

# IFRS 16 Leases

A summary of IFRS 16 and its effects

22 February 2017



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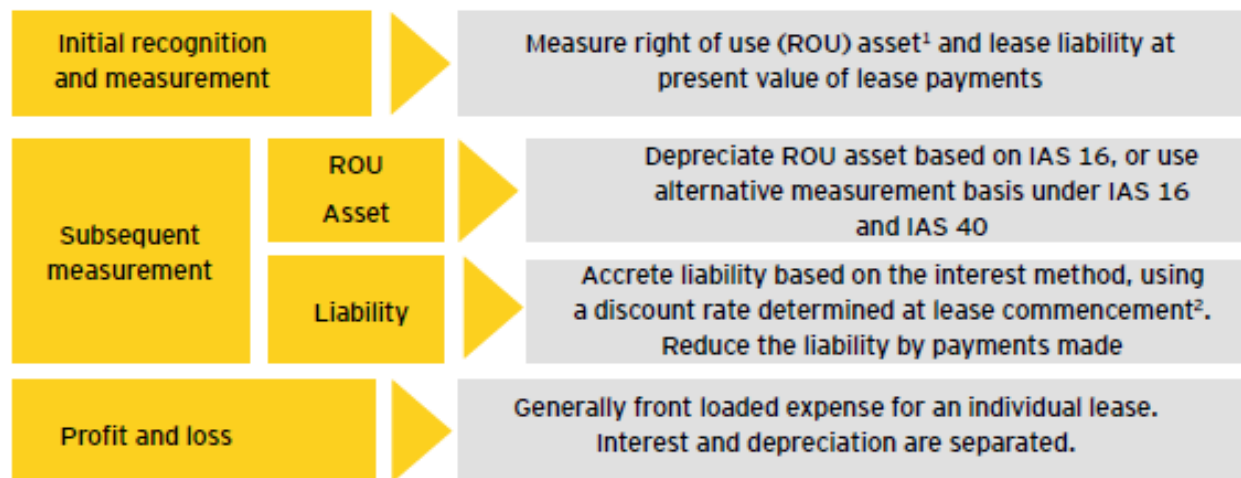
# Overview of IFRS 16 Leases

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- ▶ Leases will have a **single accounting model for all leases** with **two exceptions** ('low-value assets' and short term leases)
- ▶ **Lessor accounting** is substantially **unchanged**
- ▶ **Additional disclosure requirement**
- ▶ The **effective** date is for annual periods beginning on or after **1 January 2019**
- ▶ Early application is permitted, provided the new revenue standard, IFRS 15 *Revenue from Contracts with Customers* has been applied, or is applied at the same date as IFRS 16

# Overview of IFRS 16 Leases

## Lessee accounting - Recognition and measurement



## Lessor accounting - Recognition and measurement

Many aspects of lessor accounting will remain the same.

Effects on the income statement	Effects on the balance sheet	Effects on the cash flow statement
 EBITDA <sup>3</sup>	 Lease assets	 Cash from operating activities
 Operating profit and finance costs	 Financial liabilities	 Cash from financing activities
 Profit before tax	 Equity	 Total cash flow

