

PSAK 73 - Leases

A new era for lease accounting



At a glance

In 2017 the Indonesian Financial Accounting Standards Board (DSAK-IAI) issued PSAK 73, 'Leases', and thereby started a new era of lease accounting for lessees. Whereas, under the previous guidance in PSAK 30, Leases, a lessee had to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet), the new model requires the lessee to recognise almost all lease contracts on the balance sheet; the only optional exemptions are for certain short-term leases and leases of low-value assets. For lessees that have entered into contracts classified as operating leases under PSAK 30, this could have a huge impact on the financial statements.

At first, the new standard will affect balance sheet and balance sheet-related ratios such as the debt/equity ratio. Aside from this, PSAK 73 will also influence the income statement, because an entity now has to recognise interest expense on lease liabilities (obligations to make lease payments) and depreciation on 'right-of-use' assets (assets that reflects the right to use the leased asset). As a result, for lease contracts previously classified as operating leases the total amount of expenses at the beginning of the lease period will be higher than under PSAK 30. Another consequence of the changes in presentation is that EBIT and EBITDA will be higher for companies that have material operating leases.

The new guidance will also change the cash-flow statement. Lease payments that relate to contracts that have previously been classified as operating leases are no longer presented as operating cash flows in full. Only the part of the lease payments that reflects interest on the lease liability can be presented as an operating cash flow (depending on the entity's accounting policy regarding interest payments). Cash payments for the principal portion of the lease liability are classified within financing activities. Payments for short-term leases, leases of low-value assets and variable lease payments not included in the measurement of the lease liability remain presented within operating activities.

Although accounting remains substantially the same for lessors, the changes made by the new standard are still relevant. In particular, lessors should be aware of the new guidance on the definition of a lease, subleases and the accounting for sale and leaseback transactions. The changes in lessee accounting might also have an impact on lessors as lessee's needs and behaviours change and they enter into negotiations with their customers.

For both, lessees and lessors PSAK 73 adds significant new, enhanced disclosure requirements.

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Scope

PSAK 73 will apply to all lease contracts except for:

- leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources;
- leases of biological assets within the scope of PSAK 69, Agriculture, held by lessees;
- service concession arrangements within the scope of ISAK 16, Service Concession Arrangements;
- licences of intellectual property granted by a lessor within the scope of PSAK 72, Revenue from Contracts with Customers; and
- rights held by a lessee under licensing agreements within the scope of PSAK 19, Intangible Assets, for items such as motion-picture films, video recordings, plays, manuscripts, patents and copyrights.

Aside from this, a lessee may choose to apply PSAK 73 to leases of intangible assets other than those mentioned above.

Identifying a lease

Definition of a lease

PSAK 73 defines a lease as a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for a consideration. At first sight, the definition looks straightforward. But, in practice, it can be challenging to assess whether a contract conveys the right to use an asset or is, instead, a contract for a service that is provided using the asset.

For example, an entity might want to transport a specified quantity of goods, in accordance with a stated timetable, for a period of five years from A to B by rail. To achieve this, it could either rent a number of rail cars or it could contract to buy the transport service from a freight carrier. In both cases, the goods will arrive at B – but the accounting might be quite different.

PwC Observation:

In future, there is likely to be a greater focus on identifying whether a contract is or contains a lease, given that all leases (except short-term leases and leases of low-value assets) will be recognised on the balance sheet of the lessee.

Currently, many companies that have contracts which include both an operating lease and a service do not separate the operating lease component. This is because the accounting for an operating lease and a service or supply arrangement is the same (that is, there is no recognition on the balance sheet and straight-line expense is recognised in profit or loss over the contract period).

Under the new standard, the treatment of the two components will differ. A lessee may decide as a practical expedient not to separate non-lease components (services) from lease components, by class of underlying asset. If the lessee decides to apply this exemption each lease component and any associated non-lease component is accounted for as a single lease component. So the service component will either be separated or the entire contract will be treated as a lease.

Leases are different from service contracts: a lease provides a customer with the right to control the use of an asset, whereas, in a service contract, the supplier retains control.

PSAK 73 states that a contract contains a lease if:

- there is an identified asset; and
- the contract conveys the right to control the use of the identified asset for a period of time in exchange for consideration.

What is an identified asset?

An asset can be identified either explicitly or implicitly. If explicitly, the asset is specified in the contract (for example, by a serial number or a similar identification marking); if implicitly, the asset is not mentioned in the contract (so the entity cannot identify the particular asset) but the supplier can fulfil the contract only by the use of a particular asset. In both cases there may be an identified asset.

In any case, there is no identified asset if the supplier has a substantive right to substitute the asset. Substitution rights are substantive where the supplier has the practical ability to substitute an alternative asset and would benefit economically from substituting the asset.

The term 'benefit' is interpreted broadly. For example, the fact that the supplier could deploy a pool of assets more efficiently, by substituting the leased asset from time to time, might create a sufficient benefit as long as there are no significant costs. It is important to note that 'significant' is assessed with reference to the related benefits (that is, costs must be lower than benefits, it is not sufficient if the costs are low or not material to the entity as a whole). Significant costs could occur, in particular, if the underlying asset is tailored for use by the customer. For example, a leased aircraft might have specific interior and exterior specifications defined by the customer. In such a scenario, substituting the aircraft throughout the lease term could create significant costs that would discourage the supplier from doing so.

The assessment whether a substitution right is substantive depends on the facts and circumstances at inception of the contract and does not take into account circumstances that are not considered likely to occur.

A right to substitute an asset if it is not operating properly, or if there is a technical update required, does not prevent the contract from being dependent on an identified asset. The same is true for a supplier's right or obligation to substitute an underlying asset for any reason on or after a particular date or on the occurrence of a specified event because the supplier does not have the practical ability to substitute alternative assets throughout the period of use.

If the customer cannot readily determine whether the supplier has a substantive substitution right, it is presumed that the right is not substantive (that is, that the contract depends on an identified asset).

Portion of an asset

An identified asset can be a physically distinct portion of a larger asset, such as one floor of a multi-level building or physically distinct dark fibres within a cable.

