

Implementing IFRS 16

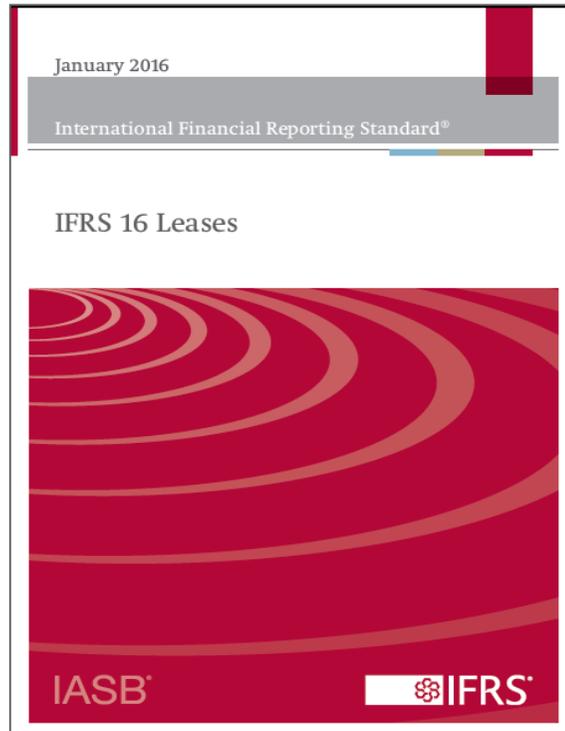
Jianqiao Lu, IASB Member
International Accounting Standards Board,
Singapore, November 2018

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New Leases Standard

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- **IFRS 16** *Leases* published in January 2016
 - **replaces IAS 17** and related interpretations
 - **changes lessee accounting** substantially
 - little change for **lessors**
- Effective date **1 January 2019**
 - early application permitted

What's changed for lessors & lessees?

Changes to lessor accounting

- **Substantially carry forward** IAS 17 accounting requirements; some additional disclosure requirements

Changes to Lessee accounting

- **Former operating leases capitalised.** All¹ leases accounted for similarly to today's finance leases

Balance Sheet

- ↑ Leased assets
- ↑ Financial Liabilities
- ↓ Equity

Income statement

- ↓ Operating expense
- ↑ Finance cost

Cash flow statement

- ↓ Operating flows
- ↑ Financing flows

¹ Exemptions for short-term leases and leases of low-value assets

Different effects by company / industry

Industry sector	Long-term financial liabilities to equity ratio			EBITDA (in billions of US\$)		
	Reported on balance sheet (IAS 17)	If all leases on balance sheet (IFRS 16)	Increase (percentage points)	Reported on balance sheet (IAS 17)	If all leases on balance sheet (IFRS 16)	Increase
Airlines	123%	251%	1.28	51.6	73.8	43%
Travel and leisure	118%	191%	0.73	50.3	63.3	26%
Retailers	48%	103%	0.55	270.4	347.7	29%
Transport	54%	84%	0.30	71.2	87.6	23%
Telecommunications	79%	96%	0.17	399.3	434.5	9%
Distributors	91%	104%	0.13	29.4	35.0	19%
...	
Total sample⁽¹⁾	59%	74%	0.15	3,394	3,722	10%

(1) 1,022 IFRS/US GAAP listed companies (excluding banks and insurance companies) each with estimated operating lease liabilities of >\$300M (discounted basis). Data obtained from financial data aggregators that may contain errors; this information should, therefore, be used with a degree of caution.

Implementation support for IFRS 16

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Introductory webinar & series of 7 webinars on specific topics

Narrow-scope standard setting

- proposed annual improvement
- Ongoing work on interaction with deferred tax



Articles and other materials



Education for

- investors
- regulators
- standard-setters

Informal technical discussions with

- regulators
- standard-setters
- audit firms



Dedicated Conferences



Email box for questions

Webinars to support the implementation of IFRS 16

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We developed a series of webinars to explain in a user-friendly way the main aspects of the requirements in IFRS 16. Implementation questions that we were informed of formed the basis of much of the content of these webinars.

