

# Leases

## 1.1. Classification of leases

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.

**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.
- (e) the leased assets are of such a specialized nature that only the lessee can use them without major modifications.
- (f) the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee.
- (g) gains or losses from the fluctuation in the residual value of the leased asset accrue to the lessee (e.g. in the form of a rent rebate equaling most of the sales proceeds at the end of the lease).
- (h) the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

These examples and indicators 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 is transferred to the lessee at the end of the lease for a variable payment equal to the asset's then fair value, or if there are contingent rents, as a result of which the lessee does not have substantially all risks and rewards incidental to ownership.

Lease classification is made at the inception of the lease and is not changed during the term of the lease unless the lessee and the lessor agree to change the provisions of the lease (other than simply by renewing the lease), in which case the lease classification shall be re-evaluated.

## 1.2. Finance leases - financial statements of lessees and lessors

### Lessee

At the commencement of the lease term, a lessee shall recognize its rights of use and obligations under finance leases as assets and liabilities in its statement 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, determined at the inception of the lease. Any initial direct costs of the lessee (incremental costs that are directly attributable to negotiating and arranging a lease) are added to the amount recognized as an asset. The present value of the minimum lease payments should be calculated using the interest rate implicit in the lease. If this cannot be determined, lessee's incremental borrowing rate shall be used.

A lessee shall apportion minimum lease payments between the finance charge and the reduction of the outstanding liability using the effective interest method. The lessee shall allocate the finance charge to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. A lessee shall charge contingent rents as expenses in the periods in which they are incurred.

A lessee shall depreciate an asset leased under a finance lease in accordance with the relevant section of this IFRS for that type of asset, e.g. Sections "Property, Plant and Equipment", "Intangible assets other than Goodwill", "Business combinations and Goodwill". 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. A lessee shall also assess at each reporting date whether an asset leased under a finance lease is impaired.

A lessee shall 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) the total of future minimum lease payments 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; and
  - (iii) later than five years.
- (c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

## Lessors

**A lessor shall recognize 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. The net investment in a lease is the lessor's gross investment in the lease discounted at the interest rate implicit in the lease. The 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.**

**For finance leases other than those involving manufacturer or dealer lessors, initial direct costs (costs that are incremental and directly attributable to negotiating and arranging a lease) are included in the initial measurement of the finance lease receivable and reduce the amount of income recognized over the lease term.**

**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. 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. If there is an indication that the estimated unguaranteed residual value used in computing the lessor's gross investment in the lease has changed significantly, the income allocation over the lease term is revised, and any reduction in respect of amounts accrued is recognized immediately in profit or loss.**

**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.**

**The sales revenue recognized 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 recognized 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 recognized in accordance with the entity's policy 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 recognized as an expense when the selling profit is recognized.**

**A lessor shall make the following disclosures 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, a lessor 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; and

(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 recognized as income in the period.

(f) a general description of the lessor's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

### **1.3. Operating leases - financial statements of lessees and lessors**

#### **Lessee**

**A lessee shall recognize lease payments under operating leases (excluding costs for services such as insurance and maintenance) as an expense on a straight-line basis** unless either:

(a) another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis, or

(b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary because of factors other than general inflation, then this condition (b) is not met.

**A lessee shall 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; and

(iii) later than five years.

(b) lease payments recognized as an expense.

(c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

## **Lessors**

**A lessor shall present assets subject to operating leases in its statement of financial position according to the nature of the asset.**

**A lessor shall recognize lease income from operating leases (excluding amounts for services such as insurance and maintenance) in profit or loss on a straight-line basis over the lease term, unless either**

(a) another systematic basis is representative of the time pattern of the lessee's benefit from the leased asset, even if the receipt of payments is not on that basis, or

(b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary according to factors other than inflation, then condition (b) is not met.

**A lessor shall recognize as an expense costs, including depreciation, incurred in earning the lease income. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets.**

**A lessor shall add to the carrying amount of the leased asset any initial direct costs it incurs in negotiating and arranging an operating lease and shall recognise such costs as an expense over the lease term on the same basis as the lease income.**

To determine whether a leased asset has become impaired, a lessor shall apply Section "Impairment of Assers".

