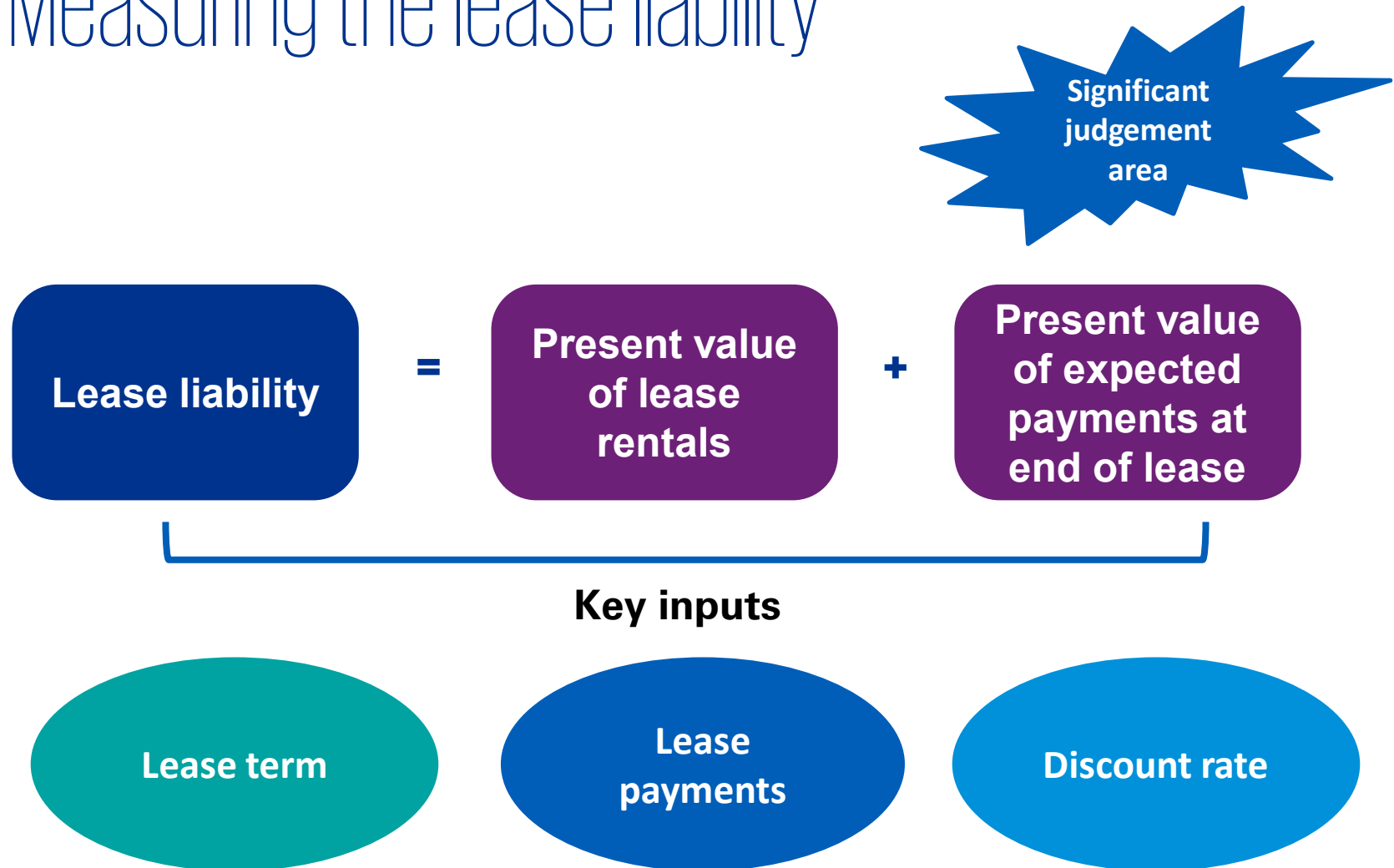


Tax effect



Sale and lease
back – Is there a
sale per IFRS 15
(performance
obligation sati

Measuring the lease liability



