

Ind AS-116 → Leases

↓
Accounting Principles

↓
Application Guidelines

ICAI has merged above two. in its module

Key changes incorporated by Ind AS 116:

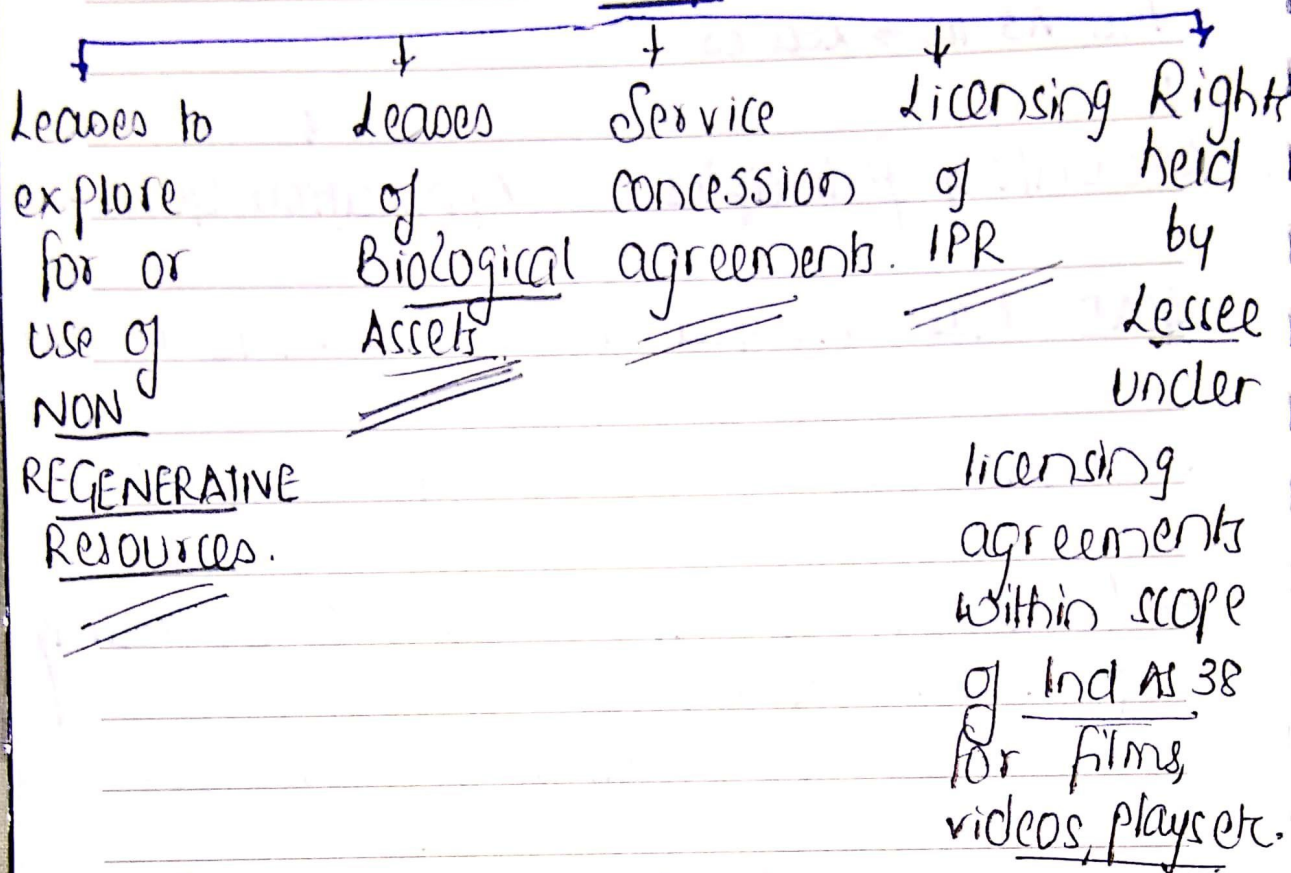
- Scrapped off the concept of Operating & Finance Lease.
- Applicable for Statutory Audits for the year ended 31.03.2020.
- Significantly changes the "Lessor" Accounting

OBJECTIVE: Set out principles for recognition, measurement, p & d of leases.

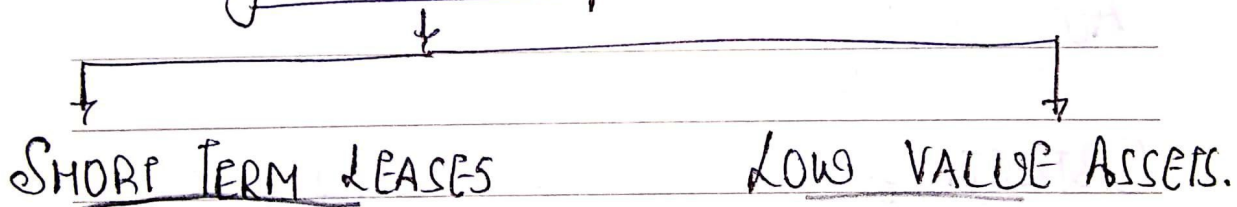
This standard to be applied to all the "Contracts" & all the relevant facts & Circumstances are to be the consideration.