**A manufacturer or dealer lessor does not recognize any selling profit on entering into an operating lease because it is not the equivalent of a sale.**

**A lessor shall disclose the following for operating leases:**

(a) the future minimum lease payments under non-cancellable operating leases for each of the following periods:

(i) not later than one year; and

(ii) later than one year and not later than five years; and

(iii) later than five years.

(b) total contingent rents recognized as income.

(c) a general description of the lessor's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, and restrictions imposed by lease arrangements.

#### **1.4. Sale and leaseback transactions**

**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 on the type of lease:**

**(a) if a sale and leaseback transaction results in a finance lease** - the seller-lessee shall not recognize immediately, as income, any excess of sales proceeds over the carrying amount. Instead, the seller-lessee shall defer such excess and amortize it over the lease term.

**(b) if a sale and leaseback transaction results in an operating lease and it is clear that the transaction is established at fair value** - the seller-lessee shall recognize any profit or loss immediately. If the sale price is below fair value, the seller-lessee shall recognize any profit or loss immediately unless the loss is compensated for by future lease payments at below market price. In that case the seller-lessee shall defer and amortize such loss 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 seller-lessee shall defer the excess over fair value and amortize it over the period for which the asset is expected to be used.

Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of significant leasing arrangements includes description of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.

## Impairment of assets

### 1.1. Impairment of inventories

**An entity shall assess at each reporting date whether any inventories are impaired.** The entity shall make the assessment **by comparing the carrying amount** of each item of inventory (or group of similar items) **with its selling price less costs to complete and sell.** If an item of inventory (or group of similar items) **is impaired,** the entity shall **reduce the carrying amount** of the inventory (or the group) **to its selling price less costs to complete and sell.** That reduction is an **impairment loss** and it is **recognized immediately in profit or loss.**

**If it is impracticable to determine the selling price less costs to complete and sell for inventories item by item, the entity may group items of inventory** relating to the same product line that have similar purposes or end uses and are produced and marketed in the same geographical area for the purpose of assessing impairment.

**An entity shall make a new assessment of selling price less costs to complete and sell at each subsequent reporting date.** When the circumstances that previously caused inventories to be impaired no longer exist or when there is clear evidence of an increase in selling price less costs to complete and sell because of changed economic circumstances, the entity shall reverse the amount of the impairment (i.e. the reversal is limited to the amount of the original impairment loss) so that the new carrying amount is the lower of the cost and the revised selling price less costs to complete and sell.

### 1.2. Impairment of assets other than inventories, impairment loss

**If, and only if, the recoverable amount of an asset is less than its carrying amount, the entity shall reduce the carrying amount of the asset to its recoverable amount. That reduction is an impairment loss. An entity shall recognize an impairment loss immediately in profit or loss.**

**An entity shall assess at each reporting date whether there is any indication that an asset may be impaired.** If any such indication exists, the entity shall estimate the recoverable amount of the asset. If there is no indication of impairment, it is not necessary to estimate the recoverable amount.

**If it is not possible to estimate the recoverable amount of the individual asset, an entity shall estimate the recoverable amount of the cash-generating unit to which the asset belongs.** This may be the case because measuring recoverable amount requires forecasting cash flows, and sometimes individual assets do not generate cash flows by themselves. An asset's cash-generating unit is the smallest identifiable group of assets that includes the asset and generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

**In assessing whether there is any indication that an asset may be impaired, an entity shall consider, as a minimum, the following indications:**

External sources of information -

(a) During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.

(b) Significant changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated.

(c) Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect materially the discount rate used in calculating an asset's value in use and decrease the asset's fair value less costs to sell.

(d) The carrying amount of the net assets of the entity is more than the estimated fair value of the entity as a whole (such an estimate may have been made, for example, in relation to the potential sale of part or all of the entity).

Internal sources of information -

(e) Evidence is available of obsolescence or physical damage of an asset.

(f) Significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite.

(g) Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.

In this context economic performance includes operating results and cash flows.

