



IAS 17 LEASES

FACT SHEET

This fact sheet is based on existing requirements as at 31 December 2015 and it does not take into account recent standards and interpretations that have been issued but are not yet effective.

IMPORTANT NOTE

This fact sheet is based on the requirements of the International Financial Reporting Standards (IFRSs). In some jurisdictions, the IFRSs are adopted in their entirety; in other jurisdictions the individual IFRSs are amended. In some jurisdictions the requirements of a particular IFRS may not have been adopted. Consequently, users of the fact sheet in various jurisdictions should ascertain for themselves the relevance of the fact sheet to their particular jurisdiction. The application date included below is the effective date of the initial version of the standard unless otherwise stated.

IASB APPLICATION DATE (NON-JURISDICTION SPECIFIC)

IAS 17 was reissued in December 2003 and is applicable for annual reporting periods commencing on or after 1 January 2005.

OBJECTIVE

The objective of IAS 17 is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases.

SCOPE

IAS 17 shall be applied in accounting for all leases except the following:

- leases to explore for, or use, minerals, oil, natural gas and similar non-regenerative resources; and
- licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights.

IAS 17 also does not apply as the basis of measurement for:

- property held by lessees that is accounted for as an investment property (refer to IAS 40 *Investment Property*);
- investment property provided by lessors under operating leases (refer to IAS 40);
- biological assets held by lessees under finance leases (refer to IAS 41 *Agriculture*); or
- biological assets provided by lessors under operating leases (refer to IAS 41).

CLASSIFICATION

At inception, the lease is classified either as an operating or finance lease, with the lease classification depending on the substance of the transaction rather than the legal form. The classification of leases adopted in IAS 17 is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee.

IAS 17 provides the following examples and indicators of situations that individually or in combination would normally lead to a lease being classified as a finance lease.

Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease:

- the lease transfers ownership of the asset to the lessee by the end of the lease term;
- 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;
- the lease term is for the major part of the economic life of the asset even if title is not transferred;
- 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; and
- the leased assets are of such a specialised nature that only the lessee can use them without major modifications.

Indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease:

- if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
- gains or losses from the fluctuation in the fair value of the residual accrue to the lessee (for example, in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and
- the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

RECOGNITION AND MEASUREMENT

The measurement and disclosure requirements for finance leases and operating leases are shown in Table 1 and Table 2 respectively. The tables detail the measurement and disclosure requirements applicable to both lessees and lessors.

TABLE 1
Measurement and disclosure requirements for finance leases in the financial statements of lessees and lessors

FINANCIAL STATEMENTS OF LESSEES	FINANCIAL STATEMENTS OF LESSORS
<p>Initial recognition</p> <ul style="list-style-type: none"> • finance leases are recognised as assets and liabilities at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments each determined at the inception of the lease. • the discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate is used. • any initial direct costs of the lessee are added to the amount recognised as an asset. 	<p>Initial recognition</p> <ul style="list-style-type: none"> • assets held under a finance lease are presented as a receivable at an amount equal to the net investment in the lease.
<p>Subsequent measurement</p> <ul style="list-style-type: none"> • minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. • the finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. • contingent rents are charged as expenses in the periods in which they are incurred. • the depreciation policy for depreciable leased assets is to be consistent with that for depreciable assets that are owned, and the depreciation recognised is calculated in accordance with IAS 16 <i>Property, Plant and Equipment</i> and IAS 38 <i>Intangible Assets</i>. • if there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset should be fully depreciated over the shorter of the lease term and its useful life. 	<p>Subsequent measurement</p> <ul style="list-style-type: none"> • 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. • manufacturer or dealer lessors recognise selling profit or loss in the period, in accordance with the policy followed by the entity 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 recognised as an expense when the selling profit is recognised.

TABLE 2
Measurement and disclosure requirements for operating leases in the financial statements of lessees and lessors

FINANCIAL STATEMENTS OF LESSEES	FINANCIAL STATEMENTS OF LESSORS
<p>Recognition</p> <ul style="list-style-type: none"> lease payments are recognised as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit. 	<p>Recognition</p> <ul style="list-style-type: none"> assets under operating leases presented in the statement of financial position based on nature of the asset. lease income is recognised on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished. initial direct costs incurred by lessors in negotiating and arranging an operating lease shall be added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease income depreciation policy on depreciable leased assets is to be consistent with lessor's normal depreciation policy for similar assets, and depreciation calculated in accordance with IAS 16 and IAS 38.

SALE AND LEASEBACK TRANSACTIONS

The accounting treatment of a sale and leaseback transaction by a seller-lessee depends upon the type of lease involved:

- sale and leaseback transaction resulting in a finance lease: any excess of sales proceeds over the carrying amount shall be deferred and amortised over the lease term
- sale and leaseback transaction resulting in an operating lease:
 - if the transaction is established at fair value: any profit or loss shall be recognised immediately
 - if the sale price is below fair value: any profit or loss shall be recognised immediately except that, if the loss is compensated for by future lease payments at below market price, it shall be deferred and amortised 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 excess over the fair value is deferred and amortised over the period for which the asset is expected to be used
 - if the fair value at the time of a sale and leaseback transaction is less than the carrying amount of the asset, a loss equal to the amount of the difference between the carrying amount and the fair value is recognised immediately.