Scope: All Leases + Subleases except



* Recognition exemptions:



- If recognition exemptions are opted, lease payments are to be recorded as an EXPENSE
 - either on straight line basis. or
 - another systematic basis.

Short term Leases:

- ↳ a lease that
 - ↳ at the commencement date
 - ↳ has a lease term of 12 months or less (P)
 - ↳ does not include an option of purchasing the asset.
- Exemption to be availed for a CLASS OF UNDERLYING ASSETS.

Low Value Assets:

- ↳ Conditions for treating an asset as a low value asset

Lessee can benefit from the asset either on its own or with other readily available resources

The underlying asset is not (P) highly dependent or related with other asset.

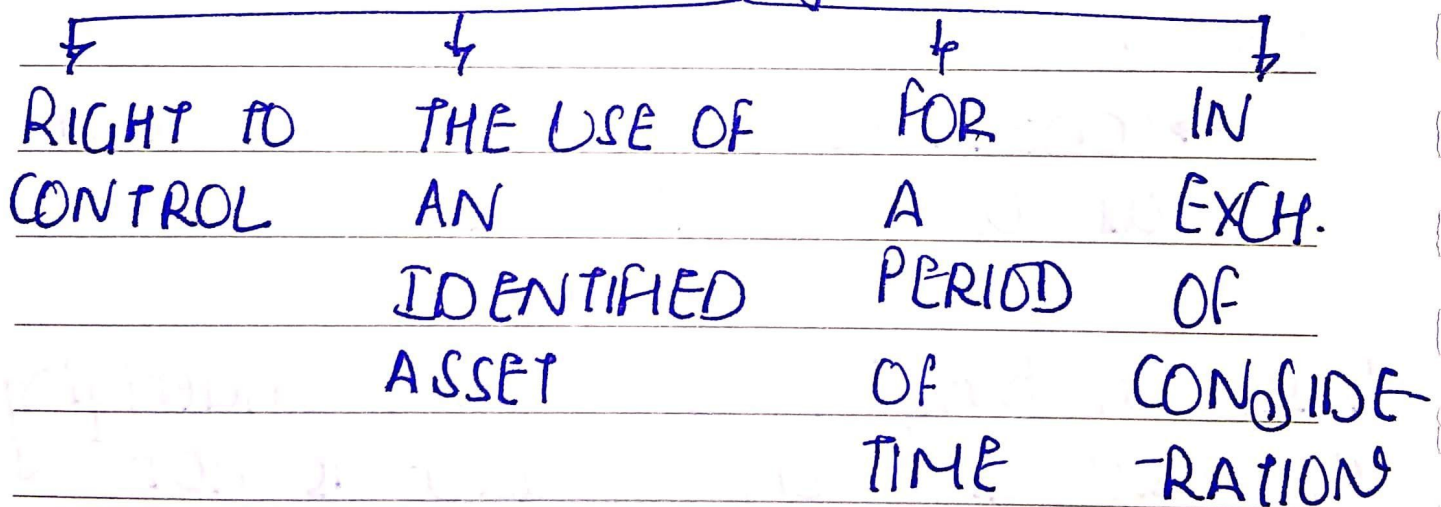
- ~~Ex~~ Exemption of low value assets can be made on lease to lease basis.