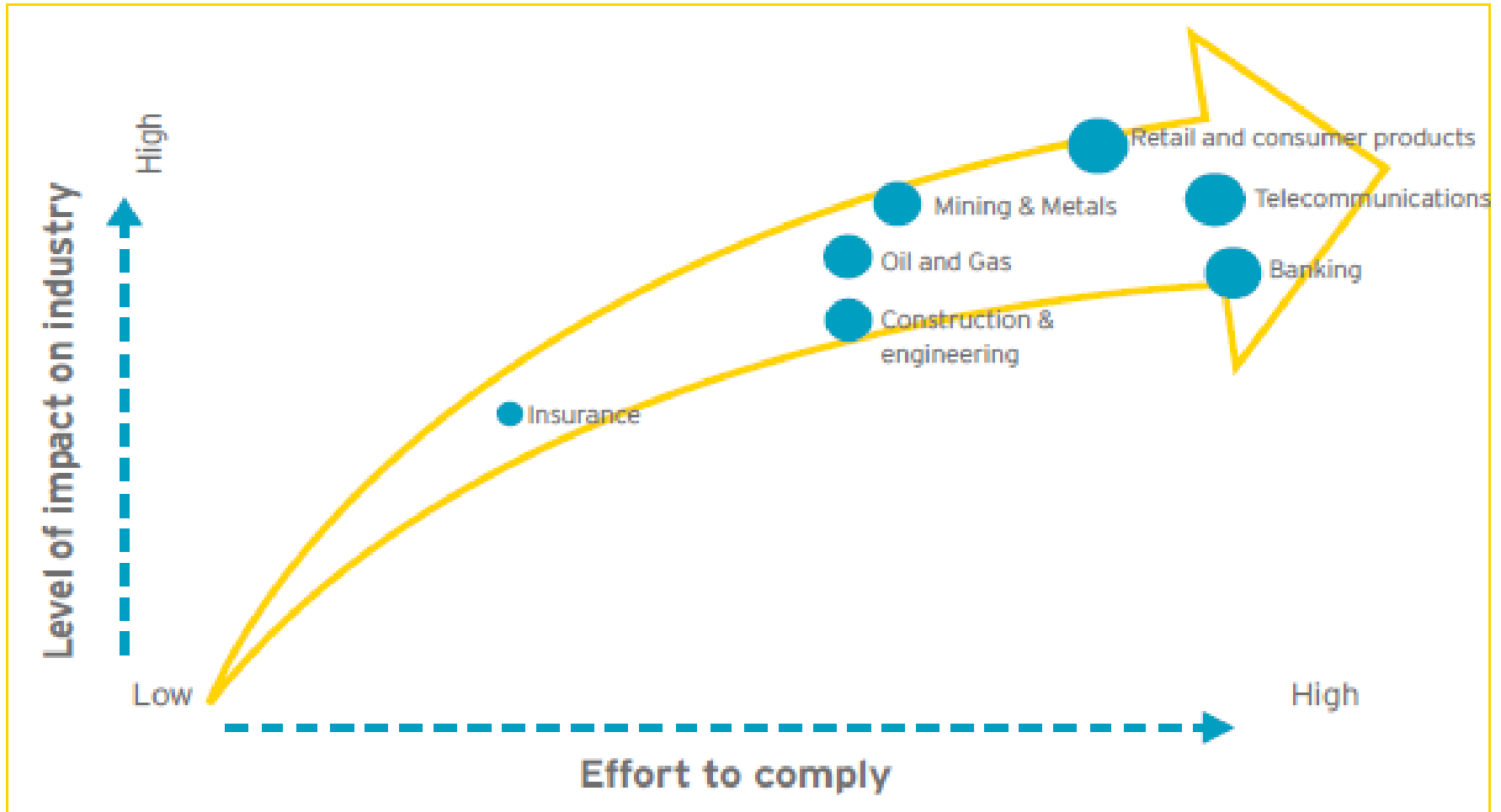
# What is in the scope or affected by the standard?

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## Leases of all assets, except for:

- ▶ Leases of non-regenerative resources
- ▶ Leases of biological assets
- ▶ Service concession arrangements
- ▶ Licences of intellectual property granted by lessor
- ▶ Rights held by a lessee under certain licensing agreements (e.g. films)

# Impact of the adoption of IFRS 16



# Entities most likely to be affected by the changes

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## ▶ Retail and consumer product entities

- ▶ Leased retail space
- ▶ Rental of manufacturing plant and equipment, distribution centres and fleet arrangements



## ▶ Telecommunication entities

- ▶ Careful consideration in Identifying arrangements that contain a lease (previously IFRIC 4)
- ▶ Tower arrangements, signal transmission devices as well as data and fixed line agreements (for example indefeasible right of use (IRU) on fibre lines)
- ▶ Retail outlets

# Entities most likely to be affected by the changes

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## ▶ Banking and other financial services

- ▶ Extensive branch networks as well as large administration and call centres
- ▶ Contracts over ATMs and the related space occupied by such machines
- ▶ Use of data storage facilities
- ▶ Monitoring how right-of-use assets will be treated for regulatory capital requirements



