

Wednesday, 17 May 2023

Mr Ian Carruthers  
Chairman  
International Public Sectors Accounting Standards Board  
529 Fifth Avenue New York  
NY 10017 USA

Submission via website: <https://www.ipsasb.org/publications/exposure-draft-ed-84-concessionary-leases-and-right-use-assets-kind>

Dear Ian

### **Concessionary Leases and Right-of-Use Assets In-kind**

As the representatives of over 300,000 professional accountants around the world, Chartered Accountants Australia and New Zealand (CA ANZ) and CPA Australia welcome the opportunity to provide a submission on Exposure Draft (ED) 84 – *Concessionary Leases and Right-of-Use Assets In-kind (Amendments to IPSAS 43 and IPSAS 23)* (the ED). We make this submission on behalf of our members and in the public interest.

We do not support the proposal to initially measure concessionary leases and right-of-use assets in-kind at the present value of payments for the lease at market rates. In our [joint submission](#) to the preceding Request for Information – Concessionary Leases and Other Arrangements Similar to Leases (the RFI) we concluded that the costs of determining the fair value of right-of-use assets arising from concessionary lease arrangements were likely to exceed any expected benefits. While the specific measurement basis for concessionary leases in the ED is “present value of market lease payments” rather than fair value (as originally proposed), we do not consider that this change is sufficient to address our concerns.

Determining the market value of a non-financial asset is a complex and judgemental process which frequently requires entities to engage a professional valuation expert. This process becomes considerably more complex when the asset being measured is specialised, or is subject to restrictions over its use, both of which are common in the public sector. We reiterate our concerns that the requirements that underpin the proposed accounting model for concessionary leases are overly complex and that the costs of applying these requirements would outweigh the benefits, due to the unique challenges faced by the public sector, which are different from those faced by the private sector.

Since the time that phase 1 of the IPSASB's leases project was introduced, the Australian Accounting Standards Board (AASB) has provided a permanent accounting policy choice for public sector entities (and private sector not-for-profit (NFP) entities) to elect to initially measure a class of concessionary right-of-use assets at cost or fair value, with supporting disclosures about the nature and terms of the arrangement.<sup>1</sup> The AASB initially allowed this as a temporary accounting policy choice whilst it undertook further research and outreach. Following this research and outreach, it concluded that it was appropriate to make this accounting policy choice permanent. To date, we are still not aware of any public sector entities in Australia that have chosen the fair value option. In addition, there is no evidence to suggest that reporting using the cost-based approach is not sufficiently meeting the information needs of users.

The **Attachment** to this letter contains our responses to the specific matters for comment raised in the ED. If you have any questions about our submission, please contact either Ram Subramanian (CPA Australia) at [ram.subramanian@cpaaustralia.com.au](mailto:ram.subramanian@cpaaustralia.com.au) or Amir Ghandar (CA ANZ) [amir.ghandar@charteredaccountantsanz.com](mailto:amir.ghandar@charteredaccountantsanz.com).

Sincerely,

**Simon Grant FCA**

Group Executive – Advocacy and International  
**Chartered Accountants Australia and New Zealand**

**Gary Pflugrath FCPA**

Executive General Manager, Policy and Advocacy  
**CPA Australia**

---

<sup>1</sup> [AASB 16 Leases](#), paragraphs Aus25.1–Aus25.2

## Attachment

**Specific Matter for Comment 1: The IPSASB decided to propose new accounting guidance for concessionary leases for lessees (see paragraphs IPSAS 43. BC124–BC137) and right-of-use assets in-kind (see paragraphs IPSAS 23. BC28–BC30). Do you agree with the proposed amendments to IPSAS 43 and IPSAS 23? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.**

We do not agree with the proposed amendments to IPSAS 43 and IPSAS 23 for the reasons outlined below and in our responses to other Specific Matters for Comment.

The financial reporting problem that the proposals in the ED are trying to address is not clear. The underlying drivers behind the proposed amendments, discussed in the Basis for Conclusions, focus on increasing transparency and accountability. If it is about improving the transparency and accountability around the management of public sector assets, then the ED does not address this problem as the proposals primarily focus on lessees. In our view lessees measuring concessionary leases and right-of-use assets in-kind at the present value of market lease payments is not the only, nor the superior, way to provide useful information. In many jurisdictions, these arrangements may already be disclosed as part of service performance reporting and/or related party transactions.