Lease term

Lease term

=

Non-cancellable period

+

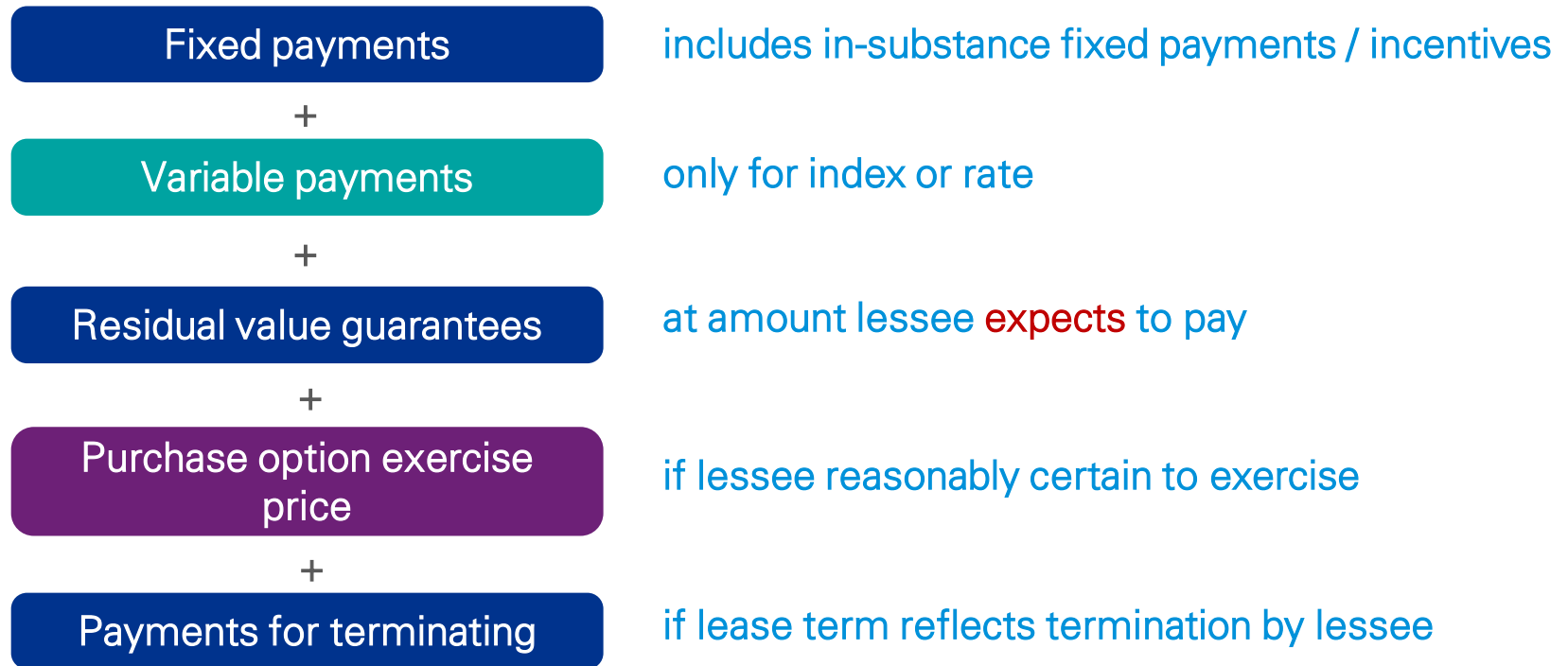
Optional renewal periods if lessee *reasonably certain* to exercise

