IND AS – 17
Leases
IND AS 17 vs AS – 19

Following concepts of IND AS 17 which are similar to AS – 19.

• Classification of Lease between Finance and Operating Lease
• Recognition, measurement and Disclosure of Finance Lease and Operating Lease.
• Sale and Lease back transactions
• Definitions
## IND AS 17 vs AS – 19

Following are the GAAP differences between AS – 19 and IND AS 17.

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Topic</th>
<th>AS – 19</th>
<th>IND AS – 17</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Matters contained</td>
<td>Leases – Operating, Finance, Sale &amp; Lease back Transactions</td>
<td>1. Apart from AS-19 contents</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2. Appendix A – Operating Lease Incentive</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3. Appendix B – Evaluating the substance of transaction involving legal form of lease</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>4. Appendix C – Determining whether an arrangement contains a lease</td>
</tr>
<tr>
<td>2</td>
<td>Leasehold Land</td>
<td>Classified as Fixed Assets</td>
<td>Recognized as either operating lease or finance lease</td>
</tr>
<tr>
<td>3</td>
<td>Initial Direct Cost - Finance lease-Lessor:</td>
<td>Initial Cost are either recognized immediately in the Statement of P &amp; L or allocated against the finance income over the lease term</td>
<td>Initial cost are included in the measurement of finance lease receivable and reduce the amount of income recognised over the lease term</td>
</tr>
</tbody>
</table>
IND AS 17 – New Concepts

Following are the New Concepts in IND AS -17:

A. Determining whether an arrangement contains a lease (Appendix C)
B. Operating Lease – Incentive (Appendix A)
C. Includes lease of Land and Building
D. Evaluation of Substance of Transactions involving legal form of lease (Appendix B)
E. First time adoption of IND AS 17
Test of an Arrangement

Test 1
Assessment of Appendix C of IND AS 115, “Service Concession Arrangements”

Yes
Accounting as per IND AS 115 / IND AS 11

No
Test 2
Assessment of Appendix C of IND AS 17, “Determining whether an arrangement contains a Lease”

Yes
Lease Accounting as per IND AS 17

Yes
Operating Lease

No
Property, Plant and Equipment Accounting

Finance Lease
A. Determining whether an arrangement contains a lease.

Determining whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether:

1. **Specific asset test**: fulfillment of the arrangement is dependent on the use of a specific asset or assets (the asset); and

2. **Right to use**: the arrangement conveys a right to use the asset

In case an arrangement is classified as lease, then the requirements of IND AS 17 are applied for accounting and measurement.
Determining whether an arrangement contains a lease....Contd/-

Specific Asset test:

Classification of these type of arrangements as lease will depend upon the evaluation whether the arrangement can be fulfilled by using only specific asset and it provides right to use the asset. Specific asset test is critical. In case the arrangement can be satisfied by using any asset, then it is not classified as lease.
Determining whether an arrangement contains a lease....Contd/-

Right to use the asset:

Meeting any one of the criteria would constitute Right to use the asset:

• The purchaser has the ability or right to operate the asset or direct others to operate the asset

• have ability or right to control physical access to asset

• There is a remote possibility that parties other than purchaser will take more than an insignificant amount of the output of the asset at a price which is neither fixed nor equal to the current market price at the time of delivery.
Conclusion:

After concluding, that the arrangement contains a lease, then a test needs to be done whether the arrangement is a finance lease or operating lease.

After evaluating as per the requirements of IND AS 17, whether an arrangement constitutes a Finance Lease or Operating Lease, appropriate disclosures and presentation to be made in the financial statements.
B. Operating Lease – Incentive

- In negotiating a new or renewed operating lease, the lessor may provide incentives for the lessee to enter into the agreement.
  E.g. Up-front cash payment to the lessee
  Rent Free or reduced rent during the initial period etc.

- All incentives for the agreement of a new or renewed operating lease shall be recognized as an integral part of the net consideration agreed for the use of the leased asset, irrespective of the incentive’s nature or form or the timing of payments.

- The lessor shall recognize the aggregate cost of incentives as a reduction of rental income over the lease term, on a straight-line basis, similarly, the lessee shall recognize incentives as a reduction of rental expense over the lease term, on a straight-line basis.
C. Lease of Land and Building

• In case the Lease includes both Land and Building, then the entity shall assess each element either as a finance lease or an operating lease separately.