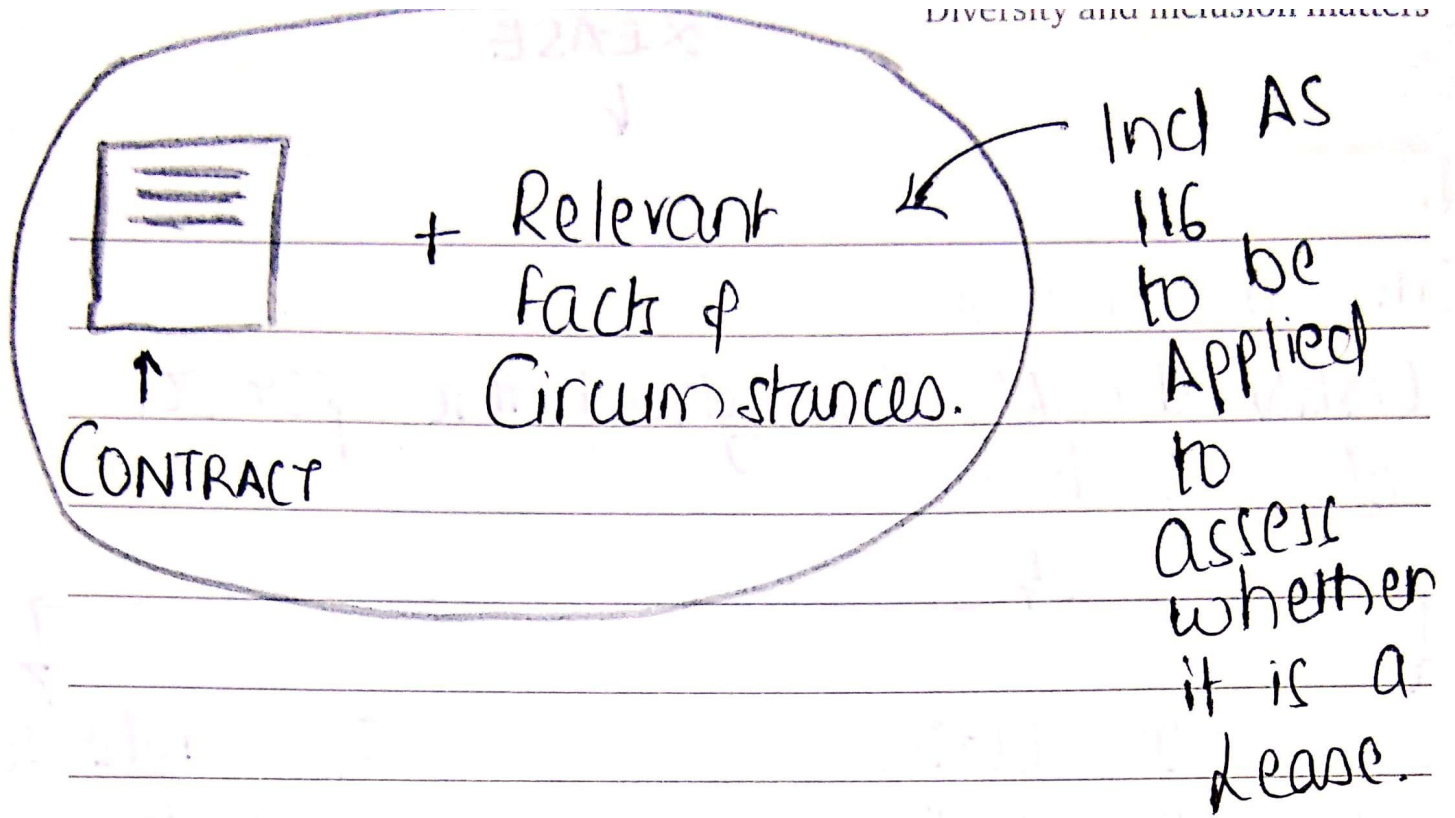
- Low value assets are exempted even if they are material to the assessee.
- Assessment of low value assets is not dependent upon size, nature & circumstances of lessee.
- Assessment to be done on the basis of the value of new asset.

What is a **LEASE?**



A contract
that conveys





Assessment to be done at the inception date or earlier.

↳ Date of Agreement

↳ Date of commitment by the parties to the principle terms & conditions of lease

LEASE

RIGHT TO CONTROL

Entity should, throughout the period of use, have

① The right to obtain substantially all the economic benefits from the use of identified asset

↓
Economic benefits may be direct/indirect.

• If there are such terms in a contract that defines the scope of use of asset, it does not, in itself, prevent the customer from ①
• If the customer has to pay some portion of output to the supplier it also will want ① prevent

• Decision reg "how & for what purpose asset will be used"

Contⁿ to a page next to next page

② THROUGHOUT THE PERIOD OF USE

IDENTIFIED ASSET

- Asset explicitly/implicitly specified in the contract
- Asset is physically distinct.

may be entire asset/portion of asset

↓
not identified asset if not physically distinct unless it represents substantially all the capacity of asset there-by providing the customer ability to get substantially all benefits.

- Supplier must not have substantive substitution Rights over the asset. Right to substitute is substantive when

Supplier has a PRACTICAL ABILITY to substitute the asset

He would BENEFIT ECONOMICALLY BY DOING SO



- The absence of SSR gives the customer the control of the Asset.
- Entity shall evaluate SSR on the basis of facts & circumstances on the inception of contract & shall not consider future events that are not likely to occur.
- Entity should presume that the right of substitution is not substantive if customer cannot readily determine the SSR.

(A)

⇒ Relevant decisions to assess the right to direct the use of asset, this is because such rights determine the economic benefits

Decisions reg. where & when the asset can be used are not that relevant.

for eg., outsourcing of operations does not prevent right to direct the use of asset.

(Para B24-B30) Right to Direct the Use

↓
Customer has right to direct how & for what purpose asset can be used

↓
If it has power to change how & for what purpose asset is used throughout the period

↓
Consider decision making rights that are most relevant for changing how & for what purpose asset is used

↓
Decisions are relevant when they affect the economic benefits.

These decisions are predetermined (or)

(&)
1) customer has right to operate the asset (or)

2) asset is designed as per customer specifications.