## ▶ Metals and mining entities

- ▶ Arrangements that contain a lease (previously IFRIC 4)
- ▶ Lease of mining equipment, vehicles, land and buildings

# Entities most likely to be affected by the changes

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## ▶ Oil and gas entities

- ▶ Arrangements that contain a lease (previously IFRIC 4)
- ▶ Arrangements in respect of land and buildings, vehicles and equipment









## ▶ Insurance entities

- ▶ All major arrangements in respect of land and buildings, vehicles and equipment that are not currently accounted for on the balance sheet



# Financial statement impact - Before and after IFRS 16

## ► Balance sheet impact

	IAS 17		IFRS 16
	Finance leases	Operating leases	All leases
Assets	 	_____	 
Liabilities	SSSS	_____	SSSS
Off balance sheet rights / obligations	_____	  SSSS	_____

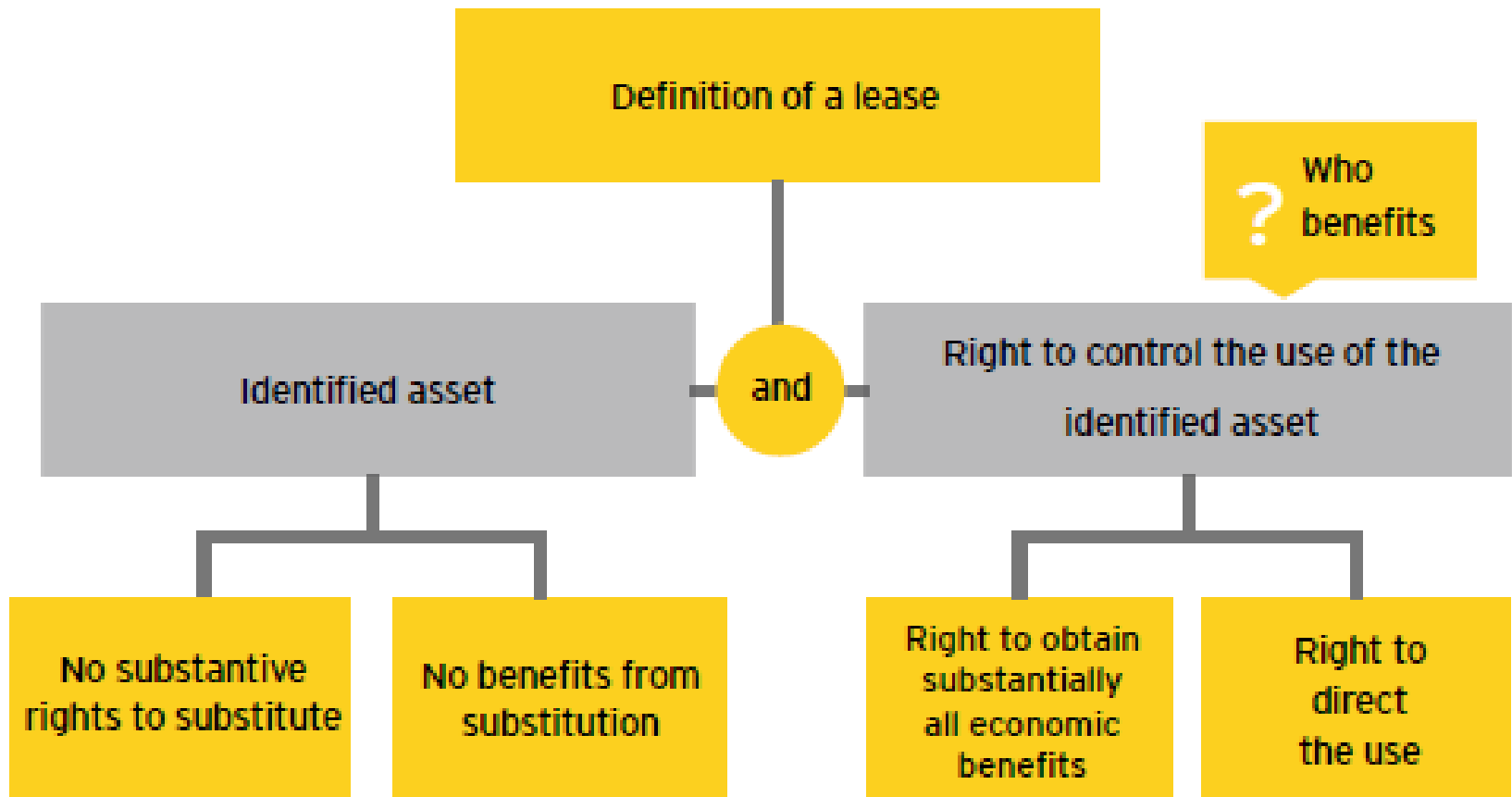
# Financial statement impact - Before and after IFRS 16

