IPSAS 43 Summary—*Leases*

This summary provides an overview of IPSAS 43, *Leases*.

Project Objective: To develop a new Leases Standard aligned with IFRS 16, *Leases* to replace IPSAS 13, *Leases*.

Approved: The International Public Sector Accounting Standards Board® (IPSASB®) approved IPSAS 43, *Leases* in December 2021. It was issued in January 2022.

Project History: The IPSASB initiated the Leases project in 2016.

In January 2018, the IPSASB issued Exposure Draft (ED) 64, *Leases* proposing a single right-of-use model for lease accounting, including new public sector specific accounting requirements for leases at below market terms (also known as "concessionary leases") for both lessors and lessees.

Following constituents' feedback to ED 64 and the advice from the Consultative Advisory Group (CAG), the IPSASB decided to adopt a phased approach to the Leases project as follows:

(a) Phase One, dealing with lease accounting model(s) for both lessees and lessors based on the same definition of a lease as in IFRS 16, by issuing ED 75, *Leases* in January 2021; and

(b) Phase Two, dealing with public sector specific issues, such as concessionary leases, access rights, and other types of arrangements in the public sector, by issuing a Request for Information.

IPSAS 43 completes Phase One of the Leases project and responds to comments received to ED 75 consultation.

IPSASB

Project Overview

The purpose of Phase One of the IPSASB's Leases project is to develop a new Leases Standard aligned with IFRS 16, *Leases* to replace IPSAS 13, *Leases*.

Why the IPSASB Undertook this project

IPSAS 13, *Leases* was drawn primarily from International Accounting Standard (IAS) 17, *Leases*, issued by the International Accounting Standards Board (IASB). In January 2016, the IASB issued International Financial Reporting Standard (IFRS) 16, *Leases*. IFRS 16 replaces IAS 17 and several related interpretations.

After consultation with constituents, the IPSASB decided to revise its leasing requirements. The IPSASB also decided to consider public sector issues, including concessionary leases, which are prevalent in the public sector.

IPSAS 43 Enhancements to Lease Accounting

The risks and reward incidental to ownership model in IPSAS 13 required lessees and lessors to classify leases as either finance leases or operating leases. Operating leases did not require lessees to recognize assets and liabilities, while finance leases did.

Furthermore, the IPSAS 13 requirements for lessors did not provide adequate information about a lessor's exposure to credit risk (arising from a lease) and exposure to asset risk (arising from the lessor's retained interest in the underlying asset).

IPSAS 43 enhances the accounting for leases by lessees because:

(a) No longer requires the classification of leases as either finance leases or operating leases; and

(b) Requires the recognition of assets and liabilities related to the rights and obligations created by leases.

Benefits of IPSAS 43

The enhancements introduced to lease accounting in IPSAS 43 have the following benefits:

(a) Increased transparency related to assets and liabilities that arise from lease contracts because lessees are required to recognize them for all leases;

(b) Eliminates information asymmetry because users no longer need to adjust the financial statements using different techniques; and

(c) Increased comparability between financial statements of lessees that buy assets from those that lease assets.

What Are the Changes to Lessee Accounting?

IPSAS 43 introduces the right-of-use model for lessees, which distinguishes the right to use an underlying asset (which the lessee controls) and the underlying asset itself (which the lessee does not control).

Recognition and Measurement of Leases—General Guidance

IPSAS 43 requires that lessees recognize:

(a) A right-of-use asset because they control the right to use the underlying asset, compared with IPSAS 13, where the lessee recognizes the underlying asset when the lease is classified as a finance lease, but not when it is classified as an operating lease.

(b) A lease liability because they have a present obligation to make future lease payments in accordance with the lease contract (once the underlying asset has been made available, and the lessee has the right to use it). Under IPSAS 13, a lease liability is not recognized when the lessee classifies the lease as operating lease.

IPSAS 43 requires measuring the right-of-use asset and the lease liability at cost (the present value of the future lease payments).

Recognition Exemptions

Lessees can elect not to apply the general guidance for leases, as IPSAS 43 includes two recognition exemptions for:

(a) Short-term leases; and

(b) Leases for which the underlying asset is of low value.