The IPSASB should reconsider the ED in the context of the following new standards which were approved at the 14-17 March 2023 IPSASB meeting:

- IPSAS 46 *Measurement* uses the term “current operational value” which differs from the valuation at “market rates based on the current use of the underlying asset” proposed in the ED.
- IPSAS 47 *Revenue* uses the terms “transactions with/without binding arrangements” which differs from the concepts of “exchange/non-exchange transactions” proposed in the ED.

We encourage the IPSASB to consider whether certain concessionary leases that meet the definition of a lease should be excluded from the scope of IPSAS 43. The IPSASB 43 lease accounting model is based on a foundational presumption that leases are financing arrangements, whereas many concessionary lease arrangements in the public sector are not entered into as financing arrangements. There are requirements in existing accounting standards that address conceptually similar arrangements, for example, services in-kind. In particular, the ED appears to be inconsistent with IPSAS 47 *Revenue* which does not require the recognition of services in-kind. Paragraphs AG143–AG149 of IPSAS 47 explain why it may not be appropriate to fair value services in-kind.

We also encourage the IPSASB to consider a broader range of ‘right to use’ arrangements that exist in the public sector (e.g., arrangements involving the transfer of rights over property), which might not meet the definition of a lease. A holistic approach that fully reflects the attributes of rules and rights that apply over the use of assets in the public sector is likely to be more fit-for-purpose than an accounting approach that is derived from private sector lease contracts.

**Specific Matter for Comment 2: For lessors, the IPSASB decided to propose accounting for leases at below-market terms in the same way as for leases at market terms (see paragraphs IPSAS 43. BC138–BC149). Do you agree with the proposed amendments to IPSAS 43? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.**

We agree with the proposed accounting for operating leases by lessors as set out in paragraph 81A of the ED and concur with the rationale provided in paragraph BC144/BC147 that there should be no separate recognition of the concession by the lessor as foregone revenue.

However, we do not agree with the proposal for lessors to account for finance leases at below-market terms in the same way as for finance leases at market terms. We recommend that the IPSASB reconsiders this proposal.

We understand that public sector entities in Australia and New Zealand often act in the capacity of lessor, with lessees in the private sector (e.g., NFPs). We also understand that most concessionary leases and right-of-use assets in-kind are land and/or buildings – which typically would be operating leases for the lessor. However, where the arrangement relates to a finance lease the lessor is required to derecognise the physical asset it holds and recognise a finance asset (net investment in the lease). This would result in a one-off expense to write-down the value of the asset to the value of the lease receivable asset, which may not be recognised by the lessor if it is immaterial. If the lessee uses the cost-based approach (as recommended in our response to SMC 1) it would result in the lessee recognising a right-of-use asset, which may not be recognised if it is immaterial. The consequence of this is that the underlying asset (e.g., land and/or buildings) would not be recognised by either party, which arguably is not in the public interest, assuming the premise that “what gets measured gets managed”. It is also inconsistent with the IPSASB’s desire to increase transparency and accountability.

We are of the view that the underlying asset that is the subject of a concessionary lease or in-kind arrangement is being used by the lessee in a manner that helps the lessor achieve its objectives, and thus continues to embody service potential. Therefore, it continues to satisfy the criteria for recognition as an asset by the lessor.

On this basis, we recommend that the disclosures focus more on qualitative information explaining the underlying nature of the concession and its purpose/objectives, as this may provide more value to users of such information than to place a monetary value on such arrangements. For example, qualitative information that might be useful for report users is the rationale for why the concessionary lease or right-of-use asset is provided (e.g., how it advances the entity’s own policy objectives).

**Specific Matter for Comment 3: The IPSASB decided to propose initially measuring right-of-use assets in concessionary leases (see paragraphs IPSAS 43. BC124–BC131) and right-of-use assets in-kind (see paragraphs IPSAS 23. BC28–BC30) at the present value of payments for the lease at market rates based on the current use of the underlying asset as at the commencement date of the lease. Do you agree with IPSASB’s decision? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.**

We do not agree with the market-based approach for the initial measurement of concessionary leases and right-of-use assets in-kind.

As noted in the cover letter, and similar to our views expressed in our response to the RFI, we are of the view that the costs arising from initially measuring right-of-use assets (both concessionary leases and in-kind arrangements) at the present value of payments for the lease at market rates are likely to exceed any benefits.

Feedback we have received from our members indicates that the costs of implementing IFRS 16 *Leases* in the for-profit sector have been higher than originally anticipated, and such costs are likely to be further amplified due to the complexities associated with identifying market rates for leases in the public sector.