## ► Income statement impact

	IAS 17		IFRS16
	Finance leases	Operating leases	All leases
Revenue	\$\$\$\$	\$\$\$\$	\$\$\$\$
Operating costs (excluding depreciation and amortisation)	_____	Single lease expense	_____
EBITDA		_____	▲▲
Depreciation and amortisation	Depreciation	_____	Depreciation
Operating profit			▲
Finance costs	Interest		Interest
Profit before tax			↔

# Key principles of IFRS 16

- ▶ Determining whether an arrangement contains a lease



# Key principles of IFRS 16

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## Identifying and separating lease and non-lease components of a contract and allocating contract consideration

- ▶ Contracts may contain non-lease components such as maintenance
- ▶ These are accounted for separately
- ▶ Lessees can make an accounting policy election to account for both components as a single lease component

Or;

- ▶ The consideration in the contract can be allocated to the lease and non-lease components on a relative standalone price basis
- ▶ Lessors are required to apply IFRS 15 to allocate the consideration in the contract

# Key principles of IFRS 16

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## Lessee accounting

### Initial recognition and measurement

- ▶ Lease liability – measured at the present value of lease payments to be made over the lease term
- ▶ Right-of-use-asset – measured at the amount of the lease liability, adjusted for lease prepayments, lease incentives received, the lessee's initial direct costs (e.g. commissions) and an estimate of restoration, removal and dismantling costs
- ▶ Permitted elections:
  - ▶ The lease term is 12 months or less
  - ▶ The underlying asset is of low value

# Key principles of IFRS 16

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## Lessee accounting

### Subsequent measurement

- ▶ Lease liability – accretion of the lease liability
- ▶ Right-of-use-asset
  - ▶ Depreciated in accordance with IAS 16 Property, Plant and Equipment
  - ▶ Alternative measurement under certain circumstances in accordance with IAS 16 and 40 Investment Property
  - ▶ Subject to impairment testing under IAS 36 Impairment of Assets

# Key principles of IFRS 16

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## Lessee accounting

### Presentation

- ▶ SFP - Lease liability and the right-of use asset can be disclosed separately on the face or in the notes
- ▶ SCI - Interest and depreciation expense cannot be combined
- ▶ SCF
  - ▶ Principal payments are presented within financing activities
  - ▶ Interest payments are presented based on accounting policy election

# Key principles of IFRS 16

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## Lessor accounting

The accounting for lessors is substantially unchanged.

### Initial recognition and measurement

- ▶ The accounting for lessors is substantially unchanged.
- ▶ Operating leases – continue to recognise the underlying asset
- ▶ Finance leases
  - ▶ Derecognise the underlying asset and recognise net investment in the lease
  - ▶ Any selling profit or loss is recognised at lease commencement