Standard provides examples of such relevant decisions.

Protective Rights:

↳ Does not in itself prevent the customer from having the right to direct the use of asset.

Separation of Lease & Non Lease Components:

↳ Lease components

The right to use of an asset is considered as a separate lease component only if

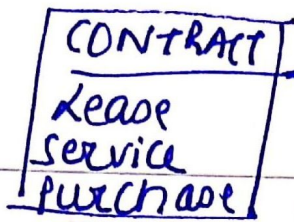
↓
The lessee can benefit from the asset either on its own or ~~from~~ with resources readily available with him

↓
(AND) The underlying asset is neither highly dependent on, nor highly interrelated with the other underlying assets.

If the above criteria are not met, the right to use of multiple assets shall be considered as a SINGLE LEASE COMPONENT.

Separation

Diversity and inclusion matters



⇒ ONLY ITEMS THAT CONTRIBUTE TO SECURE THE OUTPUT OF ASSET CAN BE CONSIDERED AS Lease Components.

Other components are separated & accounted separately.

<u>Contract:</u>		
Lease	xx	→ Ind AS 116
Service	xx	→ Ind AS 115
	xxx	
Gst	xx	
Total.	xxv	

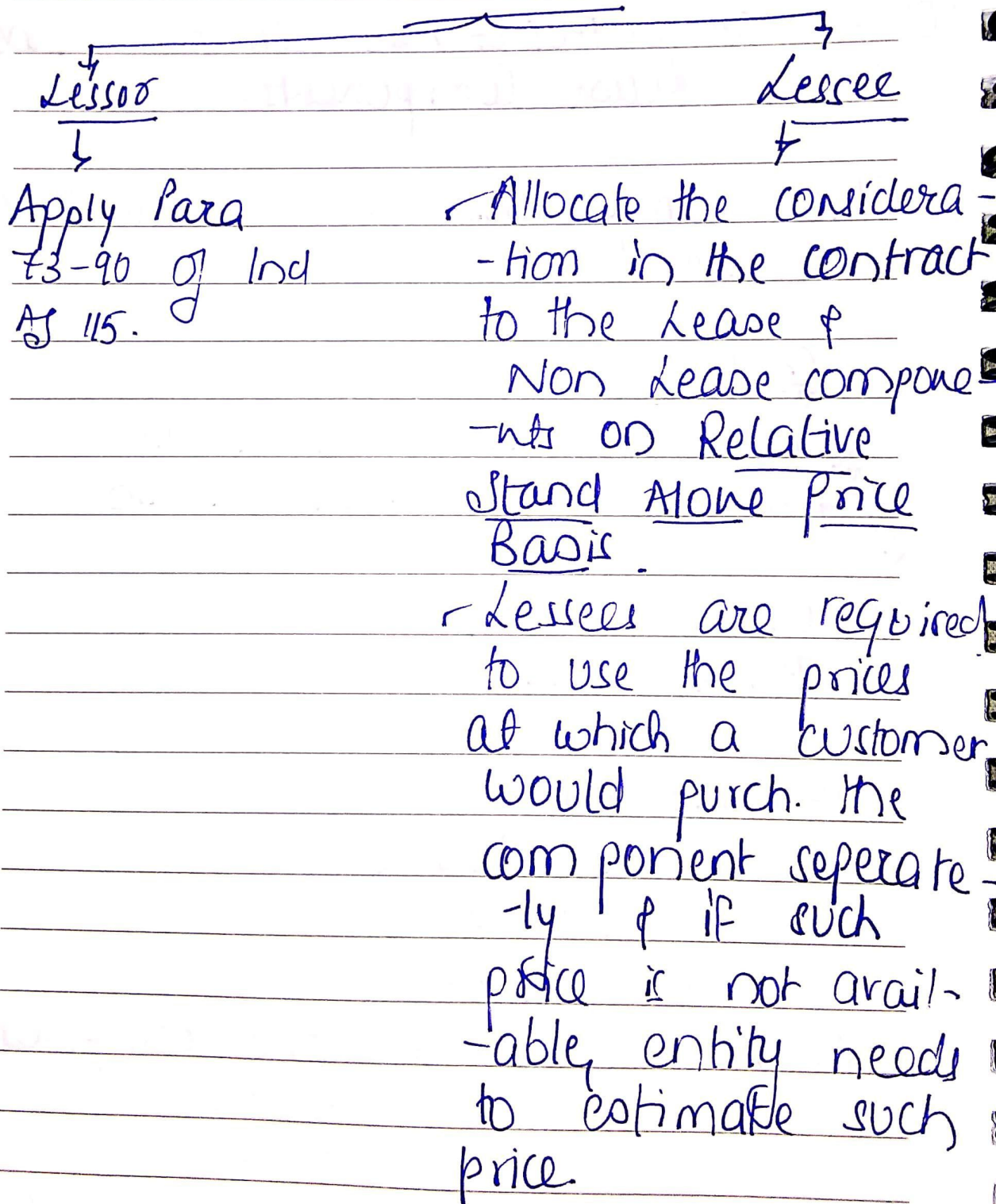
• Payments for

- maintainance
- materials
- operations

not termed as a Lease components

Practical Expedient [★]