A capacity portion (that is, a portion of a larger asset that is not physically distinct) is not an identified asset unless it represents substantially all of the capacity of the entire asset. So, for example, a capacity portion of a fibre-optic cable that does not represent substantially all of the capacity of the cable would not qualify as an identified asset.

When does the customer have the right to control the use of an identified asset?

A contract conveys the right to control the use of an identified asset if the customer has both the right to obtain substantially all of the economic benefits from the use of the identified asset and the right to direct the use of the identified asset throughout the period of use.

Substantially all of the economic benefits from use of the asset throughout the period of use

Economic benefits can be obtained directly or indirectly (for example, by using, holding or subleasing the asset). Benefits include the primary output and any by-products (including potential cash flows derived from these items), as well as payments from third parties that relate to the use of the identified asset. Economic benefits relating to the ownership of the asset are ignored.

The example below illustrates under which circumstances payments from third parties should be taken into account:

Example:

A customer rents a solar farm from the supplier. The supplier receives tax credits relating to the ownership of the solar farm, whereas the customer receives renewable energy credits from the use of the farm.

In this scenario, only the renewable energy credits are taken into account in the analysis, because the tax credits relate not to the use of the solar farm but, instead, to ownership of the asset.

Right to direct the use of an asset throughout the period of use

When assessing whether the customer has the right to direct the use of the identified asset, the key question is which party (that is, the customer or the supplier) has the right to direct how and for what purpose the identified asset is used throughout the period of use.

The standard gives several examples of relevant decision-making rights:

- Right to change what type of output is produced.
- Right to change when the output is produced.
- Right to change where the output is produced.
- Right to change how much of the output is produced.

The relevance of each of the decision-making rights depends on the underlying asset being considered. If both parties have decision-making rights, an entity considers the rights that are most relevant to changing how and for what purpose the asset is used. Decision-making rights are relevant when they affect the economic benefits to be derived from the use of the asset.

To illustrate the concept, the table below provides some questions to consider when evaluating which party has the relevant decision-making rights:

	Which party decides...
Lease of truck/aircraft/ rail cars etc.	Which goods are transported? When the goods are transported and to where? How often the asset is used? How full it needs to be run? Which route is taken?
Fibre-optic cable	When and whether to light the fibres? When and how much data the cable will transport? How to run the cable? Through which routes the data will be delivered?
Retail unit	Which goods will be sold? The prices at which the goods will be sold? Where and how the goods are displayed?
Power plant	How much power will be delivered and when? When to turn the power plant on and off?

However, there are several rights that are not taken into account:

- **Protective rights:** In many cases, a supplier might limit the use of an asset by a customer in order to protect its personnel or to ensure compliance with relevant laws and regulations (for example, a customer who has hired a ship is prevented from sailing the ship into waters with a high risk of piracy or transporting hazardous materials). These protective rights do not affect the assessment of which party to the contract has the right to direct the use of the identified asset.
- **Maintaining/operating the asset:** Decisions about maintaining and operating an asset do not grant the right to direct the use of the asset. They are only taken into account if the decisions about how and for what purpose the asset is used are predetermined (see below).
- **Decisions made before the period of use:** Decisions made before the period of use are not taken into account unless they are made in the context of the design of the asset by a customer (see below).

In some scenarios, the decisions about how and for what purpose the underlying asset is used are already predetermined before the inception of the lease. If this is the case, the customer has the right to direct the use of an asset if it either:

- has the right to operate the identified asset throughout the period of use without the supplier having the right to change those operating instructions, or
- has designed the identified asset (or specific aspects of the asset) in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

PwC Observation:

The new concept of “pre-determined” introduced by PSAK 73 can be very complex and judgmental where decisions are made before the inception of the lease. When analysing these decisions, there are several questions to be considered, such as:

- Do any decisions that are not predetermined have a significant effect on how and for what purpose the asset is used?
- How predetermined are decisions about how and for what purpose the asset is used?
- Do the decisions predetermine how and for what purpose the identified asset is used or do they only establish protective rights?
- Which party to the contract has made the decisions?

Sometimes, an identified asset is incidental to a service but has no specific use to the customer by itself. In these cases, the customer often does not have the right to direct the use of the asset.

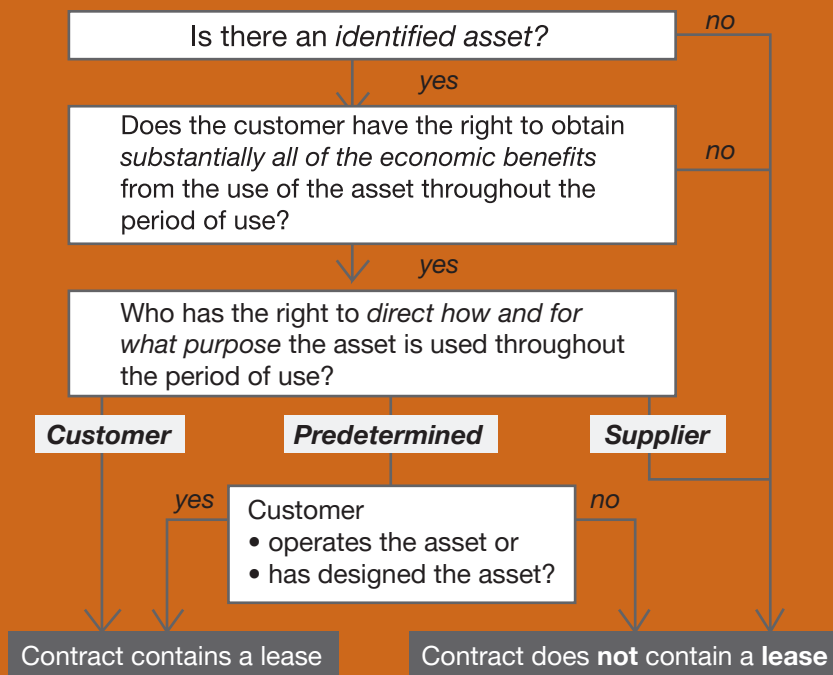
Example:

- A customer enters into a contract with a telecommunications company for network services. To supply the services, it is necessary to install a server at the customer’s premises. The supplier can reconfigure or replace the server, when needed, to provide the network services continuously; the customer does not operate the server, nor does it make any significant decisions about its use. The telecommunication company determines the speed and the quality of data transportation in the network using the servers.
- The telecommunication company has the right to control the use of the server because it makes all the relevant decisions about the use of the server throughout the period of use. It decides how the data is transported, whether to reconfigure the servers and whether to use the servers for another purpose. The customer only decides about the level of network services (that is the output of the servers) before the period of use.
- This arrangement, therefore, does not contain a lease.