January 2016	Introducing IFRS 16
March 2016	Transition to IFRS 16
April 2016	Definition of a lease
April 2016	Exemptions
June 2016	Lessee measurement
March 2017	Lease modifications
July 2017	Lessee disclosure
October 2017	Lease term Q&A

Areas of interest: Measurement

Measurement of Lease Liability

Overview

Determine Lease term

- Extension options
 - Termination options
- } 'Reasonably certain' assessment

Identify lease payments

- Fixed payments
 - including in-substance fixed payments
- Variable lease payments
 - based on an index or a rate
- Residual value guarantees
- Lease incentives
- Exercise price of purchase options
- Termination penalties

Apply Discount rates

- Rate implicit in lease, if readily determinable
- Otherwise, incremental borrowing rate

IFRS 16; paragraph B34:

....A lease is no longer enforceable when the lessee and the lessor each has the **right to terminate** the lease without permission from the other party with **no more than an insignificant penalty**

Determine lease term

Reasonably certain assessment

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Is there an *economic incentive* to lease for the longer lease term?

For example:

- ***Favourable terms*** compared to market rates
- Significant ***leasehold improvements***
- Termination or relocation ***costs***
- ***Specialised asset*** or lack of available alternative assets

Other considerations:

Interaction with other contract terms

Past practice

Length of non-cancellable period

Identify lease payments

Variable lease payments

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Include Variable Lease Payments that depend on an index or a rate

For example:

- Consumer Price Index (*CPI*)
- Benchmark interest rate (eg *LIBOR*)
- Payments that vary with *market rentals*

Initially measure based on index or rate at commencement date

do not forecast future changes in the index or rate

Remeasure only when cash flows change

generally, do not change discount rate

Identify lease payments

In-substance fixed payments

Variable lease payments—how a lessor might cover their risk:

Example:
Minimum rent
clause

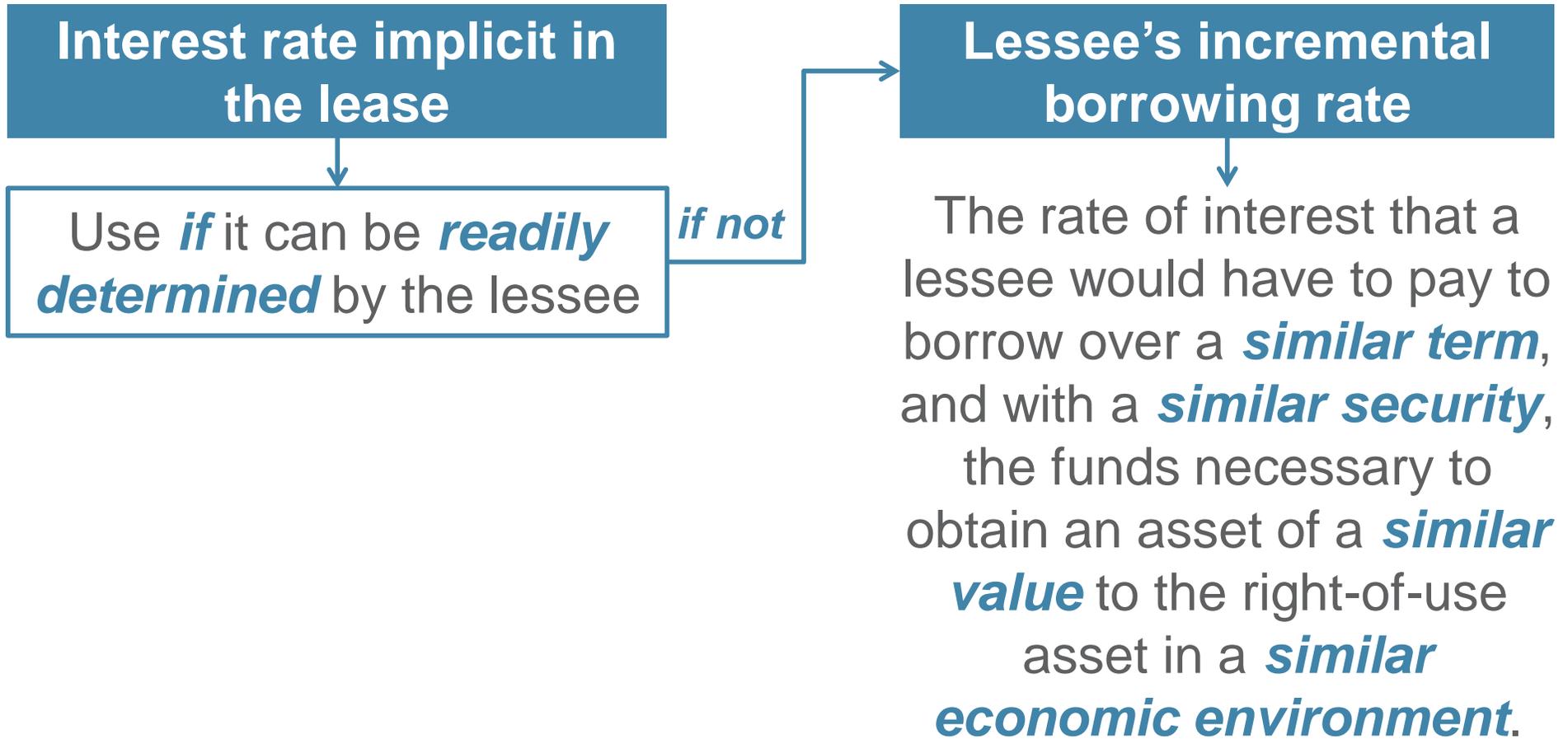
E.g. if sales
are less than
CU100, rent
is CU5