Determining & Allocating Consideration



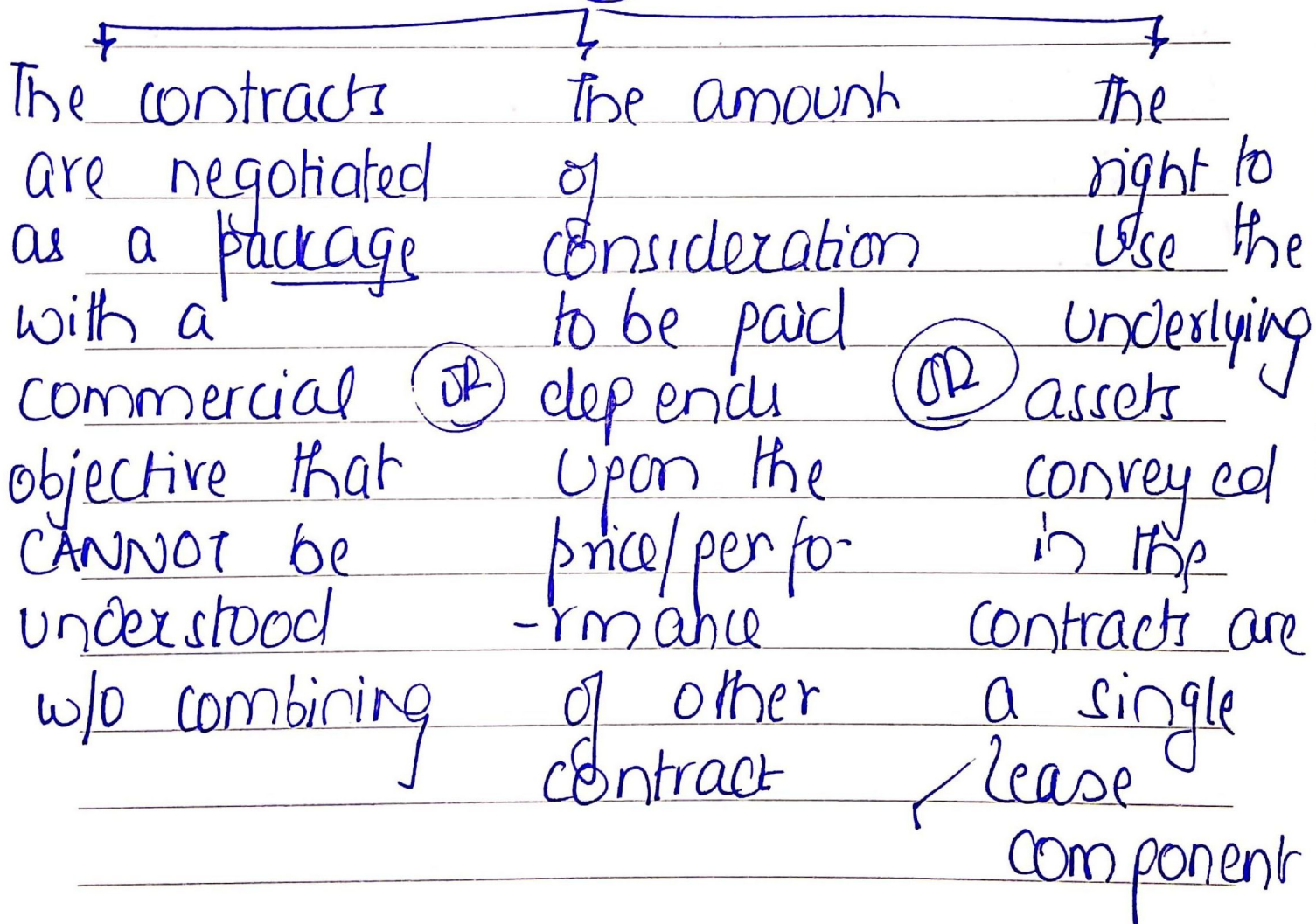
Combination of Contracts:

↳ 2 or more contracts

↳ entered into at or near the same time

↳ with same counterparty

↳ to be considered as a single contract if



Portfolio Application:

Where there are large number of leases of similar assets where lease by lease application becomes practically tough, Ind AS 116 permits portfolio application.

Condition:

The entity should reasonably expect that the effects on the financial statements would not materially differ had the application was done on lease to lease basis.

Inception Date :: Agreement
Commitment Diversity and inclusion matters

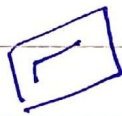
Commencement Date

↳ the date on which the lessor makes an underlying asset

↳ Available for use

If commencement date is before the inception date, the lease term is deemed to be commenced even if no rent is to be paid.