IPSAS 43 requires that leases, which qualify for the recognition exemptions, be accounted for consistent with how operating leases are treated in IPSAS 13 (expenses recognized on a straight-line basis over the lease term or another systematic basis). IPSAS 13 does not provide recognition exemptions.

What Are the Changes for Lessor Accounting?

IPSAS 43 substantially carries forward the lessor accounting in IPSAS 13.

However, IPSAS 43 also provides additional guidance and clarifications to help with applying the risks and rewards model incidental to ownership.

Risks and Rewards Incidental to Ownership Model Substantially Carried Forward

IPSAS 43 substantially carries forward the lessor accounting in IPSAS 13. However, IPSAS 43 includes specific changes to the model for consistency with the lessee accounting model.

Lease Modifications

IPSAS 43 requires accounting for a modification to a finance lease as a separate lease if:

(a) The modification increases the scope of the lease by adding the right for the lessee to use one or more underlying assets; and

(b) The consideration received for the lease increases by an amount commensurate with the stand-alone price for the increase in scope.

IPSAS 43 requires accounting for a modification to an operating lease as a new lease from the effective date of the modification, considering any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease.

IPSAS 13 does not include specific requirements relating to lease modifications.

Subleases

IPSAS 43 requires the intermediate lessor classify subleases by reference to the right-of-use assets arising from the head lease and not by reference to the underlying asset, which differs from the current requirements in IPSAS 13.

Disclosures

IPSAS 43 includes enhanced disclosures to better evaluate the amount, timing and uncertainty of cash flows arising from a lessor’s leasing activities, such as:

(a) Table of income;

(b) Information about residual asset risk;

(c) Information about assets subject to operating leases;

(d) Maturity analysis; and

(e) Changes in net investment in finance leases.

IPSASB

What Are the Changes for Sale and Leaseback Transactions?

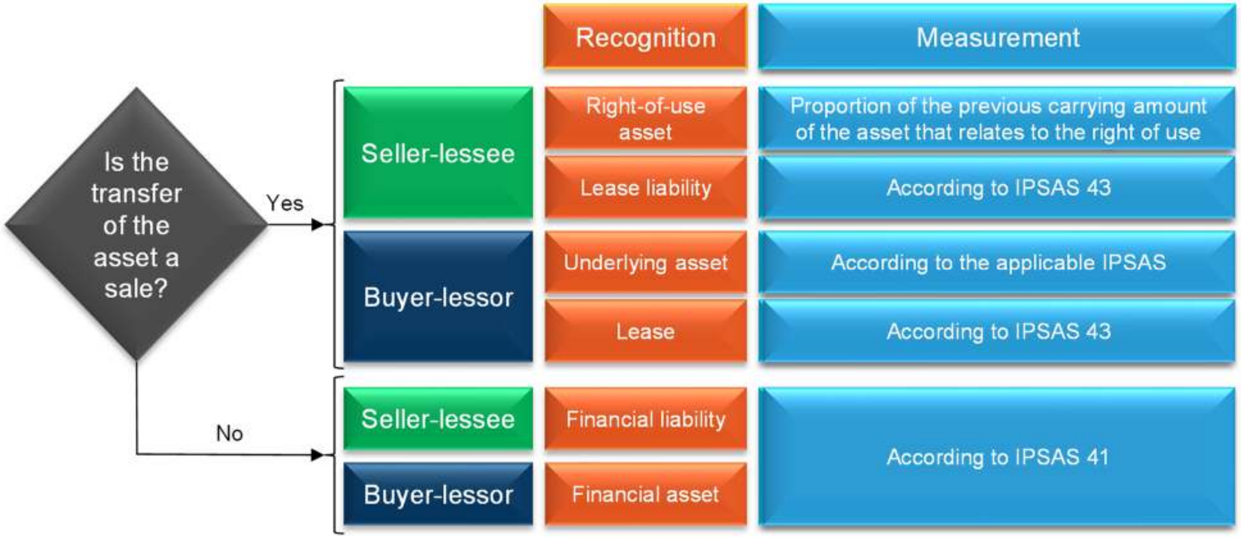
IPSAS 43 requires recognizing right-of-use assets and its related lease liabilities for all sale and leaseback transactions.