Summary overview

The flowchart below summarises the analysis to be made to evaluate whether a contract contains a lease:

Determining whether a contract contains a lease



PwC Observation:

The definition of a lease is now much more driven by the question of which party to the contract controls the use of the underlying asset for the period of use. A customer no longer needs only to have the right to obtain substantially all of the benefits from the use of an asset ('benefits' element), but must also have the ability to direct the use of the asset ('power' element).

This conceptual change becomes obvious when looking at a contract to purchase substantially all of the output produced by an identified asset (for example, a power plant). If the price per unit of output is neither fixed nor equal to the current market price, the contract would be classified as a lease under PSAK 30 and ISAK 8, Determining Whether an Arrangement Contains a Lease.

PSAK 73, however, requires not only that the customer obtains substantially all of the economic benefits from the use of the asset but also an additional 'power' element, namely the right of the customer to direct the use of the identified asset (for example, the right to decide the amount and timing of power delivered).

Comprehensive example

A customer enters into a contract that conveys the right to use an explicitly specified retail unit for a period of five years. The property owner can require the customer to move into another retail unit; there are several retail units of similar quality and specification available.

As the property owner has to pay for any relocation costs it can benefit economically from relocating the customer only if there is a new tenant that wants to occupy a large amount of retail space at a rate that is sufficient to cover the relocation costs. Those circumstances may arise, but they are not considered likely to occur.

The contract requires the customer to sell his goods during the opening hours of the larger retail space. The customer decides on the mix of goods sold, the pricing of the goods sold and the quantities of inventory held. He further controls physical access to the retail unit throughout the five-year period of use.

The rent that the customer has to pay includes a fixed amount plus a percentage of the sales from the retail unit.

Is there an identified asset ?

The retail unit is explicitly specified in the contract. The property owner has a right to substitute the asset. But, because it would benefit from the exercise of the right only under certain circumstances that are not considered likely to occur, the substitution right is not substantive.

Hence, the retail unit is an identified asset.

Does the customer have the right to direct the use of the retail ?

During the period of use, all decisions on how and for what purpose the retail unit is used are made by the customer. The restriction that goods can only be sold during the opening hours of the larger retail space defines the scope of the contract, but it does not limit the customer's right to direct the use of the retail unit

Conclusion

The contract contains a lease of retail space.

Separating components of a contract

Contracts often combine different kinds of obligations of the supplier, which might be a combination of lease components or a combination of lease and non-lease components. For example, the lease of an industrial area might contain the lease of land, buildings and equipment, or a contract for a car lease might be combined with maintenance.

Where such a multi-element arrangement exists, PSAK 73 requires each separate lease component to be identified (based on the guidance on the definition of a lease) and accounted for separately.

The right to use an asset is a separate lease component if both of the following criteria are met:

- the lessee can benefit from use of the asset either on its own or together with other resources that are readily available to the lessee; and
- the underlying asset is neither highly dependent on, nor highly interrelated with, the other underlying assets in the contract.

PwC Observation:

PSAK 72 contains guidance on how to evaluate whether a good or service promised to a customer is distinct for lessors. The question arises of how PSAK 73 interacts with PSAK 72.

For a multi-element arrangement that contains (or might contain) a lease, the lessor has to perform the assessment as follows:

1. Apply the guidance in PSAK 73 to assess whether the contract contains one or more lease components.
2. Apply the guidance in PSAK 73 to assess whether different lease components have to be accounted for separately.
3. After identifying the lease components under PSAK 73, the non-lease components should be assessed under PSAK 72 for separate performance obligations.

The criteria in PSAK 73 for the separation of lease components are similar to the criteria in PSAK 72 for analysing whether a good or service promised to a customer is distinct

Separating components of a contract

If the analysis concludes that there are separate lease and non-lease components, the consideration must be allocated between the components as follows:

- Lessee: The lessee allocates the consideration on the basis of relative stand-alone prices. If observable stand-alone prices are not readily available, the lessee shall estimate the prices, and should maximise the use of observable information.
- Lessor: The lessor allocates the consideration in accordance with PSAK 72 (that is, on the basis of relative stand-alone selling prices).

As a practical expedient, lessees are allowed to choose not to separate lease and non-lease components and, instead, account for each lease component and any associated non-lease components as a single lease component. This accounting policy choice has to be made by class of underlying asset. Because not separating a non-lease component would increase the lessee's lease liability, it is expected that a lessee will use this exemption only if the service component is not significant.

Combination of contracts

Often, several contracts with the same counterparty are entered into at or near the same time and in contemplation of another. PSAK 73 requires an entity to combine contracts entered into at or near the same time with the same counterparty (or related parties of the counterparty) before assessing whether they contain a lease and account for them as a single contract if one or more of the following conditions are met:

- the contracts are negotiated as a package with an overall commercial objective;
- the consideration in one contract depends on the price/performance of the other contract; or
- the assets involved are a single lease component.

Lease term

Similar to PSAK 30, the new standard defines the lease term as the non-cancellable period of the lease plus periods covered by an option to extend or an option to terminate if the lessee is reasonably certain to exercise the extension option or not exercise the termination option.

- The interpretation of the term 'reasonably certain' has been a source of long and controversial discussions, under PSAK 30, and led to diversity in practice. To address this, the standard states the principle that all facts and circumstances creating an economic incentive for the lessee to exercise the option must be considered, and provides some examples of such factors:
- Contractual terms and conditions for optional periods compared with market rates: It is more likely that a lessee will not exercise an extension option if lease payments exceed market rates. Other examples of terms that should be taken into account are termination penalties or residual value guarantees.
- Significant leasehold improvements undertaken (or expected to be undertaken): It is more likely that a lessee will exercise an extension option if a lessee has made significant investments to improve the leased asset or to tailor it for its special needs.
- Costs relating to the termination of the lease or the signing of a replacement lease: It is more likely that a lessee will exercise an extension option if doing so avoids costs such as negotiation costs, relocation costs, costs of identifying another suitable asset, costs of integrating a new asset and costs of returning the original asset in a contractually specified condition or to a contractually specified location.
- The importance of the underlying asset to the lessee's operations: It is more likely that a lessee will exercise an extension option if the underlying asset is specialised or if suitable alternatives are not available.
- If an option is combined with one or more other features such as for example a residual value guarantee with the effect that the cash return for the lessor is the same regardless of whether the option is exercised an entity will assume that the lessee is reasonably certain to exercise the option to extend the lease, or not to exercise the option to terminate the lease.

