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Alerte de votre conseiller IFRS

Aperçu d'IFRS 16 *Contrats de location*

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Résumé

Grant Thornton International Ltd a mis à jour *Insights into IFRS 16 – Sale and leaseback accounting* (en anglais seulement).

Présentation

La série *Insights into IFRS 16* résume les éléments clés de la norme IFRS 16 *Contrats de location* et cherche à démystifier les exigences qui se révèlent difficiles à appliquer. Depuis sa première publication, la norme a fait l'objet de plusieurs modifications, ainsi que de décisions de l'IFRS Interpretation Committee (IFRIC) relatives à la norme IFRS 16. Grant Thornton International Ltd procède donc actuellement à une révision et à une mise à jour de ses publications afin de s'assurer qu'elles reflètent toutes les informations et les directives les plus récentes, en mettant l'accent sur les domaines ayant fait l'objet de modifications.

Le document mis à jour *Insights into IFRS 16 – Sale and leaseback accounting* fournit des indications sur la comptabilisation des transactions de cession-bail.

Contexte

La norme IFRS 16 apporte des modifications notables à la comptabilisation des transactions de cession-bail.

Une transaction de cession-bail est une méthode couramment utilisée par les entités pour obtenir un financement à long terme à partir d'immobilisations corporelles importantes telles que des terrains et des bâtiments. Il s'agit d'une transaction dans laquelle une entité (le vendeur-preneur) cède un bien à une autre entité (l'acheteur-bailleur) moyennant une contrepartie et qu'elle le reprend en location de l'acheteur-bailleur.

La norme IAS 17 *Contrats de location* traitait en détail de la comptabilisation d'une transaction de cession-bail, mais uniquement du point de vue du vendeur-preneur. Puisque la norme IFRS 16 a supprimé les concepts de contrats de location simple et de contrats de location-financement de la comptabilisation par le preneur, les exigences comptables que le vendeur-preneur doit appliquer à une transaction de cession-bail sont désormais plus simples. En outre,

la norme IFRS 16 fournit également un aperçu des exigences comptables applicables aux acheteurs-bailleurs.

Le document mis à jour explique les nouveaux concepts et fournit des exemples illustrant ces exigences.

Ressource

Le document *Insights into IFRS 16 – Sale and leaseback accounting* est joint à la présente *Alerte de votre conseiller*.

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À propos de Raymond Chabot Grant Thornton

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Insights into IFRS 16

Sale and leaseback accounting

The introduction of IFRS 16 'Leases' addressed many of the shortcomings of its predecessor. The result is a robust, fit for purpose framework that delivers a level of transparency and insight that was previously unavailable to investors.

Our 'Insights into IFRS 16' series summaries key areas of the Standard and aims to demystify those key requirements that are challenging to apply in practice. This article considers accounting for sale and leaseback arrangements.

A sale and leaseback transaction is a common arrangement and one that many entities may use to manage and finance their assets. IFRS 16 includes specific requirements for sale and leaseback accounting. A sale and leaseback transaction is one where an entity (the seller-lessee) transfers an asset to another entity (the buyer-lessor) for consideration and leases that asset back from the buyer-lessor.

When a seller-lessee has undertaken a sale and lease back transaction with a buyer-lessor, both the seller-lessee and the buyer-lessor must first determine whether the transfer qualifies as a sale. This determination is based on the requirements for satisfying a performance obligation in IFRS 15 'Revenue from Contracts with Customers'.

The accounting treatment will vary depending on whether or not the transfer qualifies as a sale. This is described opposite.

Transfer of the asset is a sale

Initial recognition

If the transfer qualifies as a sale according to IFRS 15 (ie it results in the transfer of control of the underlying asset – for more of the IFRS 15 five step control-based model refer to our article '**Insights into IFRS 15 – Overview and scope**') and the transaction is on market terms the seller-lessee should recognise:

- a portion of the carrying amount of the underlying asset as a right-of-use asset arising from the leaseback, and
- the remaining portion of the carrying amount of the underlying asset as the cost of the rights in the asset transferred to the buyer-lessor when calculating the gain or loss on disposal.