Less Opportunity for ‘Off-Balance Sheet’ Accounting

IPSAS 13 provides an opportunity for an entity to report fewer assets and less debt by selling its assets and leasing those assets back through operating leases. However, in substance the entity has neither changed its operations nor the use of the assets that it leased back.

IPSAS 43 requires recognizing the rights to use those same assets and related liabilities for all sale and leaseback transactions and restricts the amount of any gain recognized on the sale of an asset.

As a result, IPSAS 43 provide less opportunity for entities to enter into sale and leaseback transactions and more comparability of financial information reported in the statement of financial position between entities that lease assets and entities that buy assets.



What Other Changes Does IPSAS 43 Include?

IPSAS 43 includes additional guidance in several areas of lease accounting.

Definition of a Lease

IPSAS 43 includes a definition of a lease that is consistent with IPSAS 13. However, IPSAS 43 changes the guidance on how to apply the definition. The changes are based on the concept of control within the definition of a lease.

Identifying a Lease

IPSAS 43 includes guidance to help in determining whether a contract conveys the right to control the use of an identified asset over a period of time. The proposed guidance requires an entity to assess whether, throughout the period of use, the customer has both of the following:

(a) The right to obtain substantially all of the economic benefits or service potential from use of the identified asset; and

(b) The right to direct the use of the identified asset.

The IPSASB decided to refer to both "economic benefits" and "service potential" when identifying a lease because it is consistent with *The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* in referring to assets in terms of both economic benefits and service potential.

Combination of Contracts

IPSAS 43 requires that an entity shall combine two or more contracts entered into at or near the same time with the same counterparty (or related parties of the counterparty), and account for the contracts as a single contract if one or more of the following criteria are met:

(a) The contracts are negotiated as a package with an overall commercial objective that cannot be understood without considering the contracts together;

(b) The amount of consideration to be paid in one contract depends on the price or performance of the other contract; or

(c) The rights to use underlying assets conveyed in the contracts (or some rights to use underlying assets conveyed in each of the contracts) form a single lease component.

Variable Lease Payments

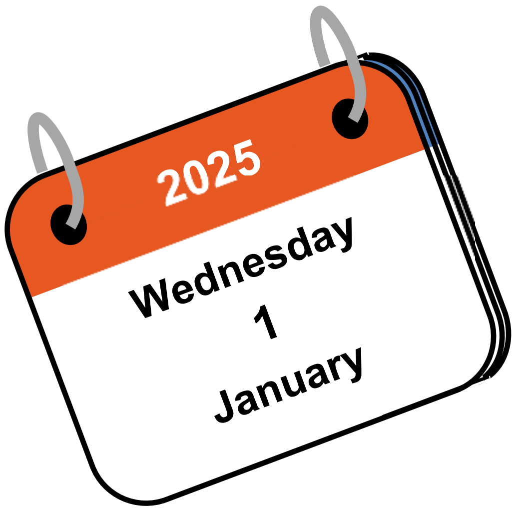
IPSAS 43 requires measuring of lease liabilities including variable lease payments, such as:

(a) In-substance fixed lease payments; and

(b) Those that depend on an index or a rate.

Effective Date and Project History

The effective date of IPSAS 43 is January 1, 2025.



Effective Date

The effective date of IPSAS 43 is January 1, 2025, with earlier application permitted for entities that apply IPSAS 41, *Financial Instruments* at or before the date of initial application of this Standard.

The IPSASB selected this effective date because:

(a) IFRS 16 also had a three-year period for its application;

(b) It allows public sector entities sufficient time to apply IPSAS 43, after applying IPSAS 41, *Financial Instruments* on or before January 1, 2023;

(c) It allows preparers sufficient time to fully evaluate the implications of applying IPSAS 43, after implementing IPSAS 41, *Financial Instruments* on or before on January 1, 2023;

(d) It allows the IPSASB time to finalize other IPSAS under development, including Revenue, which may have consequential amendments to IPSAS 43;

(e) It allows the IPSASB time to finish Phase Two of the Leases project; and

(f) It allows public sector entities time to identify the impacts of and to prepare for the implementation of the new Leases Standard.

Project History

To learn more about the project history, and to view the consultation documents and responses, please visit:

https://www.ipsasb.org/consultations-projects/leases