In our view, the requirements of the right-of-use model, as it relates to concessionary leases or in-kind arrangements, are overly complex. Furthermore, the costs of applying these requirements would outweigh the benefits due to the challenges faced by the public sector, which are different from those faced by the private sector. Our reasons for this view include:

- The need for evidence-based standard-setting. We are not aware of any evidence to suggest that users want information on market rates-based information for concessionary leases or in-kind arrangements.
- The market-based approach relies on the existence of an active market in which identical and/or easily substituted assets are available and being exchanged. However, for such public sector assets:
  - an active market might not exist, and/or
  - an asset with an identical or similar remaining useful life, service potential, etc. might not be able to be identified, because such assets are usually specialised and/or have restricted use.
- It is entirely feasible that the market rate is the concessionary amount.
- The market-based approach disregards potential alternative uses for, and any other characteristics of, the asset that could maximise its market value (e.g., the asset's highest and best use).
- The sheer quantity of such arrangements in the public sector e.g., Auckland Council is lessor for 1,700 concessionary leases.
- In many instances there are no formal contractual agreements in place for such arrangements. Therefore, it is not always clear which party controls the asset, and whether the arrangement represents a lease.
- The difficulty in determining the appropriate discount rate to be used in calculating the present value. If an entity does not have borrowings/debt it would not have the inputs needed to determine the incremental borrowing rate for discounting the market-rate of the lease.
- Entities may not have the necessary financial resources to develop in house capabilities or engage external valuers.
- Recognising a large amount of "non-exchange" revenue arising from a concessionary lease or right-of-use asset in-kind in the first year, followed by a long series of subsequent depreciation/amortisation, may not help users to understand an entity's financial performance or

how it uses its resources to advance its policy objectives. The lack of clarity around the information could diminish the value of the financial reports being provided, meaning that user needs are no longer being met.

- In some jurisdictions reporting obligations are determined by thresholds based on revenue and/or assets. As a large amount of revenue would be recognised in the first year, and a significant asset, a potential unintended consequence is the imposition of higher financial reporting requirements.

### *Disclosures*

The proposed disclosures focus on the quantitative aspects of the lease arrangement and asset. The disclosure requirements do not consider the differing qualitative impacts of the lease arrangement on the lessee and lessor. Specifically, a lessee's dependency on an asset could be an indicator of possible going concern risk should the asset be withdrawn or terminated. As such, we recommend that the IPSASB also considers qualitative factors which would lead to more decision-useful information for users when considering the financial position of a lessee.

### *Subsequent measurement*

The ED does not propose any specific requirements for subsequent measurement, which suggests that the subsequent measurement requirements that are already in IPSAS 43 must be applied. This uncertainty presents a risk of divergence in practice. We consider that additional guidance is needed on how to apply the subsequent measurement requirements in IPSAS 43 to ensure they will be understood and applied consistently.

Furthermore, under IPSAS 43, part of the subsequent measurement requirements of a right-of-use asset includes adjusting for any remeasurement of the lease liability. It is not clear how this would work in practice if the right-of-use asset and lease liability have different measurement bases (i.e., the right-of-use asset is measured based on the present value of market lease payments while the lease liability is measured based on the present value of the contract lease payments).

### *Transition approach*

If the IPSASB proceeds with a market-based approach as proposed, our view is that it should be applied prospectively. In our opinion, the cost of applying the initial measurement requirements retrospectively will significantly exceed the benefits to users of the financial statements, especially when considering the cost and effort involved in obtaining information on legacy arrangements.

**Specific Matter for Comment 4: When the payments for the lease at market rates based on the current use of the underlying asset are not readily available, the IPSASB decided to propose initially measuring right-of-use assets in concessionary leases (see paragraphs IPSAS 43, BC132–BC133) at the present value of contractual payments for the lease. Do you agree with IPSASB's decision? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.**

We are of the view that right-of-use assets in concessionary leases should be measured in all circumstances at the present value of contractual payments for the lease, not just when the payments for the lease at market rates based on the current use of the underlying asset are not readily available.

We note that no guidance is proposed in the ED for determining when market rates are deemed to be not “readily available”. We also note that paragraph BC133 states that “the IPSASB expects preparers to apply a reasonable level of effort in determining the present value of lease payments at market rates based on the current use of the underlying asset”. What constitutes a “reasonable level of effort” to reach a conclusion that market rates are not readily available is highly subjective. This raises questions about the practicality of such assessment and related enforceability.

The Australian experience suggests that the cost-based approach, supplemented by disclosures about the nature and terms of the arrangement, would provide sufficient information for users about concessionary leases and right-of-use assets in-kind.