When the option can only be exercised if one or more conditions are met the likelihood that those conditions will exist should also be taken into account.

Aside from this, a lessee's past practice regarding the period over which it has typically used particular types of assets, and its economic reasons for doing so, may also provide helpful information.

PwC Observation:

One of the primary reasons for including extension options (and not limiting the accounting to the non-cancellable lease term) is to avoid the potential for structuring opportunities. For example, one could theoretically structure a 20-year lease as a daily lease with 20 years' worth of daily renewals.

There is no guidance in the standard on how to weight the individual factors when determining whether it is 'reasonably certain' that a lessee will exercise an option. For example, consider a flagship store that in a prime and much sought-after location. Significant judgement would be needed to determine whether the prime geographical location of the store or other factors (for example termination penalties, lease hold improvements, etc.) indicate that it is reasonably certain whether or not the lessee will renew the store lease.

Often, The assessment of whether the exercise of an option is reasonably certain is made at the commencement date (that is, the date on which the lessor makes the underlying asset available for use).

The lease term is only reassessed in limited circumstances:

- where the lessee exercises or does not exercise an option in a different way than the entity had previously determined was reasonably certain;
- where an event occurs that contractually obliges the lessee to exercise an option (prohibits the lessee from exercising an option) not previously included in the determination of the lease term (previously included in the determination of the lease term); or
- where a significant event or change in circumstances occurs that is within the control of the lessee and affects whether it is reasonably certain to exercise an option. This trigger is only relevant for the lessee (and not the lessor).

Example

An entity leases a building for a ten-year period, with the option to extend for five years. At the commencement date, the entity concludes that it is not reasonably certain that it will exercise the extension option. It determines the lease term to be ten years. After using the building for five years, the entity decides to sublease the building to another party, and it enters into a sublease contract with a term of ten years.

Entering into a sublease is a significant event that is within the control of the lessee, and it affects the entity's assessment of whether it is reasonably certain to exercise the extension option. Accordingly, the lessee has to reassess the lease term of the head lease upon the occurrence of the significant event.

This requirement can be seen as a compromise: on the one hand, the DSAK-IAI believes that a regular reassessment of the lease term would provide more relevant information to users of the financial statements; on the other hand, the Board acknowledges that such a requirement could be very costly.

Accordingly, an approach similar to the one for impairment testing is developed – a reassessment is only made if there are indicators that it would result in a different outcome.

Recognition and measurement exemptions

The standard contains two recognition and measurement exemptions. Both exemptions are optional and only apply to lessees. If one of these exemptions is applied, the leases are accounted for in a way that is similar to current operating lease accounting (that is, payments are recognised on a straight-line basis or another systematic basis that is more representative of the pattern of the lessee's benefit):

- **Short-term leases:** Short-term leases are defined as leases with a lease term of 12 months or less. The lease term also includes periods covered by an option to extend or an option to terminate if the lessee is reasonably certain to exercise the extension option or not exercise the termination option. A lease that contains a purchase option is not a short-term lease. If a lessee elects this exemption, it has to be made by class of underlying asset. If an entity applies the short-term lease exemption it shall treat any subsequent modification or change in lease term as resulting in a new lease.
- **Leases for which the underlying asset is of low value:** The standard does not define the term 'low value'. Examples of assets of low value are IT equipment or office furniture. For certain assets (such as assets that are dependent on, or highly interrelated with, other underlying assets), the exemption is not applicable.

The election can be made on a lease-by-lease basis. It is important to note that the analysis does not take into account whether low-value assets are material in aggregate. Accordingly, although the aggregated value of the assets captured by the exemption may be material the exemption is still available.

PSAK 73 also clarifies that both a lessee and a lessor can apply the standard to a portfolio of leases with similar characteristics if the entity reasonably expects that the resulting effect is not materially different from applying the standard on a lease-by-lease basis.

Lessee accounting

Initial recognition and measurement

The new lessee accounting model within PSAK 73 is the most important change to current guidance.

Under PSAK 73, lessees will no longer distinguish between finance-lease contracts (on balance sheet) and operating-lease contracts (off balance sheet), but they are required to recognise a right-of-use asset and a corresponding lease liability for almost all lease contracts. This is based on the principle that, in economic terms, a lease contract is the acquisition of a right to use an underlying asset with the purchase price paid in instalments.

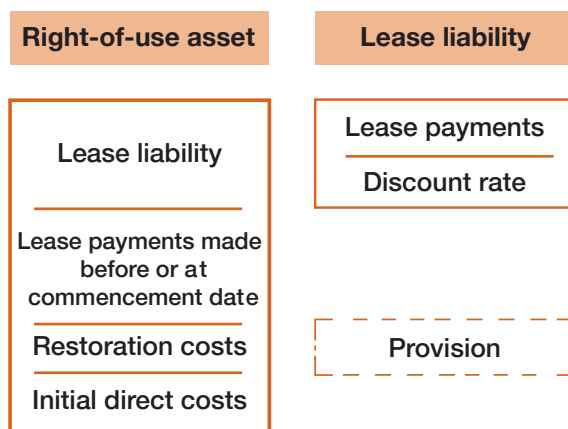
The effect of this approach is a substantial increase in the amount of recognised financial liabilities and assets for entities that have entered into significant lease contracts that are currently classified as operating leases.

The lease liability is initially recognised at the commencement day and measured at

an amount equal to the present value of the lease payments during the lease term that are not yet paid; the right-of-use asset is initially recognised at the commencement

day and measured at cost, consisting of the amount of the initial measurement of the lease liability, plus any lease payments made to the lessor at or before the commencement date less any lease incentives received, the initial estimate of restoration costs and any initial direct costs incurred by the lessee. The provision for the restoration costs is recognised as a separate liability.