Lease Term:



- ✓ Non Cancellable Period (+)
- ✓ Period covered by option to extend if the lessee is reasonably certain that it will exercise the option (+)
- ✓ Period covered by option to terminate the lease if the lessee is reasonably certain that it will not exercise the option.

✓ Assessment to be done on the commencement date.

✓ Detailed discussion in module.

• Lease term begins at the commencement date.

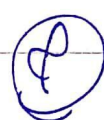
Cancellable Leases:

Lease term → Non cancellable → Apply
term Defⁿ of
CONTRACT

To determine for what period the contract is enforceable. ←

An arrangement is not enforceable if

Both the parties have right to terminate w/o permission of each other



with no more than an insignificant penalty.

Right to terminate.

Diversity and inclusion matters

Lessor

Lessee

Option to terminate

Option to terminate

↳ NON CANCELLABLE PERIOD.

Assess the option

⇒ Reassessment of Lease term & Purchase option

• Lessees are required to monitor the leases for significant changes that can change the lease term

Reassessment

if

Significant event/change

that is within the control of lessee.

that affects the certainty to exercise / not to exercise renewal / termination / purch.

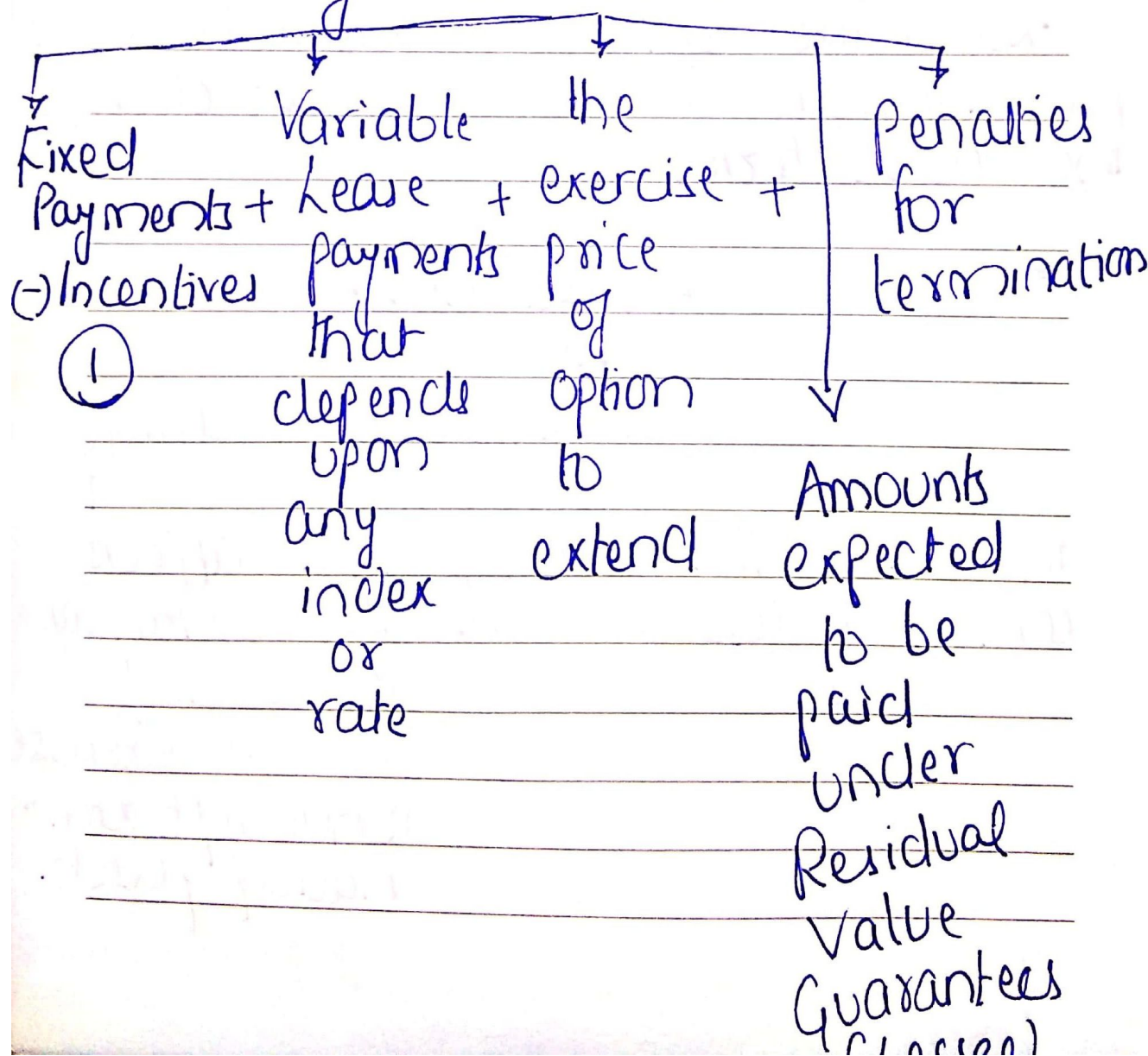


Examples: [Pg 7.99 of module]

* Changes in market based factors that are not under control of the lessee does not, in itself, trigger a reassessment.