DISCLOSURES

Refer to Appendix 1 for a checklist to assist with IAS 17 disclosure requirements.

DEFINITIONS

Economic life	<p>either:</p> <ol style="list-style-type: none"> the period over which an asset is expected to be economically usable by one or more users; or the number of production or similar units expected to be obtained from the asset by one or more users.
Finance lease	lease that transfers substantially all the risks and rewards incidental to ownership of an asset, title may or may not eventually be transferred.
Guaranteed residual value	<ol style="list-style-type: none"> for a lessee, that part of the residual value that is guaranteed by the lessee or by a party related to the lessee (the amount of the guarantee being the maximum amount that could, in any event, become payable); and for a lessor, that part of the residual value that is guaranteed by the lessee or by a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.
Inception of the lease	<p>the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease; at this date:</p> <ol style="list-style-type: none"> a lease is classified as either an operating or a finance lease; and in the case of a finance lease, the amounts to be recognised at the commencement of the lease are determined.
Initial direct costs	incremental costs that are directly attributable to negotiating and arranging a lease, except for such costs incurred by manufacturer or dealer lessors.
Interest rate implicit in the lease	<p>the discount rate that, at the inception of the lease, causes the aggregate present value of:</p> <ol style="list-style-type: none"> the minimum lease payments; and the unguaranteed residual value. <p>to be equal to the sum of:</p> <ol style="list-style-type: none"> the fair value of the leased asset; and any initial direct costs of the lessor.
Lease	an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.
Lease term	the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

Minimum lease payments	<p>payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:</p> <ul style="list-style-type: none"> a. for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or b. for a lessor, any residual value guaranteed to the lessor by: <ul style="list-style-type: none"> i. the lessee; ii. a party related to the lessee; or iii. a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee. <p>However, if the lessee has an 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, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.</p>
Net investment in the lease	the gross investment in the lease discounted at the interest rate implicit in the lease.
Non-cancellable lease	<p>lease that is cancellable only:</p> <ul style="list-style-type: none"> a. upon the occurrence of some remote contingency; b. with the permission of the lessor; c. if the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or d. upon payment by the lessee of such an additional amount that, at inception of the lease, continuation of the lease is reasonably certain.
Operating leases	leases other than finance leases.
Useful life	the estimated remaining period, from the commencement of the lease term, without limitation by the lease term, over which the economic benefits embodied in the asset are expected to be consumed by the entity.

RELATED INTERPRETATIONS

- IFRIC 4 *Determining whether an Arrangement contains a Lease*
- SIC 15 *Operating Leases – Incentives*
- SIC 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*
- SIC 29 *Service Concession Arrangements: Disclosures*

IFRIC 4 and SIC 15 are relatively more significant than the others.

An entity may enter into an arrangement, comprising a transaction or a series of related transactions, that does not take the legal form of a lease but conveys a right to use an asset (e.g. an item of property, plant or equipment) in return for a payment or series of payments. Examples of arrangements in which one entity (the supplier) may convey such a right to use an asset to another entity (the purchaser), often together with related services, include:

- outsourcing arrangements (e.g. the outsourcing of the data processing functions of an entity)
- arrangements in the telecommunications industry, in which suppliers of network capacity enter into contracts to provide purchasers with rights to capacity
- take-or-pay and similar contracts, in which purchasers must make specified payments regardless of whether they take delivery of the contracted products or services (e.g. a take-or-pay contract to acquire substantially all of the output of a supplier's power generator)

IFRIC 4 provides guidance for determining whether such arrangements are, or contain, leases that should be accounted for in accordance with Accounting Standard IAS 17 *Leases*.

SIC 15 clarifies the recognition of incentives related to operating leases by both the lessee and lessor. As per SIC 15, lease incentives (such as rent-free periods, up-front cash payment to the lessee by the lessor or the reimbursement or assumption by the lessor of costs of the lessee) should be considered an integral part of the net consideration for the use of the leased asset. The lessor should recognise the aggregate cost of incentives as a reduction of rental income over the lease term, on a straight-line basis unless another systematic basis is representative of the time pattern over which the benefit of the leased asset is diminished. Similarly, the lessee should recognise the aggregate benefit of incentives as a reduction of rental expense over the lease term, on a straight-line basis unless another systematic basis is representative of the time pattern of the lessee's benefit from the use of the leased asset.