# Key principles of IFRS 16

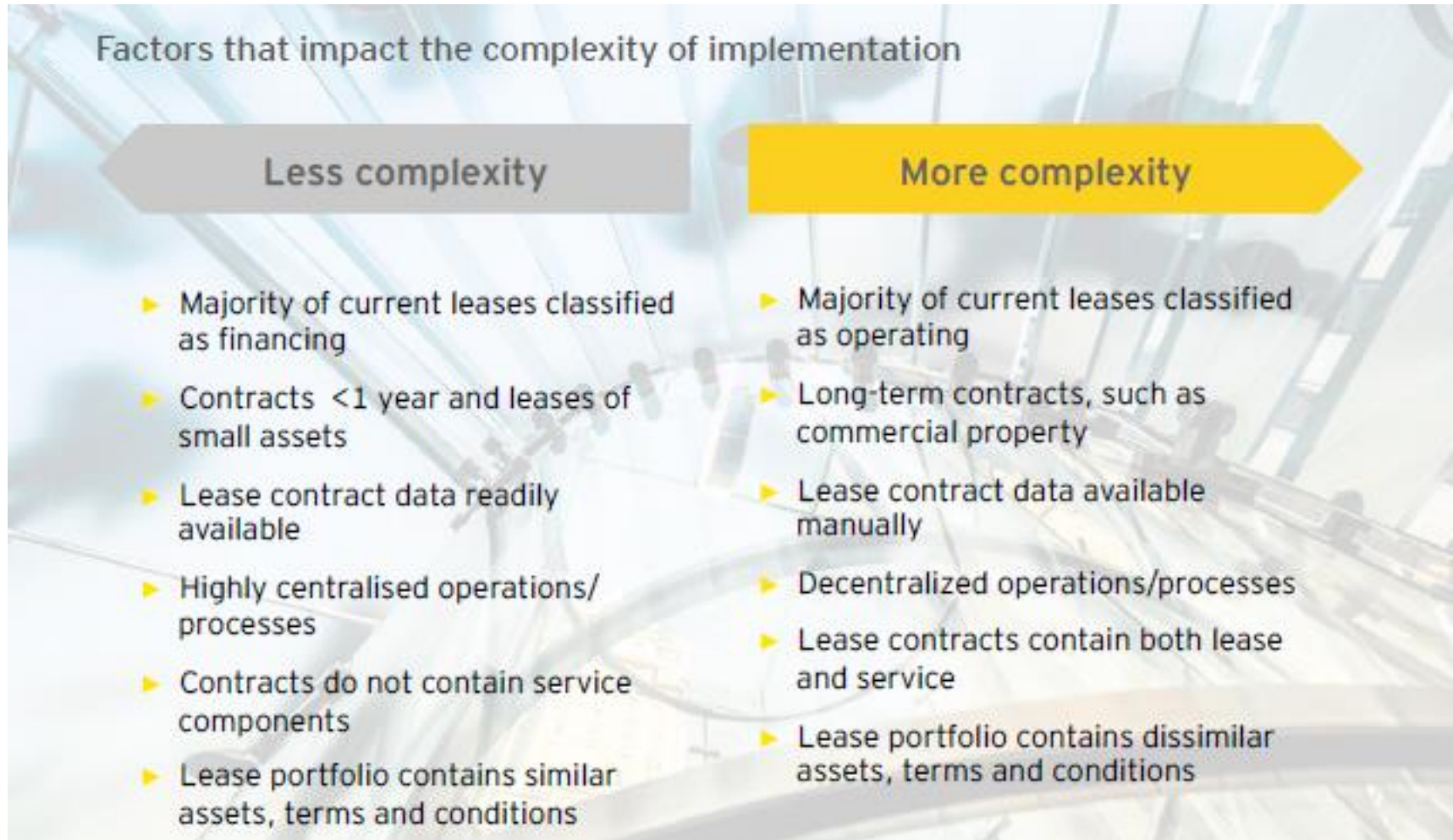
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## Lessor accounting