+

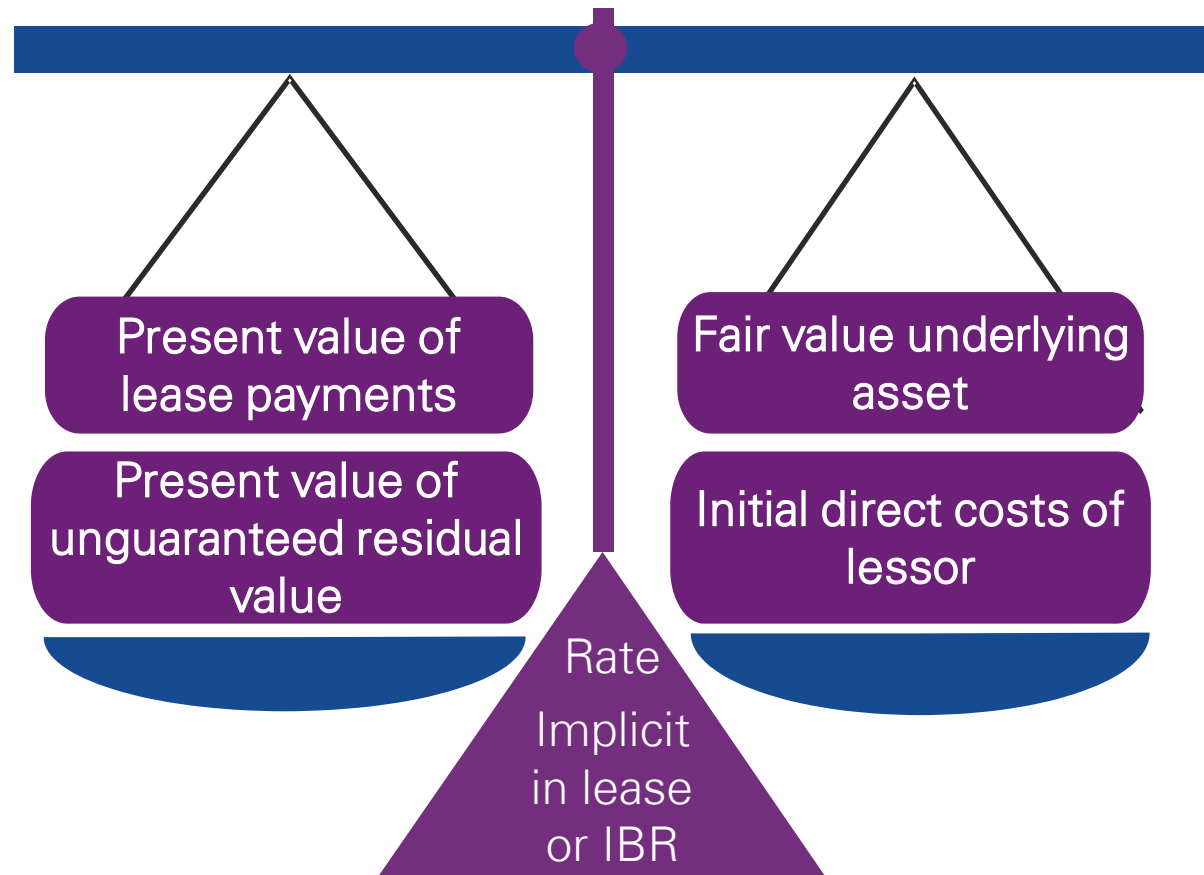
Periods after optional termination date if lessee *reasonably certain not* to terminate

Significant judgement area

Lease payments



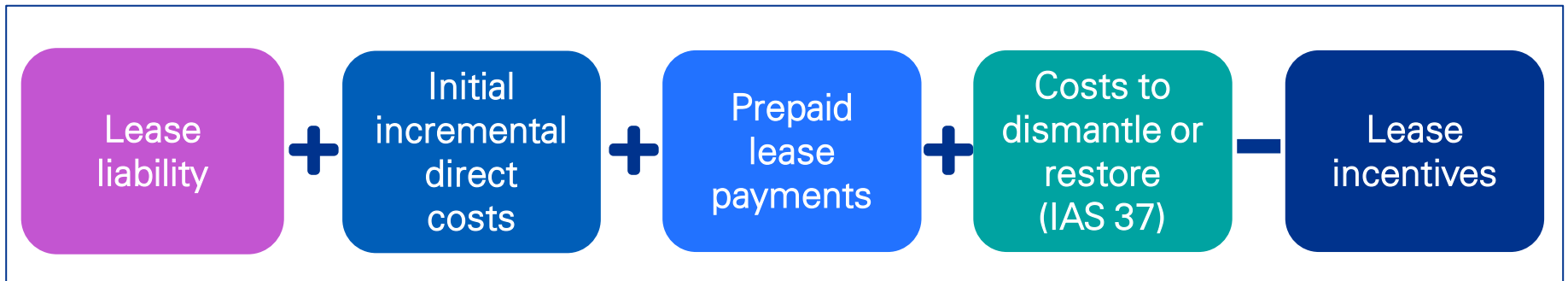
Discount rate - Rate implicit in the lease or incremental borrowing rate (IBR)



Measuring the right-of-use (ROU) asset

ROU asset

=





Lessee Accounting

Subsequent
Measurement

Subsequent measurement

Lease liability

- Amortised cost using the effective interest method
- Cannot be measured at FVTPL/FVOCI.

ROU asset (cost model)

- Depreciated in accordance with IAS 16 *Property, Plant & Equipment*.
- Depreciation period is the shorter of lease term/useful life.
- Impairment testing under IAS 36 *Impairment*.