AUSTRALIAN SPECIFIC REQUIREMENTS

The Australian equivalent standard is AASB 117 *Leases* and is applicable for annual reporting periods commencing on or after 1 January 2005. The Australian equivalent interpretations are:

- Interpretation 4 *Determining whether an Arrangement contains a Lease*
- Interpretation 115 *Operating Leases – Incentives*
- Interpretation 127 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*
- Interpretation 129 *Service Concession Arrangements: Disclosures*

REDUCED DISCLOSURE REQUIREMENTS (RDR)

On 30 June 2010, the Australian Accounting Standards Board published AASB 1053 *Application of Tiers of Australian Accounting Standards* (and AASB 2010-2 *Amendments to Australian Accounting Standards arising from Reduced Disclosure Requirements*) which established a differential reporting framework, consisting of two Tiers of reporting requirements for preparing general purpose financial statements:

- a. Tier 1: Australian Accounting Standards; and
- b. Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

Tier 2 comprises the recognition, measurement and presentation requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements.

A Tier 2 entity is a 'reporting entity' as defined in SAC 1 *Definition of the Reporting Entity* that does not have 'public accountability' as defined in AASB 1053 and is not otherwise deemed to be a Tier 1 entity by AASB 1053.

RDR is applicable to annual periods beginning on or after 1 July 2013.

When developing AASB 1053, the AASB concluded that the Australian Government and state, territory and local governments should be subject to Tier 1 requirements. The AASB also decided that General Government Sectors of the Australian Government and state and territory governments should continue to apply AASB 1049 *Whole of Government and General Government Sector Financial Reporting*, without the reduction in disclosures provided by Tier 2. Other public sector entities are able to apply Tier 2 reporting requirements.

The requirements that do not apply to RDR entities are identified in Appendix 1 by shading of the relevant text.

APPENDIX 1 – DISCLOSURE CHECKLIST

This checklist can be used to review your financial statements. You should complete the “Yes / No / N/A” column about whether the requirement is included. To ensure the completeness of disclosures, provide an explanation for “No” answers.

CODE		YES / NO / N/A	EXPLANATION (If required)
FINANCE LEASES – LESSEES			
IAS 17.31	<p>Has the entity in addition to meeting the requirements of IFRS 7 <i>Financial Instruments: Disclosure</i>, disclosed the following information for finance leases:</p> <ul style="list-style-type: none"> a. for each class of asset, the net carrying amount at the reporting period; b. a reconciliation between the total of future minimum lease payments at the end of the reporting period, and their present value. In addition, an entity shall disclose the total of future minimum lease payments at the end of the reporting period, and their present value, for each of the following periods: <ul style="list-style-type: none"> – not later than one year; – later than one year and not later than five years; and – later than five years; c. contingent rents recognised as an expense in the period; d. the total of future minimum sublease payments expected to be received under non-cancellable subleases at the end of the reporting period; and e. a general description of the lessee’s material leasing arrangements including, but not limited to, the following: <ul style="list-style-type: none"> – the basis on which contingent rent payable is determined; – the existence and terms of renewal or purchase options and escalation clauses; and – restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing? 		

CODE		YES / NO / N/A	EXPLANATION (If required)
OPERATING LEASES – LESSEES			
IAS 17.35	<p>Has the entity in addition to meeting the requirements of IFRS 7 <i>Financial Instruments: Disclosure</i>, disclosed the following information for operating leases:</p> <ol style="list-style-type: none"> a. the total of future minimum lease payments under non-cancellable operating leases for each of the following periods: <ul style="list-style-type: none"> – not later than one year; – later than one year and not later than five years; and – later than five years; b. the total of future minimum sublease payments expected to be received under non-cancellable subleases at the end of the reporting period; c. lease and sublease payments recognised as an expense in the period, with separate amounts for minimum lease payments, contingent rents, and sublease payments; d. a general description of the lessee's significant leasing arrangements including, but not limited to, the following: <ul style="list-style-type: none"> – the basis on which contingent rent payable is determined; – the existence and terms of renewal or purchase options and escalation clauses; and – restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing? 		
FINANCE LEASES – LESSORS			
IAS 17.47	<p>Has the entity in addition to meeting the requirements of IFRS 7 <i>Financial Instruments: Disclosure</i>, disclosed the following information for finance leases:</p> <ol style="list-style-type: none"> 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, an entity shall disclose the gross investment in the lease and the present value of minimum lease payments receivable at the reporting period, for each of the following periods: <ul style="list-style-type: none"> – not later than one year; – later than one year and not later than five years; and – 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 recognised as income in the period; and f. a general description of the lessor's material leasing arrangements? 		

CODE		YES / NO / N/A	EXPLANATION (If required)
OPERATING LEASES – LESSORS			
IAS 17.56	<p>Has the entity in addition to meeting the requirements of IFRS 7 <i>Financial Instruments: Disclosure</i>, disclosed the following information for operating leases:</p> <p>a. the future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods:</p> <ul style="list-style-type: none"> – not later than one year; – later than one year and not later than five years; and – later than five years; <p>b. total contingent rents recognised as income in the period; and</p> <p>c. a general description of the lessor's leasing arrangements?</p>		

OTHER MATTERS

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