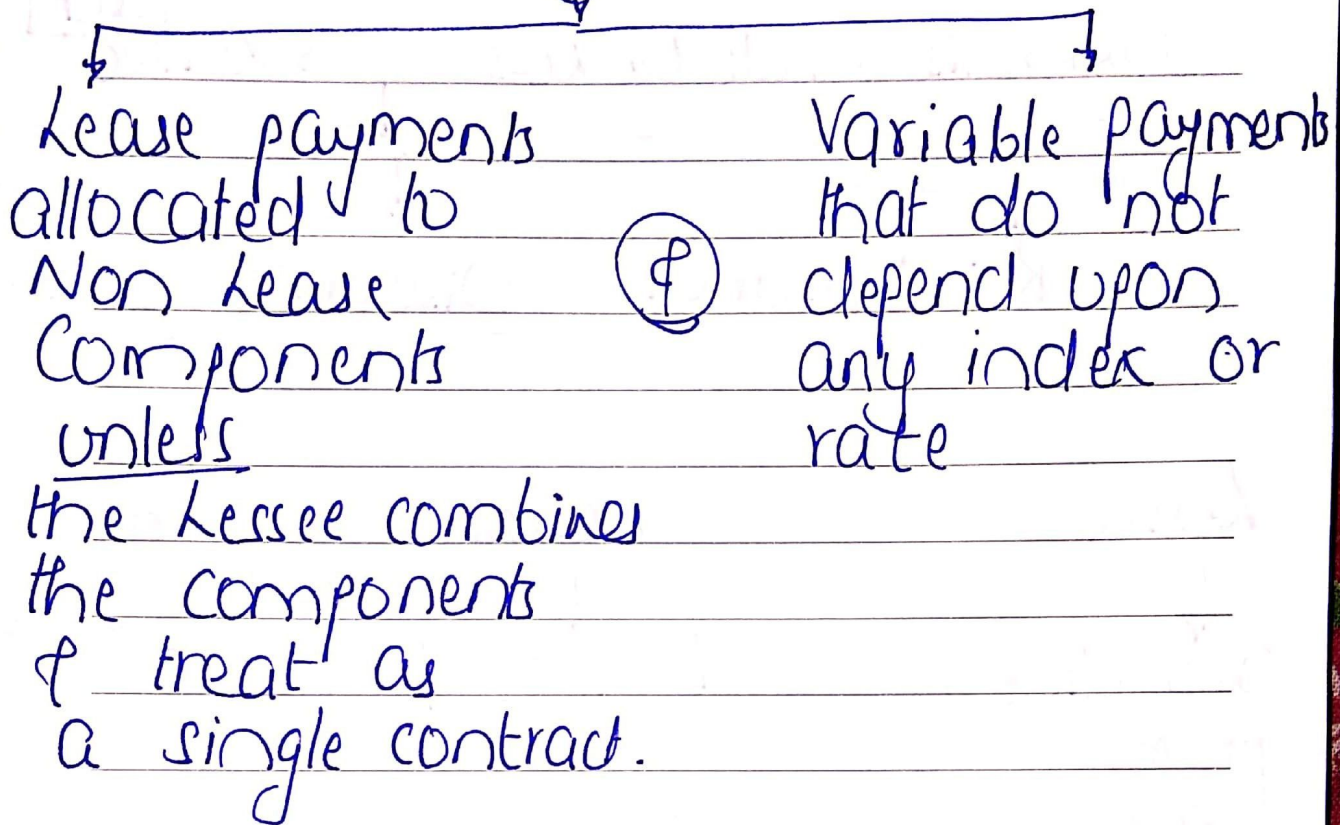
"LEASE PAYMENTS"

→ Payments made by lessee relating to the right to use the Asset



Exclusion from lease payments:

Diversity and inclusion matters



① Fixed Payments:

- Either a fixed amount paid at fixed intervals [£10,000 for 3 years annually]
- or payments that change over time [£10,000 in 1st year, £15000 in 2nd year & so on]

"In substance" fixed payments

- Payments that are in form variable but in substance unavoidable. (Pg 7.102 contains examples)



Incentives:

Evaluate the Nature
of Incentive & Determine whether it is an Asset

Payments made by lessor → lessee

Reimbursement

Discount

Assumption

of
cost
of
lessee

Lessee



Deductible
from
lease
payments

⊕

reduce
initial
measurement
of ROU
Asset

lessor



Deducted
from
lease
payments

⊕

if

↓
Finance
Lease



Reduce
the
Net
Investment

↓
Operating
Lease



Reduce
the
Lease
Income
over the
lease terms

Variable Lease Payments: [That Depend upon an Index or Rate]

→ Payments that vary because of changes in facts & circumstances occurring after the commencement date.