**If there is an indication that an asset may be impaired, this may indicate that the entity should review the remaining useful life, the depreciation (amortization) method or the residual value for the asset and adjust it in accordance with the section of this IFRS applicable to the asset** (e.g. Sections "Property, Plant and Equipment", "Intangible Assets other than Goodwill"), even if no impairment loss is recognized for the asset.

**The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use.** If it is not possible to estimate the recoverable amount of an individual asset, further presented in this Section indicators (e.g. fair value less costs to sell, value in use) referring to an asset should be read as indicators referring also to an asset's cash-generating unit.



**It is not always necessary to determine both an asset's fair value less costs to sell and its value in use.** If either of these amounts exceeds the asset's carrying amount, the asset is not impaired and it is not necessary to estimate the other amount.

**If there is no reason to believe that an asset's value in use materially exceeds its fair value less costs to sell, the asset's fair value less costs to sell may be used as its recoverable amount.** This will often be the case for an asset that is held for disposal.

**Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. The best evidence of the fair value less costs to sell of an asset is a price in a binding sale agreement in an arm's length transaction or a market price in an active market.** If there is no binding sale agreement or active market for an asset, fair value less costs to sell is based on the **best information available to reflect the amount that an entity could obtain, at the reporting date, from the disposal of the asset in an arm's length transaction between knowledgeable, willing parties, after deducting the costs of disposal.** In determining this amount, an entity considers the outcome of recent transactions for similar assets within the same industry.

**Value in use is the present value of the future cash flows expected to be derived from an asset.** This present value calculation involves first the estimation of the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal, and, then, application of the appropriate discount rate to those future cash flows.

The following elements shall be reflected in the calculation of an asset's value in use:

- (a) an estimate of the future cash flows the entity expects to derive from the asset.
- (b) expectations about possible variations in the amount or timing of those future cash flows.
- (c) the time value of money, represented by the current market risk-free rate of interest.
- (d) the price for bearing the uncertainty inherent in the asset.
- (e) other factors, such as illiquidity, that market participants would reflect in pricing the future cash flows the entity expects to derive from the asset.

In measuring value in use, estimates of future cash flows shall include:

- (a) projections of cash inflows from the continuing use of the asset.
- (b) projections of cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset (including cash outflows to prepare the asset for use) and can be directly attributed, or allocated on a reasonable and consistent basis, to the asset.
- (c) net cash flows, if any, expected to be received (or paid) for the disposal of the asset at the end of its useful life in an arm's length transaction between knowledgeable, willing parties.

**The entity may wish to use any recent financial budgets or forecasts to estimate the cash flows, if available.** To estimate cash flow projections beyond the period covered by the most recent budgets or forecasts an entity may wish to extrapolate the projections based on the budgets or forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified.

**Estimates of future cash flows shall not include cash inflows or outflows from financing activities, or income tax receipts or payments.**

**Future cash flows shall be estimated for the asset in its current condition. Estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from a future restructuring to which an entity is not yet committed, or improving or enhancing the asset's performance.**

**The discount rate (rates) used in the present value calculation shall be a pre-tax rate (rates) that reflect(s) current market assessments of the time value of money, and the risks specific to the asset for which the future cash flow estimates have not been adjusted.** The discount rate (rates) used to measure an asset's value in use shall not reflect risks for which the future cash flow estimates have been adjusted, to avoid double-counting.

**An impairment loss shall be recognized for a cash-generating unit if, and only if, the recoverable amount of the unit is less than the carrying amount of the unit. The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit in the following order:**

- (a) first, to reduce the carrying amount of any goodwill allocated to the cash-generating unit, and
- (b) then, to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the cash-generating unit.

**However, an entity shall not reduce the carrying amount of any asset in the cash-generating unit below the highest of:**

- (a) its fair value less costs to sell (if determinable);
- (b) its value in use (if determinable); and
- (c) zero.

**For all assets other than goodwill, an entity shall assess at each reporting date whether there is any indication that an impairment loss recognized in prior periods may no longer exist or may have decreased.** Indications that an impairment loss may have decreased or may no longer exist are generally the opposite of those set out in earlier stated paragraphs (a)-(g). If any such indication exists, the entity shall determine whether all or part of the prior impairment loss should be reversed.