"Our 'Insights into IFRS 16' series summaries key areas of the Standard and aims to demystify those key requirements that are challenging to apply in practice."

From an economic standpoint, the seller-lessee has sold only its interest in the value of the underlying asset at the end of the leaseback, and it has retained its right to use the asset for the duration of the leaseback.

The seller-lessee recognises a portion of the total gain or loss on the sale. The total gain or loss is split into:

- an unrecognised amount relating to the rights retained by the seller-lessee, and
- a recognised amount relating to the buyer-lessor's rights in the underlying asset at the end of the leaseback.

Recognising the gain that relates only to the rights transferred to the buyer-lessor appropriately reflects the economics of the transaction, ie that only a portion of the underlying asset has been transferred to the buyer-lessor.

The leaseback itself is then accounted for under the lessee accounting model.

The buyer-lessor accounts for the purchase in accordance with the applicable IFRS Accounting Standards (eg IAS 16 'Property, Plant and Equipment' if the asset is property, plant or equipment or IAS 40 'Investment Property' if the property is investment property). The lease is then accounted for as either a finance lease or an operating lease using IFRS 16's lessor accounting requirements.

Adjustments are required if consideration for the sale is not at fair value and/or payments for the lease are not at market rates. These adjustments result in recognition of:

- a prepayment to reflect below-market terms
- additional financing provided by the buyer-lessor to the seller-lessee to reflect above-market terms.

Example 1 – Sale and leaseback

SellCo sells a building to BuyCo for cash of CU1,800,000, which is its fair value at that date. The previous carrying value of the building is CU1,000,000. At the same time, SellCo enters into a lease with BuyCo conveying back the right to use the building for 18 years. Annual payments are CU120,000 payable at the end of each year, which is at market rate. The transfer qualifies as a sale based on the guidance on satisfying a performance obligation in IFRS 15.

The rate implicit in the lease is 4.5%, which is readily determinable by SellCo.

Analysis

a) SellCo

The present value of the annual payments (18 payments of CU120,000, discounted at 4.5%) is CU1,459,200.

SellCo measures the right-of-use asset retained through the leaseback as a proportion of the previous carrying amount of the building. This is calculated as: CU1,000,000 (previous carrying value) x [CU1,459,200 (PV of lease payments)/ CU1,800,000 (fair value of building)]. The right-of-use asset calculated in this way is CU810,667.

SellCo recognises a portion of the total gain on the sale, to the extent it relates to the rights retained in the underlying asset by BuyCo at the end of the leaseback. The total gain on sale of building is CU800,000 (CU1,800,000 – CU1,000,000). This total is split into:

- the portion relating to the rights to use the building retained by SellCo, calculated as CU800,000 × [CU1,459,200/ CU1,800,000] which is CU648,533, and
- the portion relating to BuyCo's rights in the underlying asset at the end of the leaseback, calculated as CU800,000 × [(CU1,800,000 – CU1,459,200)/CU1,800,000], which is CU151,467.

The first portion is not recognised, while the second portion should be accounted for as a gain in the statement of profit or loss.

At the commencement date, SellCo's accounting entries are:

	Debit (CU)	Credit (CU)
Cash	1,800,000	–
Right-of-use asset*	810,667	–
Building	–	1,000,000
Gain on sale*	–	151,467
Lease liability	–	1,459,200

b) BuyCo

At the commencement date, BuyCo's accounting entries are:

	Debit (CU)	Credit (CU)
Building	1,800,000	–
Cash	–	1,800,000

BuyCo classifies the lease as an operating lease taking into account, among other things, that the present value of the lease payments is 19% less than the fair value of the building. BuyCo accounts for the lease accordingly.

* Adjustments are required if the sale is not at fair value or lease payments are off-market. An entity is not required to assess both, however – only whichever one is more 'readily determinable'.

Subsequent accounting

After the commencement date, the seller-lessee follows IFRS 16 subsequent accounting for the lease for both the right-of-use asset and the lease liability. In terms of the lease liability, the seller-lessee must determine 'lease payments' or 'revised lease payments' in a way that ensures the seller-lessee does not recognise any part of the gain related to the rights retained by them in the transaction. This is applied during the term of the lease, but does not prevent the recognition in the statement of profit or loss of any gain or loss arising from the full or partial termination of the lease.