Initial measurement of a right-of-use asset and a lease liability



Lease Payment

Lease payments consist of the following components:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payments that depend on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option (if the lessee is reasonably certain to exercise that option); and
- payments of penalties for terminating the lease (if the lease term reflects the lessee exercising the option to terminate the lease).

PSAK 73 distinguishes between three kinds of contingent payments, depending on the underlying variable and the probability that they actually result in payments:

1. Variable-lease payments based on an index or a rate: Variable lease payments based on an index or a rate (for example, linked to a consumer price index, a benchmark interest rate or a market rental rate) are part of the lease liability. From the perspective of the lessee, these payments are unavoidable, because any uncertainty relates only to the measurement of the liability but not to its existence. Variable lease payments based on an index or a rate are initially measured using the index or the rate at the commencement date (instead of forward rates or indices). This means that an entity does not forecast future changes of the index or rate; these changes are taken into account at the point in time in which lease payments change. The accounting for variable lease payments that depend on an index or a rate is illustrated in the example on page 32.
2. Variable-lease payments based on any other variable: Variable lease payments not based on an index or a rate are not part of the lease liability. These include payments linked to a lessee's performance derived from the underlying asset, such as payments of a specified percentage of sales made from a retail store or based on the output of a solar or a wind farm. Similarly payments linked to the use of the underlying asset are excluded from the lease liability, such as payments if the lessee exceeds a specified mileage. Such payments are recognised in profit or loss in the period in which the event or condition that triggers those payments occurs.
3. In-substance fixed payments: Lease payments that, in form, contain variability but, in substance, are fixed are included in the lease liability. The standard states that a lease payment is in-substance fixed if there is no genuine variability (for example, where payments must be made if the asset is proven to be capable of operating, or where payments must be made only if an event occurs that has no genuine possibility of not occurring). Furthermore, the existence of a choice for the lessee within a lease agreement can also result in an in-substance fixed payment. If, for example, the lessee has the choice either to extend the lease term or to purchase the underlying asset, the lowest cash outflow (that is, either the discounted lease payments throughout the extension period or the discounted purchase price) represents an in-substance fixed payment. In other words, the entity cannot argue that neither the extension option nor the purchase option will be exercised.

If payments are initially structured as variable-lease payments linked to the use of the underlying asset but the variability will be resolved at a later point in time, those payments become in-substance fixed payments when the variability is resolved.

PSAK 30 does not contain any specific guidance on in-substance fixed payments.

However, the current practice already follows this approach.

PwC Observation:

Determining whether a contingent payment is a 'disguised' or in-substance fixed lease payment will require a significant judgement, particularly as the standard includes only limited guidance on how to interpret the term.

A residual-value guarantee captures any kind of guarantee made to the lessor that the underlying asset will have a minimum value at the end of the lease term. The Board indicated it believed that a residual-value guarantee could be interpreted as an obligation to make payments based on variability in the market price for the underlying asset and is similar to variable-lease payments based on an index or a rate.

Discount rate

The lessee uses as the discount rate the interest rate implicit in the lease: this is the rate of interest that causes the present value of (a) lease payments and (b) the unguaranteed residual value to equal the sum of (i) the fair value of the underlying asset and (ii) any initial direct costs of the lessor. Determining the interest rate implicit in the lease is a key judgement that can have a significant impact on an entity's financial statements.

If this rate cannot be readily determined, the lessee should instead use its incremental borrowing rate.

The incremental borrowing rate is defined as the rate of interest that a lessee would have to pay to borrow, over a similar term and with a similar security, the funds necessary to obtain an asset of a similar value to the cost of the right-of-use asset in a similar economic environment.

Restoration costs

In many cases, the lessee is obliged to return the underlying to the lessor in a specific condition or to restore the site on which the underlying asset has been located. To reflect this obligation, the lessee recognises a provision in accordance with PSAK 57, Provisions, Contingent Liabilities and Contingent Assets. The initial carrying amount of the provision, if any, (that is, the initial estimate of costs to be incurred) should be included in the initial measurement of the right-of-use asset. This corresponds to the accounting for restoration costs in PSAK 16 Property, Plant and Equipment.

Any subsequent change in the measurement of the provision, due to a revised estimation of expected restoration costs, is accounted for as an adjustment of the right-of-use asset as required by ISAK 9, Changes in Existing Decommissioning, Restoration and Similar Liabilities.

Initial direct costs

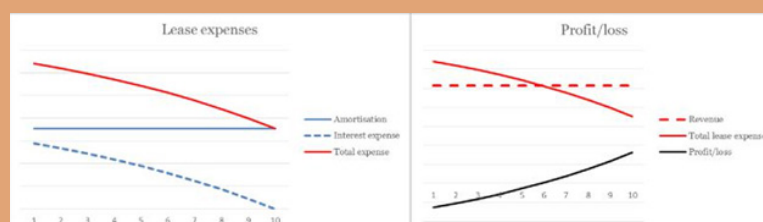
The standard defines initial direct costs as incremental costs that would not have been incurred if a lease had not been obtained. Such costs include commissions or some payments made to existing tenants to obtain the lease. All initial direct costs are included in the initial measurement of the right-of-use asset.

Subsequent measurement

The lease liability is measured in subsequent periods using the effective interest rate method. The right-of-use asset is depreciated in accordance with the requirements in PSAK 16, 'Property, Plant and Equipment' which will result in a depreciation on a straight-line basis or another systematic basis that is more representative of the pattern in which the entity expects to consume the right-of-use asset. The lessee must also apply the impairment requirements in PSAK 48, Impairment of Assets, to the right-of-use asset

PwC observation:

The combination of a straight-line depreciation of the right-of-use asset and the effective interest rate method applied to the lease liability results in a decreasing 'total lease expense' throughout the lease term. This effect is sometimes referred to as 'frontloading'.