### Subsequent measurement

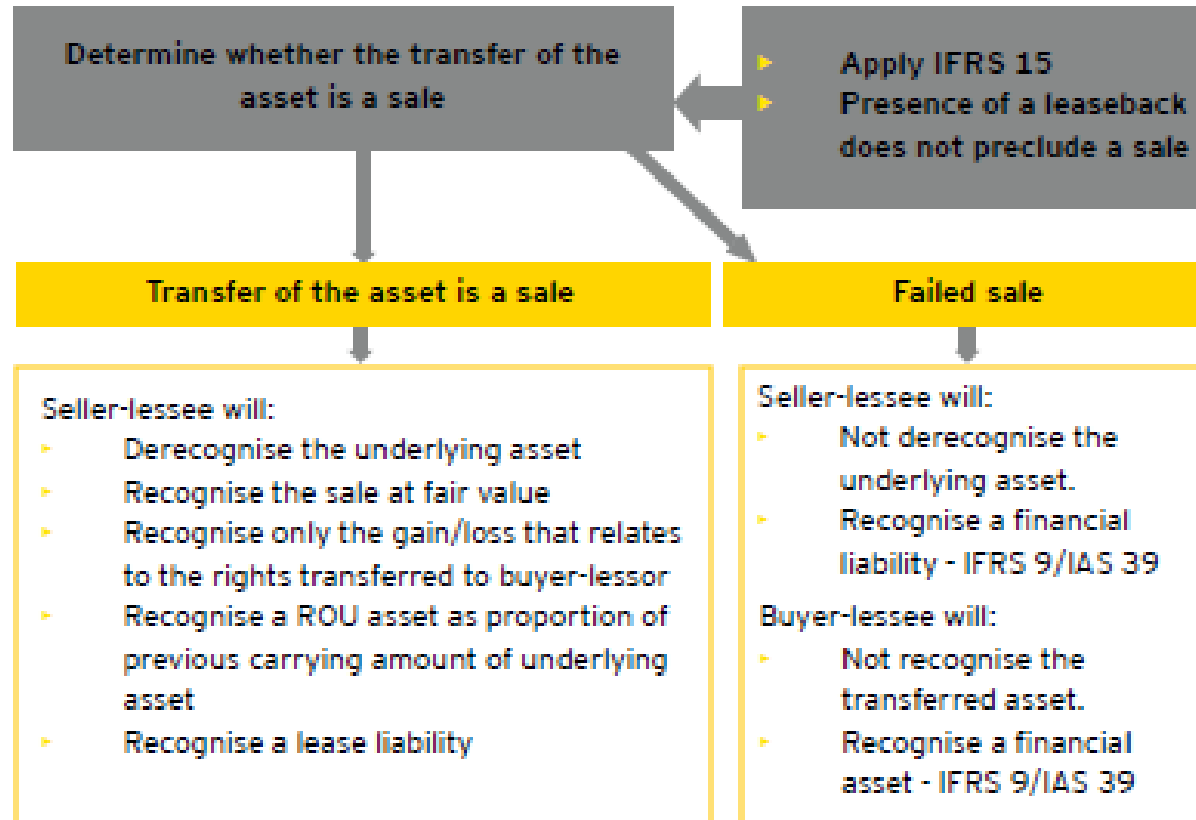
- ▶ Operating leases – recognise lease income on either a straight-line basis or another systematic basis
- ▶ Finance leases
  - ▶ Recognise interest income for the accretion of the net investment in the lease
  - ▶ Payments received reduce the net investment in the lease
  - ▶ The net investment in the lease is subject to derecognition and impairment requirement in IFRS 9 Financial Instruments