ROU asset (alternative models)

- Revaluation model under IAS 16.
- Fair value model under IAS 40 *Investment Property*.

Re-measurement of lease liability

Re-measure to reflect reassessment of any changes in:

- | | |
|--|---|
| <ul style="list-style-type: none">▪ Expected amount payable on the residual value guarantee▪ Index or rates▪ In-substance fixed payments | A |
| <ul style="list-style-type: none">▪ Lease term▪ Floating interest rates▪ Assessment of purchase options | B |

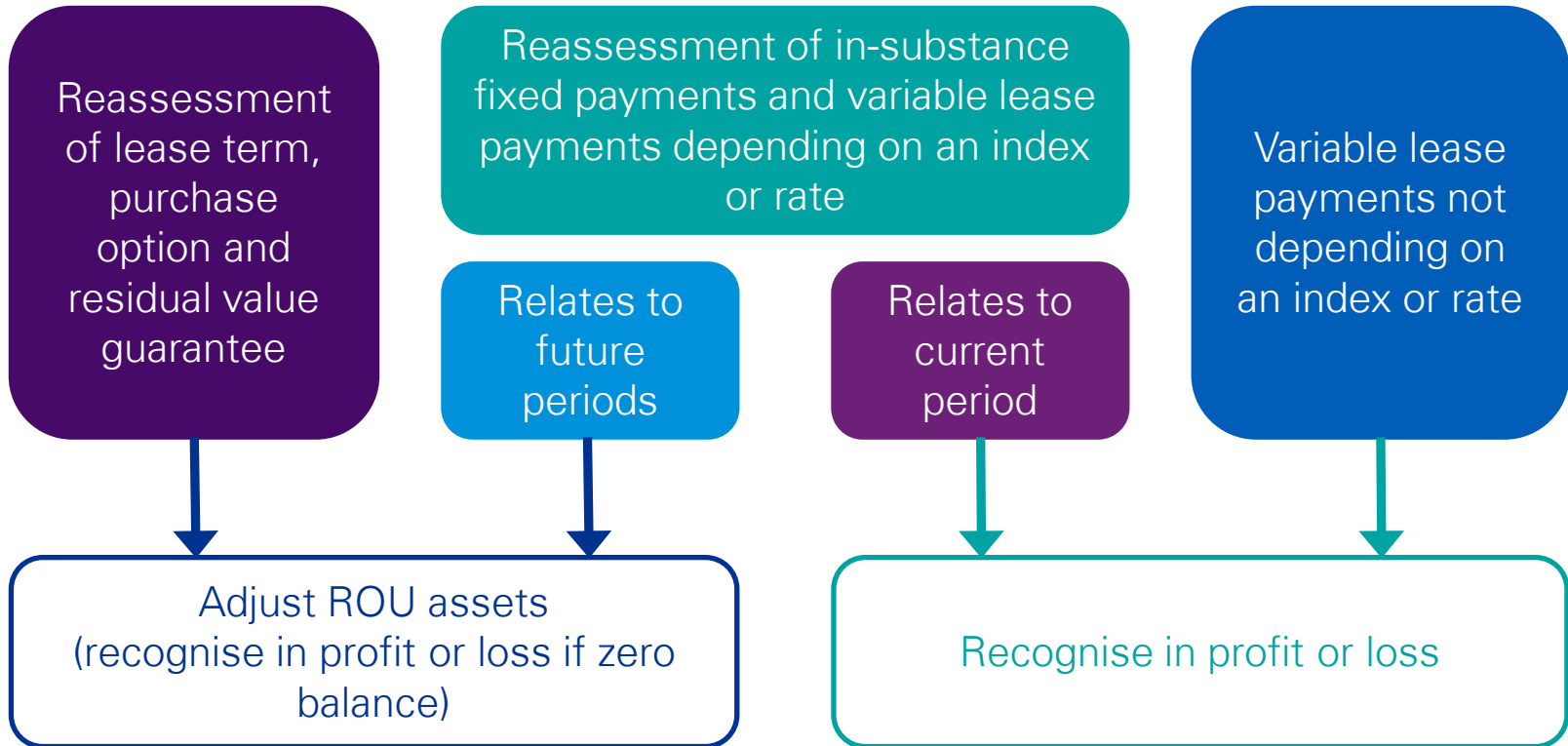
Which discount rate ?