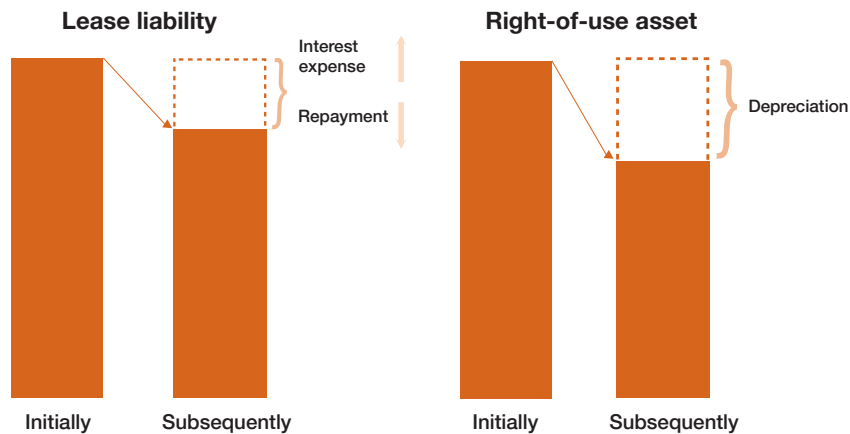


Many stakeholders believe that the 'frontloading effect' creates artificial volatility in the income statement that does not properly reflect the economic characteristics of a lease contract, particularly if the risk and rewards incidental to ownership stay with the lessor (operating lease). Others believe that in economic terms, a lease contract is the acquisition of a right to use an underlying asset with the purchase price paid in instalments and that 'frontloading' reflects this.

It should be noted, however, that, if the lessee has a portfolio of similar lease assets that are replaced on a regular basis, the effect should even out.

The carrying amount of the right-of-use asset and the lease liability will no longer be equal in subsequent periods. Due to the 'frontloading' effect described above, the carrying amount of the right-of-use asset will, in general, be below the carrying amount of the lease liability.

Subsequent measurement of lease liability and right-of-use asset



Reassessment

As actual lease payments can differ significantly from lease payments incorporated in the lease liability on initial recognition, the standard specifies when the lease liability is to be reassessed. It is important to note that a reassessment only takes place if the change in cash flows is based on contractual clauses that have been part of the contract since inception. Any changes that result from renegotiations are discussed under 'modification of a lease' below.

The requirements for reassessment are summarised below:

Component of the lease liability	Reassessment
Lease term and associated extension and termination payments	When? – If there is a change in the lease term. How? – Reflect the revised payments using a revised discount rate (the interest rate implicit in the lease for the remainder of lease term (if that rate can be readily determined); otherwise: incremental borrowing rate at the date of reassessment).
Exercise price of a purchase option	When? – If a significant event or change in circumstances occurs that is within the control of the lessee and affects whether the lessee is reasonably certain to exercise an option. How? – Reflect the revised payments using a revised discount rate (the interest rate implicit in the lease for the remainder of lease term (if that rate can be readily determined); otherwise: incremental borrowing rate at the date of reassessment).
Amounts expected to be payable under a residual value guarantee	When? – If there is a change in the amount expected to be paid. How? – Include the revised residual payment using the unchanged discount rate.
Variable lease payment dependent on an index or a rate	When? – If a change in the index or rate results in a change in cash flows. How? – Reflect the revised payments based on the index or rate at the date when the new cash flows take effect for the remainder of the term using the unchanged discount rate. (Exception: the discount rate has to be updated if the change results from a change in floating interest rates).

Example

An entity operating in an inflationary environment entered into a ten-year lease contract with annual lease payments of CU 50,000, payable at the beginning of each year. Every two years, lease payments will be adjusted to reflect changes in the Consumer Price Index (CPI) for the preceding 24 months. At the commencement date, the CPI was 125. At the beginning of the third year, CPI is 135.

When is the lease liability reassessed?

On initial recognition, the lease liability is calculated based on the contractual lease payments of CU 50,000 p.a. Even if the CPI may change the entity will not re-measure its lease liability before the beginning of the third year because until then the change in CPI does not result in a change in cash flows. At the beginning of the third year, however, the lease liability has to be adjusted because the contractual cash flows have changed.

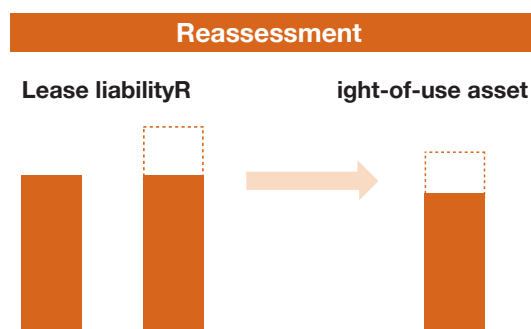
How is the lease liability reassessed?

The revised measurement of the lease liability is at the present value of the revised payments, based on the CPI at the date of change for the remainder of the term using the unchanged discount rate (that is $CU\ 50,000 \times 135 / 125 = CU\ 54,000$).

Aside from this, the lease liability must be re-measured if payments initially structured as variable payments become in-substance fixed-lease payments because the variability is resolved at some point after the commencement date.

Any re-measurement of the lease liability results in a corresponding adjustment of the right-of-use asset. If the carrying amount of the right-of-use asset has already been reduced to zero, the remaining re-measurement is recognised in profit or loss.

Reassessment of a lease liability



The right-of-use asset is also re-measured if the carrying amount of the provision for restoration costs has changed due to a revised estimate of expected costs. In that instance, the change in the carrying amount of the right-of-use asset is equal to the change in the carrying amount of the provision. If adjustments result in an addition the entity must consider whether this is an indication that the new carrying amount of the right-of-use asset may not be fully recoverable.