**When the prior impairment loss was based on the recoverable amount of the individual impaired asset, the following requirements apply:**

(a) The entity shall estimate the recoverable amount of the asset at the current reporting date.

(b) If the estimated recoverable amount of the asset exceeds its carrying amount, the entity shall increase the carrying amount to recoverable amount, subject to the limitation described in (c) below. That increase is a reversal of an impairment loss. The entity shall recognize the reversal immediately in profit or loss.

(c) The reversal of an impairment loss shall not increase the carrying amount of the asset above the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior years.

(d) After a reversal of an impairment loss is recognized, the entity shall adjust the depreciation (amortization) charge for the asset in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

**When the original impairment loss was based on the recoverable amount of the cash-generating unit to which the asset belongs, the following requirements apply:**

(a) The entity shall estimate the recoverable amount of that cash-generating unit at the current reporting date.

(b) If the estimated recoverable amount of the cash-generating unit exceeds its carrying amount, that excess is a reversal of an impairment loss. The entity shall allocate the amount of that reversal to the assets of the unit, except for goodwill, pro rata with the carrying amounts of those assets, subject to the limitation described in (c) below. Those increases in carrying amounts shall be treated as reversals of impairment losses for individual assets and recognized immediately in profit or loss.

(c) In allocating a reversal of an impairment loss for a cash-generating unit, the reversal shall not increase the carrying amount of any asset above the lower of its recoverable amount and the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior periods.

(d) Any excess amount of the reversal of the impairment loss that cannot be allocated to an asset because of the restriction in (c) above shall be allocated pro rata to the other assets of the cash-generating unit, except for goodwill.

(e) After a reversal of an impairment loss is recognized, if applicable, the entity shall adjust the depreciation (amortization) charge for each asset in the cash-generating unit in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

### **1.3. Additional requirements for impairment of goodwill**

**Goodwill, by itself, cannot be sold. Nor does it generate cash flows to an entity that are independent of the cash flows of other assets. Thus, the fair value of goodwill cannot be measured directly. Therefore, the fair value of goodwill must be derived from measurement of the fair value of the cash-generating unit(s) of which the goodwill is a part.** For the purpose of impairment testing, **goodwill acquired in a business combination shall, from the acquisition date, be allocated to each of the acquirer's cash-generating units that is expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquire are assigned to those units.**

**Part of the recoverable amount of a cash-generating unit is attributable to the non-controlling interest in goodwill.** For the purpose of impairment testing a non-wholly-owned cash-generating unit with goodwill, **the carrying amount of that unit is notionally adjusted, before being compared with its recoverable amount, by grossing up the carrying amount of goodwill allocated to the unit to include the goodwill attributable to the non-controlling interest.** This **notionally adjusted carrying amount is then compared with the recoverable amount of the unit** to determine whether the cash-generating unit is impaired.

If goodwill cannot be allocated to individual cash-generating units (or groups of cash-generating units) on a non-arbitrary basis, then for the purposes of testing goodwill the entity shall test the impairment of goodwill by determining the recoverable amount of either (a) or (b):

(a) the acquired entity in its entirety, if the goodwill relates to an acquired entity that has not been integrated. Integrated means the acquired business has been restructured or dissolved into the reporting entity or other subsidiaries.

(b) the entire group of entities, excluding any entities that have not been integrated, if the goodwill relates to an entity that has been integrated.

In applying this paragraph, **an entity will need to separate goodwill into goodwill relating to entities that have been integrated (i.e. business combination) and goodwill relating to entities that have not been integrated.**

**An impairment loss recognized for goodwill shall not be reversed in a subsequent period.**

#### **1.4. Disclosures**

An entity shall disclose the following for each class of assets indicated in that Section:

(a) the amount of impairment losses recognized in profit or loss during the period and the line item(s) in the statement of comprehensive income (and in the income statement, if presented) in which those impairment losses are included.

(b) the amount of reversals of impairment losses recognized in profit or loss during the period and the line item(s) in the statement of comprehensive income (and in the income statement, if presented) in which those impairment losses are reversed.