# Factors that impact the complexity of implementation



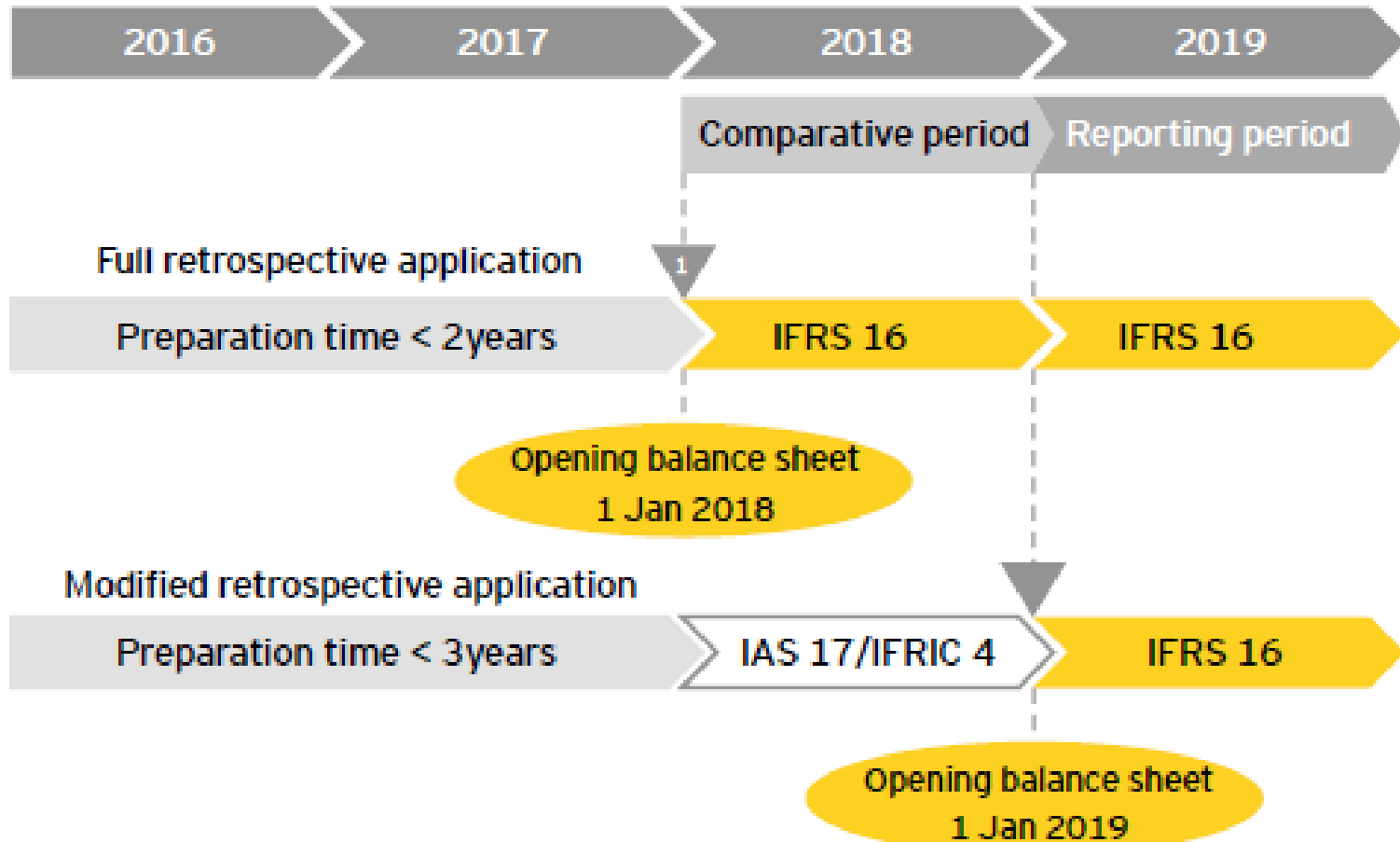
# Key principles of IFRS 16

## Sale and leaseback - recognition and measurement



# Transition

Early preparation is recommended due to complexity of challenges



# How will your business be affected?

## Lessees

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# How will your business be affected?

## Lessors

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- ▶ Accounting is substantially unchanged
- ▶ New disclosure requirements
- ▶ Understand how the standard will affect their customers (lessees)
  - ▶ Request for shorter lease periods
  - ▶ Request for larger portion of variable income
  - ▶ Request for separate pricing of non-lease components

# Lessons learned

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1

## Project structure

Break the project into manageable stages with clear responsibilities, roles and time lines.

3

## Beyond finance

Ensure there is engagement of all stakeholders across the organisation, as this is not just a finance function exercise.

5

## Training and awareness

Develop a clear plan for communication to all stakeholders, including briefing analysts, media and investors, on the impact of the new standard.

2

## Details are crucial

Make sure all types of lease are fully understood to give a complete picture of the issues

4

## Act early

Plan for engagement early on, initially with key internal stakeholders, minimising surprises to/from the business later and building a consensus.

6

## Amount of effort

Do not underestimate the amount of work and resources that will be involved. Systems and data gathering impacts may be significant.

# Preparation

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- ▶ Education
- ▶ Project team and planning
- ▶ Diagnostic: understand current state and identify challenges



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