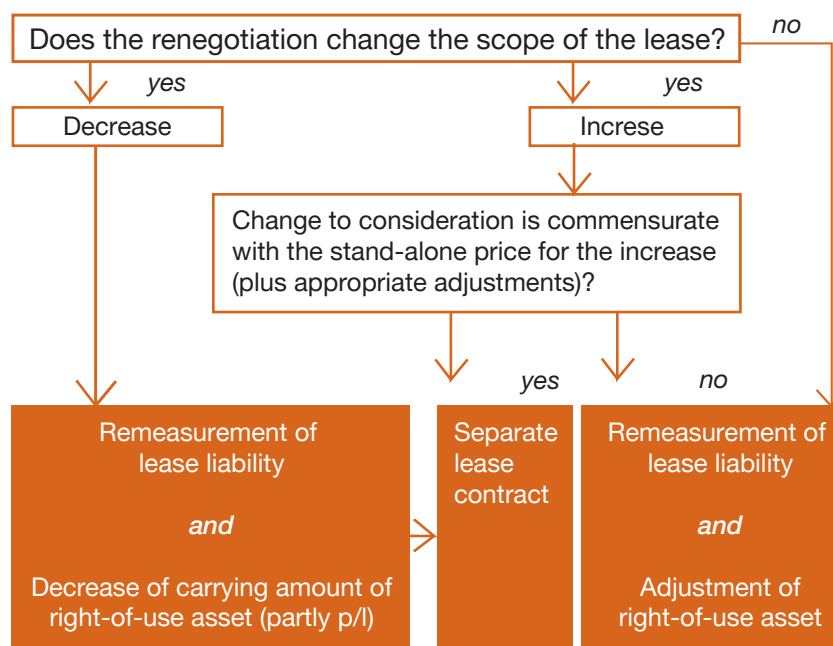
Modification of a lease

There are many different reasons why the parties to a contract might decide to renegotiate and modify an existing lease contract during the lease term. One objective might be to extend or shorten the term of an existing contract (with or without changing the other contractual terms); another reason might be to change the underlying asset (for example, a lessee already leases two floors of a building and the parties agree to add a third floor). If the lessee is in financial difficulties, the lessor might agree to reduce lease payments as a concession to support a restructuring.

PSAK 73 defines a modification as a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease. Any change that is triggered by a clause that is already part of the original lease contract (including changes due to a market rent review clause or the exercise of an extension option) is not regarded as a modification.

The accounting for the modification of a lease depends on how the contract is modified. The standard distinguishes between three different scenarios:

Modification of a lease



An example for a renegotiation that would result in a change of the scope of the lease would be adding an additional floor to the existing lease of a building for the remaining lease term. The effective date of the modification is the date on which the parties agree to the modification of the lease.

In cases where the modification is not accounted for as a separate lease the lessee must, as a first step, allocate the consideration in the modified contract between separate lease and non-lease components and determine the lease term of the modified lease (that is, reassess the previous estimation of the lease term).

Decrease in scope

If the lease is modified to terminate the right of use of one or more underlying assets (for example, a lessee already leases three floors of a building and the parties agree to reduce the lease by one floor for the remaining contractual term) or to shorten the contractual lease term, the lessee remeasures the lease liability at the effective date of the modification using a revised discount rate. The revised discount rate is the interest rate implicit in the lease for the remainder of the lease term (or, if not readily determinable, the lessee's incremental borrowing rate at that time). Furthermore, it decreases the carrying amount of the right-of-use asset to reflect the partial or full termination of the lease. Any gain or loss relating to the partial or full termination is recognised in profit or loss.

Example

A lessee enters into a lease for 5,000 square metres of office space for ten years. The lease payment are fixed at CU 50,000 p.a. After five years, the parties amend the contract to reduce the office space by 2,500 square metres. From year six onwards, the annual lease payment will be CU 30,000. At the beginning of year six, the lessee's incremental borrowing rate is 5% (assuming that the rate implicit in the lease at that date is not readily determinable).

The carrying amounts of the lease liability and right-of-use asset before modification are as follows:

Carrying amount of the right-of-use asset before the modification: CU184,002

Carrying amount of the lease liability before the modification: CU210,618

The value of the lease liability after the modification is

$$\text{CU } 129,884 = \frac{\text{CU } 30,000}{1.05} + \frac{\text{CU } 30,000}{1.05^2} + \frac{\text{CU } 30,000}{1.05^3} + \frac{\text{CU } 30,000}{1.05^4} + \frac{\text{CU } 30,000}{1.05^5}$$

In a first step, the right-of-use asset and the lease liability are reduced by 50%, because the original office space has been reduced by 50%. The difference between these two amounts is recognised as a gain in profit or loss:

(1) Decrease of the carrying amount of the right-of-use asset

Lease liability	CU 105,309
<i>(50% of carrying amount before modification)</i>	
Right-of-use asset	CU 92,001
<i>(50% of carrying amount before modification)</i>	
Gain	CU 13,308

In a second step, the right-of-use asset has to be adjusted to reflect the updated discount rate and the change in the consideration. Accordingly, the difference between the remaining lease liability (CU105,309) and the modified lease liability (CU129,884) is recognised as an adjustment to the right-of-use asset:

(2) Adjustment of the right-of-use asset

Right-of-use asset	CU 24,575
Financial liability	CU 24,575

Increase in scope with a corresponding increase in the lease consideration

If there has been an increase in the scope of the lease and the consideration for the lease increase is commensurate with the stand-alone price for the increase in scope, the modification is accounted for as a separate lease. To be commensurate, the increase in the consideration does not need to be equal to the stand-alone price of the increase in scope. The standard makes clear that any 'appropriate adjustments' to reflect the circumstances of the particular contract are still in line with the assumption that a change in the consideration is commensurate. So for example a discount that reflects the costs the lessor would have incurred when looking for a new lessee (such as marketing costs), may be an appropriate adjustment.

It is important to note that an increase in the scope of the lease only arises if the parties add the right to use one or more underlying assets. The extension of an existing right of use (for example, by a change in the lease term) is not an increase in scope and, therefore, always results in the continuation of the existing lease; however, it is still accounted for as a modification of a lease.

PwC Observation:

In practice, it might be difficult to decide whether an increase in consideration is commensurate with an increase in scope of the lease. According to PSAK 73, a change in consideration will still be commensurate with the change in the scope of the lease if it includes appropriate adjustments to reflect the circumstances of the particular contract. However, the assessment of whether an adjustment is appropriate will be highly subject to judgment.

Increase in scope without a corresponding increase in the lease consideration

If the consideration paid for the increase in the scope of the lease does not increase by a commensurate amount (that is, the stand-alone price for the increase in scope and any appropriate adjustments), the lessee re-measures the lease liability at the effective date of the modification using a revised discount rate and makes a corresponding adjustment to the right-of-use asset. The revised discount rate is the interest rate implicit in the lease for the remainder of the lease term (or, if not readily determinable, the lessee's incremental borrowing rate at that time).