• In determining whether the land is an operating lease or a finance lease an important consideration is that land normally has an indefinite economic life. Therefore, normally lease of land shall be treated as an operating lease. In certain cases land may have restricted economic life because of planned alternative use, hence in such case the lease of land could be classified as finance lease depending upon the lease term and other features.
C. Lease of Land

• Classification of Land as Finance or Operating Lease:

In order to classify the Land as finance lease, following condition needs to be fulfilled:

“At the inception of the Lease, the present value of Minimum Lease Payment amounts to at least substantially (i.e. at least 90%) all of the fair value of the leasehold land”.

In case the above condition is fulfilled, the lessee should present the leasehold land under “Property Plant and Equipment”.

Further, if there is reasonable certainty that the lessee will obtain ownership at the end of the lease term then the land shall not be depreciated else shall be depreciated over the lease term or useful life whichever is lower.
C. Lease of Land and Building

For the purpose of classification of Land and Building separately, following methods are followed:

• The **Minimum Lease Payments** (including lumpsum upfront payments) are **allocated** between the land and buildings in **proportion to the relative fair values** of the leasehold interest in the land and building at the inception of lease.

• If the lease payments **cannot be allocated reliably**, the entire lease is classified as a finance lease unless it is clear that both elements are operating lease, in which the entire lease is classified as an operating lease.

• If the land value is immaterial, the land and building may be treated as a single unit for the purpose of lease classification. In such case the economic life of the building is regarded as the economic life of the entire leased asset.
D. Evaluating the Substance of Transactions Involving the Legal Form of a Lease

• Often a series of transactions are entered into bundling which may be necessary for giving effect to the “substance over form” and in effect the series of transaction may lead to aborting lease accounting although the legal form of the transactions is Lease.

• A series of transactions that involve the legal form of a lease is linked and shall be accounted for as one transaction when the overall economic effect cannot be understood without reference to the series of transactions as a whole. This is the case, for example, when the series of transactions are closely interrelated, negotiated as a single transaction, and takes place concurrently or in a continuous sequence.
D. Evaluating the Substance of Transactions Involving the Legal Form of a Lease....Contd

Indicators that individually demonstrate that an arrangement may not, in substance, involve a lease under Ind AS 17 include:

1. an Entity **retains all the risks and rewards** incident to ownership of an underlying asset and enjoys substantially the same rights to its use as before the arrangement;

2. the primary reason for the arrangement is to **achieve a particular tax result**, and not to convey the right to use an asset; and

3. an **option** is included on terms that make its exercise almost certain (e.g. a put option that is exercisable at a price sufficiently higher than the expected fair value when it becomes exercisable).
D. Evaluating the Substance of Transactions Involving the Legal Form of a Lease....Contd

• Example

Entity A leases a asset to an Investor under **Head Lease** and the Investor leases the same asset back to Entity A under a **Sub-Lease**. At the end of the Sub-Lease Entity A has the right to buy back the rights of the Investor under a purchase option.
D. Evaluating the Substance of Transactions Involving the Legal Form of a Lease....Contd

Disclosure

An **Entity shall disclose** the following in each period that an arrangement exists:

- a description of the arrangement including;
  - the underlying asset and any restrictions on its use;
  - the life and other significant terms of the arrangement;
  - the transactions that are linked together, including any options; and

- the accounting treatment applied **to any fee received**, the amount recognised as income in the period, and the line item of the statement of profit and loss in which it is included.

- The disclosures shall be provided individually for each arrangement or in aggregate for each class of arrangement.
E. First Time Adoption of IND AS 17

First Time adoption of IND AS 17

• IND AS 101, provides an option to make an assessment of the requirements of Appendix C of IND AS 17 as at the transition date rather than at the inception of the arrangement.

• Similarly, in case an entity has already made the same determination as required by Appendix C of Ind AS-17 but at a date other than that required under IND AS 17, the entity need not reassess that determination when it adopts IND AS 17.

• When a lease includes both land and building elements, an Entity may assess the classification of each element as finance or operating lease as at the date of transition to IND AS on the basis of the facts and circumstances existing as at that date.

If there is any land lease newly classified as finance lease then the Entity may recognise assets and liability at fair value on that date; and any difference between those fair values to be recognised in retained earnings.
THANK YOU