In-substance fixed lease
payments of CU5p.a.
included in lease liability

Example: Higher
variable
payments to
compensate risk
of zero return

E.g. variable
payments
based on 7%
of sales

Genuine variability: variable
payments not included in
lease liability, recognise in
P&L when incurred



Areas of interest: Disclosure

- Two main elements to IFRS 16 disclosures:

**Mandatory
quantitative
information**



Information that users want to see for **all** material lease portfolios

**Additional
entity specific
information**



Companies **apply judgement** to determine whether and what further information is needed to meet the disclosure objectives

- To be disclosed whenever material:

Information about lease costs, cash flows and assets

- Breakdown of lease costs
- Total lease cash flows
- ROU assets by major class of leased asset
- Additions to ROU assets

Maturity analysis

- Maturity analysis of lease commitments
 - as for all other financial liabilities
 - apply judgement in determining time bands

Information about lease costs

Year Ended 31 December 2019	2019 <i>CU'm</i>
<i>Income Statement Disclosures:</i>	
Depreciation of ROU assets	X
Interest on lease liabilities	X
	X
Depreciation of ROU assets comprises:	
Property	X
Other classes of underlying asset	X
	X
Short term lease expense	X
Low-value asset lease expense	X
Variable lease expense	X

Used by equity analysts to determine **whole asset information**

Information about **lease payments not included in the lease liability**

Information about lease cash flows and assets

Year Ended 31 December 2019 (continued)	2019 <i>CU'm</i>
<i>Cash Flow Statement Disclosures:</i>	
Total cash flow for leases	X
<i>Balance Sheet Disclosures:</i>	
Carrying amount of Property ROU assets	X
Carrying amount of other classes of ROU assets	X
Total ROU assets	X
Additions to ROU assets	X
Lease liabilities	X

Doesn't appear in the
cash flow statement

Information similar to
capex

Maturity analysis

Company X

	Maturity							
	Total	less than 1 month	1-3 months	3-6 months	6 months -1 year	1-3 years	3-5 years	more than 5 years
Bank borrowings	1,625				285	740	600	
Lease liabilities	2,300	70	140	210	400	750	620	110
Trade and other payables	350	70	190	90				

Company Y

	Maturity						
	Total	less than 1 month	1-6 months	6 months -1 year	1-2 years	2-3 years	more than 3 years
Bonds	2,100	7	34	40	79	1,940	
Lease liabilities*	4,970			340	310	290	4,030
Trade and other payables	980	280	700				

*Further information about the maturity of lease liabilities is provided in the table below:

	Maturity						
	Total	less than 1 year	1-5 years	5-10 years	10-15 years	15-20 years	20-25 years
Lease liabilities	4,970	340	1,200	1,110	1,050	970	300



Companies can use **most relevant time bands** for their lease portfolio



Additional Entity-Specific Information

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- Lessee to apply judgement about what is relevant:

Extension and termination options	Variable lease payments	Residual value guarantees	Sale & leaseback transactions
<p>For example....</p> <ul style="list-style-type: none">• Why have them?• Prevalence within lease portfolio• Relative magnitude of optional payments vs committed payments• Exercise of options not recognised on balance sheet	<p>For example....</p> <ul style="list-style-type: none">• Why have them?• Prevalence within lease portfolio• Relative magnitude of variable payments vs fixed payments	<p>For example....</p> <ul style="list-style-type: none">• Why have them?• Nature of relevant assets• Prevalence within lease portfolio• Magnitude of exposure to residual value risk	<p>For example....</p> <ul style="list-style-type: none">• Why use them?• Prevalence• Key terms and conditions• Payments not recognised on balance sheet• Cash flow effect

- Considerations

What information
is **monitored**
and **reported**
internally?

What information
is used in
decision
making?

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