→ for eg., payments linked to consumer price index (CPI) or such other indices, interest benchmarks like LIBOR/MIBOR (London Interbank Offer Rate).

→ Such payments are INCLUDED in the lease payments & measured using the prevailing rates.
[Refer Illustration 23 (Pg 7.105) for clarity]

→ If a lease contract stipulates such payments, it becomes "unavoidable" & they also do not depend upon future activity of lessee" & hence it meets the defⁿ of Lease Liability



Lease payments that do not depend upon index or rate.

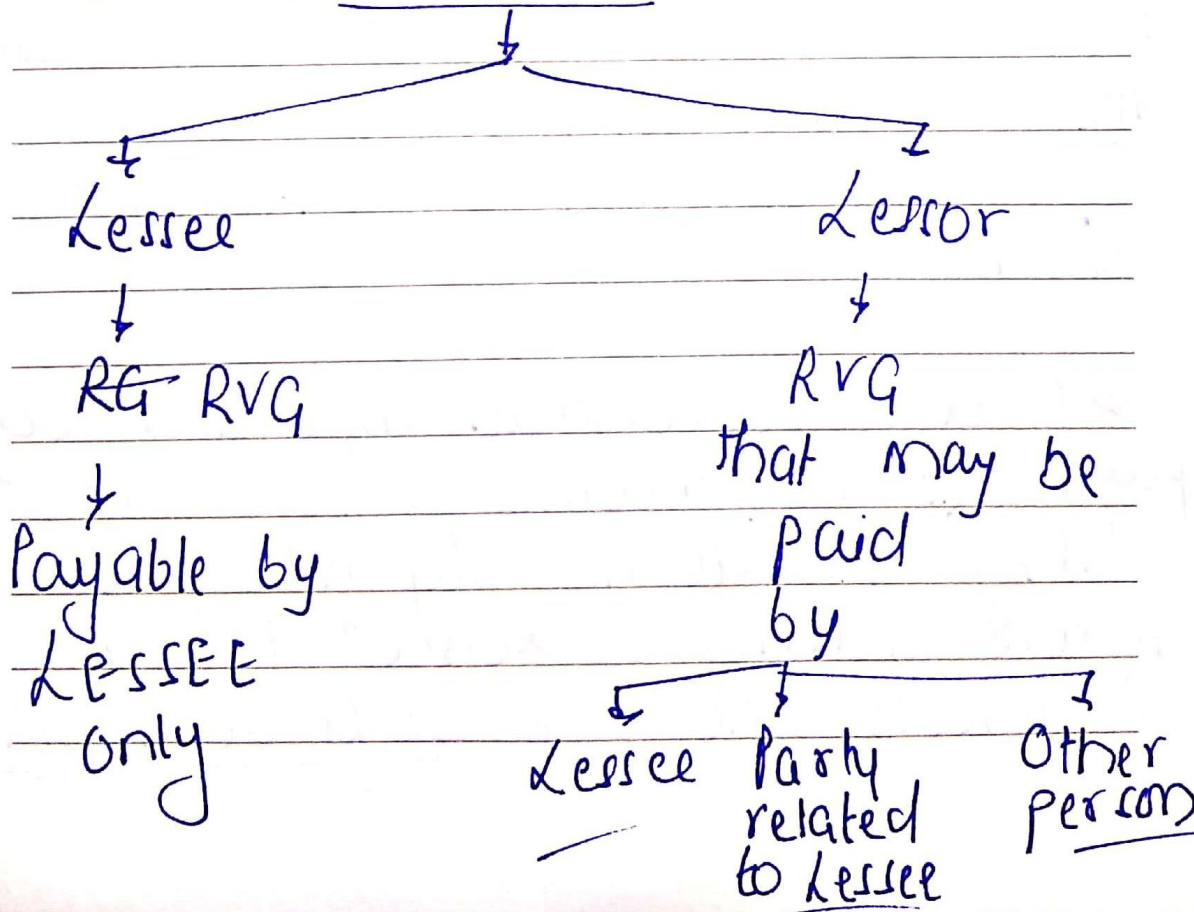
= Variable lease payments that are not substance as fixed.

for eg., payments based on performance, usage or results of the asset

- These are NOT INCLUDED in the lease payments & recognised in P&L.

[Refer example 25]

→ Residual Value Guarantees:



Lease Payments

Lease Payments

Fixed &
In substance
fixed &
fixed in
nature &
accrue over
period

Variable

Depend
Upon
any
index
or
rate
↓
Include

Does not
depend upon
any index
or
rate
↓
Exclude

Exercise
price (Option)
& or
penalties
(Termination)

Exercise
price
↓
Include

Termination
penalty
↓
Exclude

Only if entity is
reasonably certain

RGVs
↓
Include

Diversity and inclusion matters