A. Unchanged discount rate

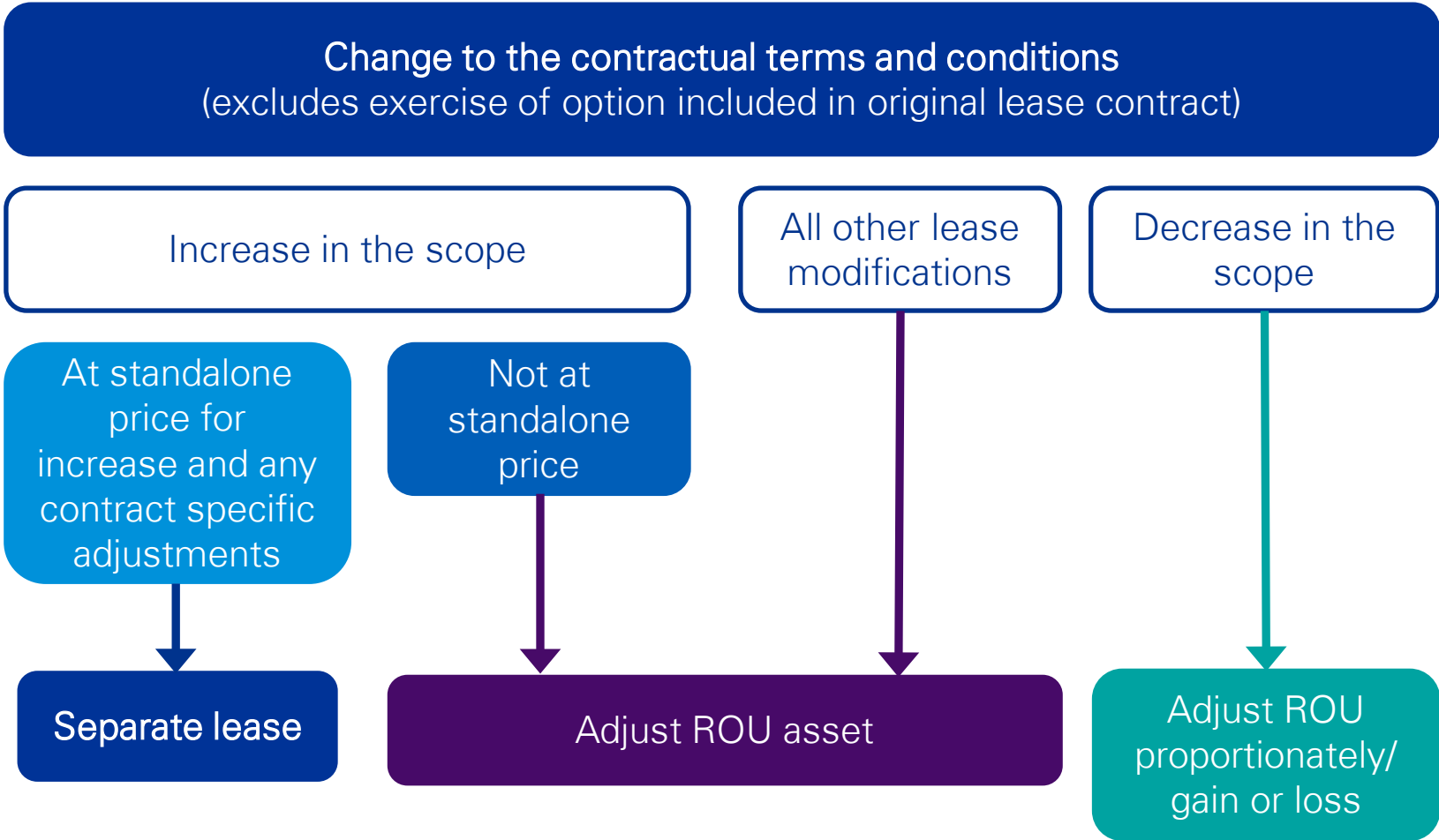
B. Revised discount rate

Re-measurement of ROU asset

Changes in carrying amount of lease liability due to:



Lease modifications- Lessee



Lessor accounting

Unchanged from IAS 17

- Lease classification test.
- Finance lease model.
- Operating lease model.

Different to IAS 17

- Definition of a lease.
- Sale-and-leaseback guidance.
- Sub-lease guidance.
- Accounting for lease modifications.
- Disclosure requirements.

No symmetry
between
lessee and
lessor
accounting



Disclosure

Key reminder - use of disclosure
checklist



Question Break

