Leases and IFRIC discussions

Introduction

This accounting update covers

- Technical IFRS
  - Lease accounting
  - July 2016 IFRIC update
- Business and accounting
  - The relationship between accountancy expertise and business performance

Lease accounting – IFRS 16

The IASB issued IFRS 16 *Leases* in January 2016 with an effective date from 1 January 2019. Earlier application is allowed provided that IFRS 15 *Revenue from Contracts with Customers* has already been adopted. IFRS 16 replaces IAS 17 *Leases* and related interpretations.

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract i.e. lessee and lessor.

Significant changes:

Lease definition	Contract that conveys the right to the customer ("lessee") to use an asset for a period of time in exchange for consideration. A company assesses whether a contract contains a lease on the basis of whether the customer has the right to control the use of an identified asset for a period of time.
Impact on lessees	No distinction between a finance lease and operating lease
	- All leases must now be capitalised, similar to the treatment of finance lease under IAS 17
	- Leases are capitalised by recognising the present value of lease payments either as a right-to-use asset or as part of property, plant and equipment with a corresponding liability for payments to be made in accordance with the lease contract
	- Instead of recognising operating lease payments as an expense in the income statement, all leases will now result in a depreciation/amortisation charge as well as interest paid

The full standard can be accessed here. Also see the very useful IASB Effects Analysis which includes a summary of changes and describes the likely costs and benefits of IFRS 16.

Note: the IFRS Foundation offers free access to the current year's consolidated unaccompanied English language Standards and official Interpretations (this includes IFRS, IAS*, IFRIC and SIC*). 'Unaccompanied' means without the Implementation Guidance and the Basis for Conclusions. You need to be an eIFRS Basic, Professional or Comprehensive user to access the unaccompanied Standards. You can however access the Standards with a subscription to the PKF / Wiley InSight IFRS research service available from PKF International.

IFRIC – discussions and decisions

The Interpretations Committee met in London on 12 July 2016 to discuss the following issues:

IAS 21 *The Effects of Changes in Foreign Exchange Rates – Foreign currency transactions and advance consideration*

The Interpretations Committee completed its discussion of the more significant matters raised in comment letters to the draft Interpretation *Foreign Currency Transactions and Advance Consideration*, and reviewed the due process steps taken in the development of the Interpretation.

The following decisions were tentatively agreed on by the Committee:

1. The effective date of the Interpretation should be 1 January 2018, with earlier application permitted;
2. First-time adopters should be permitted to apply the Interpretation prospectively to all assets, expenses and income initially recognised on or after the date of transition to IFRS

IAS 19 *Employee Benefits* and IFRIC 14 *IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* – Comment letter summary of proposed amendments

The committee discussed the summary on the feedback received on the Exposure Draft *Remeasurement on a Plan Amendment, Curtailment or Settlement/Availability of a Refund from a Defined Benefit Plan*.

No decisions were made.

IAS 12 *Income Taxes* – Uncertainty over Income Tax Treatments – Comment letter summary

The Committee discussed a summary of the feedback received on the Exposure Draft *Uncertainty over Income Tax Treatments.*

No decisions were made.

IFRS 11 *Joint Arrangements* and IFRS 10 *Consolidated Financial Statements* – Accounting for loss of control IAS 21 *The Effects of Changes in Foreign Exchange Rates* – Foreign currency transactions and advance consideration

The Committee discussed whether an entity should remeasure its retained interest in the assets and liabilities of a joint operation when the entity loses control of a business, or an asset or group of assets that is not a business. In the transaction discussed, the entity either retains joint control of a joint operation or is a party to a joint operation (with rights to assets and obligations for liabilities) after the transaction.

As the Board already issued amendments to IFRS 10 and IAS 28 Investments in Associates and Joint Ventures to address the accounting for the sale or contribution of assets to an associate or a joint venture, which address a similar conflict that exists between the requirements in IFRS 11 and IAS 28, the Committee decided that the accounting for the two transactions should be considered concurrently by the Board given the similarity between the transactions. The item has not been added to the agenda.

IFRIC 12 *Service Concession Arrangements* – Payments made by an operator to a grantor in a service concession arrangement

Clarification was requested as to how an operator accounts for payments it makes to a grantor in a service concession arrangement within the scope of IFRIC 12. The following decisions were made in the cases where the operator was not collecting amounts on behalf of, and remitting them to, the grantor:

If payments are for a right to a good or service that is separate from the service concession arrangement	Account for those payments by applying the applicable IFRS standard
If payments are for the right to use an asset that is separate from the infrastructure within the scope of IFRIC 12	Consider whether the arrangement contains a lease. If it does, apply IFRS 16 (IAS 17) *Leases*
If payments are not for the right to a separate good or service or a separate right-to-use asset that is a lease	- If the service concession arrangement results in the operator having only a contractual right to receive cash from the grantor, the operator accounts for those payments as a reduction of the transaction price, applying IFRS 15 *Revenue from Contracts with Customers* - If the service concession arrangement results in the operator having only a right to charge users of the public service, the operator has received an intangible asset and should apply the principles of IAS 38 *Intangible Assets* - If the operator has both a right to charge users of the public service and a contractual right to receive cash from the grantor, the operator must consider whether those payments represent payments for the intangible asset or consideration payable to a customer, or both.

For the full deliberations on the above matters please see the IFRS Interpretations Committee Activities on the IFRS Foundation website.

The relationship between accountancy expertise and business performance

Commissioned by IFAC, researchers at the Bucharest University of Economic Studies conducted a literature review to assess the relationship between accountancy expertise and business performance. The IFAC report summarises and discusses the findings of more than 90 academic research papers and relevant publications covering literature from around the world that investigates this relationship for small and medium-sized entities (SMEs) as well as large entities.

The full report can be accessed here.

SME owners can review performance as a mix of financial and non-financial expectations; this is due to the fact that they may measure their performance in terms of profitability and growth, but also image and work-life balance. Prior studies indicate that accountancy expertise, generally analysed as the accounting or business advice accessed by SMEs, is associated with better performance. Research has also implied that advice in non-traditional areas such as human resources, environmental issues, and business and management support are most likely to impact SME performance.

Key findings: Small and Medium-sized Entities

- Growing SMEs make the most use of external advice
- Advisory services have a positive impact on start-ups
- Enterprises using an external accountant saw an 8.1% average increase in sales growth and a 29% decrease in the likelihood of failure
- Companies using accounting services saw growth in employees, assets and turnover/revenue
- More than 50% of SMEs with no written budgets saw sales decrease while 75% of SMEs with detailed budgets saw sales increase
- Under the guidance of an external advisor, adopting environmentally-friendly practices internally leads to organisational, financial and human capital benefits

Large entities make use of accountancy expertise, both internal and external, in different ways to some of their SME counterparts. Business performance appears to improve in those enterprises where the accounting function takes a greater strategic role as a business partner and advisor.

Key findings: Large entities

- The professional identity of management accountants is evolving with roles relating to business integrator, business partner/advisor, change agent and decision enabler. Management accountants also contribute to cost efficiency and value creation
- Main functions of management accounting are:
  a) Providing information on results and part performance
  b) Facilitating decision making
  c) Directing staff behavior
- Companies with CFOs focused on risk management and decision support and "transformed" accounting functions to perform better
- High-performance businesses are more likely to report high levels of satisfaction with their finance function and have CFOs with higher strategic influence

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