Transfer of the asset is not a sale

If the transfer does not qualify as a sale the parties account for it as a financing transaction. This means that:

- the seller-lessee continues to recognise the asset on its statement of financial position as there is no sale. The seller-lessee accounts for proceeds from the sale and leaseback as a financial liability in accordance with IFRS 9 'Financial Instruments'. This arrangement is similar to a loan secured over the underlying asset – in other words a financing transaction.
- the buyer-lessor has not purchased the underlying asset and therefore does not recognise the transferred asset on its statement of financial position. Instead, the buyer-lessor accounts for the amounts paid to the seller-lessee as a financial asset in accordance with IFRS 9. From the perspective of the buyer-lessor, this arrangement is a financing transaction.

Example 2 – Financing transaction

Entity A sells a building to Entity B for cash of CU1,800,000, which is its fair value at that date. The previous carrying value of the building is CU1,000,000. At the same time, Entity A enters into a lease with Entity B conveying back the right to use the building for 18 years. Annual payments are CU148,000 payable at the end of each year, which is at market rate.

At the end of the 18-year period Entity A has the right to repurchase the building (a call option) at a nominal price of CU1.

Analysis

a) Entity A

IFRS 15 contains clear guidance that if Entity A has a right to repurchase the asset, then Entity B does not obtain control of the asset, ie no sale has occurred. In making this assessment, Entity A should consider whether the call option is substantive. Entity A determines that the call option is substantive as it has a nominal price of CU1 and the fair value of the building at the end of the 18-year period is expected to be higher. Entity A therefore concludes that the transfer does not qualify as a sale based on the guidance on satisfying a performance obligation in IFRS 15.*

Entity A continues recognising the building on its statement of financial position and recognises a financial liability for the proceeds received from Entity B. No gain or loss is recognised in the statement of profit or loss.

At the commencement date, Entity A's accounting entries are:

	Debit (CU)	Credit (CU)
Cash	1,800,000	–
Financial liability	–	1,800,000

In subsequent accounting Entity A accounts for the annual payment of CU148,000 as repayment of the financial liability and interest in accordance with IFRS 9.

b) Entity B

Entity B does not obtain control of the building and therefore does not recognise the building as property, plant and equipment (PPE) on its statement of financial position. Instead Entity B recognises a financial asset.

At the commencement date, Entity B's accounting entries are:

	Debit (CU)	Credit (CU)
Financial asset	1,800,000	–
Cash	–	1,800,000

In subsequent accounting Entity B accounts for the annual cash receipt of CU148,000 as reduction of the financial asset and receipt of interest in accordance with IFRS 9.

*A similar conclusion would be reached if, instead of the call option, Entity A had the unlimited renewal option, meaning that it could obtain substantially all the economic benefits generated by the building during its entire useful life.

Sale and leaseback with variable payments

Sometimes the lease payments relating to a leaseback are completely variable and, as a result, it can be challenging to measure the right-of-use asset. Consequently, in 2020, the IFRS Interpretations Committee (IFRIC) received a question on how to measure the right-of-use asset for a sale and leaseback transaction where the subsequent lease payments are variable.

In their agenda decision, the IFRIC explained that, as with other sale and leaseback transactions, the right-of-use asset should be initially measured as the proportion of the previous carrying amount of the asset that relates to the right-of-use retained by the seller-lessee. It does this by comparing the right-of-use retained via the leaseback to the rights of the entire asset. The Standard does not specify the method to use to do this, see example 3 below for the method IFRIC used to illustrate this.

As part of the amendments to the Standard in 2022, the International Accounting Standards Board (IASB) added a new illustrative example for the sale and leaseback transactions with variable payments. The amendments did not add new guidance on measurement of the right-of-use asset and lease liability on initial recognition, in line with the IFRIC's conclusion that the IFRS 16 requirements were clear in this respect. The amendments focused on subsequent accounting of sale and leaseback transactions, illustrating two acceptable approaches for reducing the lease liability after initial recognition:

- Expected value of lease payments at the commencement date. This method results in reducing the lease liability each year by the variable lease payments estimated for that year at the commencement date. The difference between the actual payments and the payments initially estimated for each year would be recognised in the statement of profit or loss.
- Equal lease payments over the lease term. This method results in reducing the lease liability each year by equal lease payments. The difference between the actual payments for each year and the equal payments used for reducing the lease liability would be recognised in the statement of profit or loss.

The Standard allows either approach to be used for subsequent accounting of a lease liability depending on the facts and circumstances, including considering the method used for the initial measurement.

Example 3 – Sale and leaseback with variable payments

Consider the same fact pattern set out in Example 1, and assume that the building is a large retail space that will be used for a supermarket. However, instead of annual lease payments of CU120,000, the payment will be entirely variable and determined as a percentage of the revenue generated by the supermarket throughout the 18-year lease term. This is concluded to be at market rate. At the lease commencement date, the present value (PV) of the expected payments throughout the term of the lease is determined to be CU450,000.

Analysis

a) SellCo

SellCo performs the same assessment as before to compare the value of the rights retained to the previous carrying value of the asset. SellCo used the expected value of payments. This is calculated as: CU1,000,000 (previous carrying value) x [CU450,000 (PV of expected lease payments)/ CU1,800,000 (fair value of building)]. The right-of-use asset calculated in this way is CU250,000.

SellCo recognises a portion of the total gain on the sale, to the extent it relates to the rights retained in the underlying PPE by BuyCo at the end of the leaseback. The total gain on sale of building is CU800,000 (CU1,800,000 – CU1,000,000). This total is split into:

- the portion relating to the rights to use the building retained by SellCo, calculated as CU800,000 × [CU450,000/ CU1,800,000] which is CU200,000, and
- the portion relating to BuyCo's rights in the underlying asset at the end of the leaseback, calculated as CU800,000 × [(CU1,800,000 – CU450,000)/CU1,800,000], which is CU600,000.

The first portion is not recognised, while the second portion should be accounted for as a gain in the statement of profit or loss. At the commencement date, SellCo's accounting entries are:

	Debit (CU)	Credit (CU)
Cash	1,800,000	–
Right-of-use asset	250,000	–
PPE	–	1,000,000
Gain on sale	–	600,000
Lease liability	–	450,000

For the subsequent accounting SellCo uses the 'expected value of lease payments at the commencement date' method. At the commencement date SellCo estimated variable lease payments for the first year of the lease to be CU30,000. The actual lease payments based on the percentage of revenue generated in year 1 were CU31,000. Interest on the lease liability was determined to be CU20,250 based on an interest rate of 4.5%. SellCo recognises depreciation on the right-of-use asset based on a straight-line method over the 18-year period.

In year 1 of the lease, SellCo's accounting entries would be:

	Debit (CU)	Credit (CU)
Lease liability	30,000	–
Variable lease expense	1,000	–
Cash	–	31,000
Interest expense	20,250	–
Lease liability	–	20,250
Depreciation expense	13,889	–
Right-of-use asset	–	13,889

Example 3 – Sale and leaseback with variable payments (continued)

Analysis

b) BuyCo

BuyCo applies the guidance in IFRS 16, recognising the purchase of the asset by applying applicable standards and accounting for the lease under the lessor accounting requirements in IFRS 16.

	Debit (CU)	Credit (CU)
Building	1,800,000	–
Cash	–	1,800,000

At the commencement date, BuyCo's accounting entries are:

BuyCo classifies the lease as an operating lease taking into account, among other things, that the present value of the lease payments is 25% of the fair value of the building. Entirely variable payments dependent on SellCo's revenue also indicate that BuyCo did not transfer to SellCo substantially all the risks and rewards associated with the asset.

BuyCo accounts for the lease accordingly. Variable lease payments are recognised as income in the profit or loss. They are recognised in the period in which a change occurs in the facts and circumstances on which the variable payments are based, in this case based on the percentage of the revenue generated by the supermarket in each particular year. In year 1 BuyCo recognises lease income of CU31,000.

How we can help

We hope you find the information in this article helpful in giving you insight into aspects of IFRS 16. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact or visit **www.grantthornton.global/locations** to find your local member firm.

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