Example

A lessee enters into a lease for 5,000 square metres of office space for ten years. The lease payments are fixed at CU100,000 p.a. After five years, the parties amend the contract for an additional 5,000 square metres. The annual lease payments increase to CU150,000. The market rent for the additional 5,000 square metres is CU100,000. At the beginning of year six, the lessee's incremental borrowing rate is 7% (assume that the interest rate implicit in the lease at that date is not readily determinable).

The parties decided to add an additional right of use (that is, for 5,000 square metres of office space) and increase the scope of the lease. However, the additional lease payments are not commensurate with the stand-alone price for the additional office space and any appropriate adjustments. Accordingly, the modification is not accounted for as a separate lease but as an adjustment to the original lease. The modified lease liability is calculated as the present value of the five remaining lease payments (CU150,000 each) discounted using the lessee's incremental borrowing rate at the effective date of the lease modification (7%). This results in a (revised) lease liability of CU615,030. The difference between this amount and the carrying amount of the lease liability immediately before the modification of the lease is recognised as an adjustment to the right-of-use asset.

If, however, the consideration for the additional office space is increased by CU100,000 p.a. to CU200,000 p.a. (that is, by an amount equal to the stand-alone price for the additional right of use), the modification is instead accounted for as a second, separate lease for 5,000 square metres of office space over a five-year period.

Change in the lease consideration

If the parties to the contract change the consideration of the lease without increasing or decreasing the scope of the lease, the lessee re-measures the lease liability using the interest rate implicit in the lease for the remainder of the lease term (or, if not readily determinable, the lessee's incremental borrowing rate at the effective date of modification) and makes a corresponding adjustment to the right-of-use asset.

PwC Observation:

PSAK 30 did not contain guidance on accounting for modifications. Accordingly, although the guidance in PSAK 73 requires the application of judgement (for example, in assessing whether the increase in the consideration for the lease is commensurate with the stand-alone price for the additional right of use and any appropriate adjustments), it is expected that this will improve consistency in the accounting for lease modifications.

Other measurement models

Aside from the cost model described above, PSAK 73 contains two alternative measurement models that can impact measurement for certain right-of-use assets:

- A right-of-use asset must be subsequently measured in accordance with the fair value model in PSAK 13 if the right-of-use asset meets the definition of investment property and the lessee has elected the fair value model in PSAK 13.
- A right-of-use asset can be subsequently measured at the revalued amount in accordance with PSAK 16 if it relates to a class of property, plant and equipment and the lessee applies the revaluation model to all assets in that class.

Presentation and disclosures

On the balance sheet, the right-of-use asset can be presented either separately or in the same line item in which the underlying asset would be presented. The lease liability can be presented either as a separate line item or together with other financial liabilities. If the right-of-use asset and the lease liability are not presented as separate line items, an entity discloses in the notes the carrying amount of those items and the line item in which they are included.

In the statement of profit or loss and other comprehensive income, the depreciation charge of the right-of-use asset is presented in the same line item or items in which similar expenses (such as depreciation of property, plant and equipment) are shown. The interest expense on the lease liability is presented as part of finance costs. However, the amount of interest expense on lease liabilities has to be disclosed in the notes.

In the statement of cash flows, lease payments are classified consistently with payments on other financial liabilities:

- The part of the lease payment that represents cash payments for the principal portion of the lease liability is presented as a cash flow resulting from financing activities.
- The part of the lease payment that represents interest portion of the lease liability is presented either as an operating cash flow or a cash flow resulting from financing activities (in accordance with the entity's accounting policy regarding the presentation of interest payments).
- Payments on short-term leases, for leases of low-value assets and variable-lease payments not included in the measurement of the lease liability are presented as an operating cash flow.

To provide users with information that allows them to assess the amount, timing and uncertainty of lease payment, PSAK 73 includes enhanced disclosure requirements. The most disclosures are shown in the appendix to this publication.

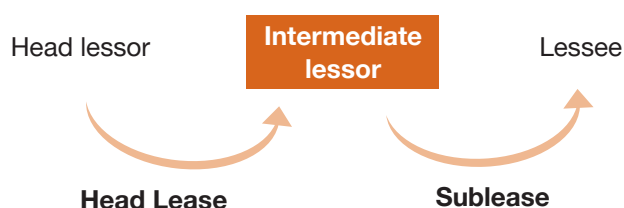
Lessor Accounting

PSAK 73 does not contain substantial changes to lessor accounting compared to PSAK 30. The lessor still has to classify leases as either finance or operating, depending on whether substantially all of the risk and rewards incidental to ownership of the underlying asset have been transferred. For a finance lease, the lessor recognises a receivable at an amount equal to the net investment in the lease which is the present value of the aggregate of lease payments receivable by the lessor and any unguaranteed residual value. If the contract is classified as an operating lease, the lessor continues to present the underlying assets.

There are, however, some changes to current requirements worth mentioning.

Subleases

Structure of a sublease



Under PSAK 30, a sublease was classified with reference to the underlying asset. PSAK 73 now requires the lessor to evaluate the sublease with reference to the right-of-use asset. Because, typically, the fair value of the right-of-use asset is below the fair value of the underlying asset, subleases are now more likely to be classified as finance leases. Aside from this, since the lessor of the sublease is, at the same time, the lessee with respect to the head lease, it will in any case have to recognise an asset on its balance sheet: as a right-of-use asset with respect to the head lease (if the sublease is classified as an operating lease) or a lease receivable with respect to the sublease (if the sublease is classified as a finance lease).

If the head lease is a short-term lease, the sublease must be classified as an operating lease.

For a sublease that results in a finance lease, the intermediate lessor is not permitted to offset the remaining lease liability (from the head lease) and the lease receivable (from the sublease). The same is true for the lease income and lease expense relating to head lease and sublease of the same underlying asset.

Manufacturer/dealer lessor

The guidance regarding when and to what extent a manufacturer or dealer lessor should recognise profit or loss remains almost unchanged. According to PSAK 73:

- revenue is the fair value of the underlying asset, or, if lower, the present value of the lease payments accruing to the lessor, discounted using a market rate of interest;
- cost of sale is the cost, or carrying amount if different, of the underlying asset less the present value of the unguaranteed residual value; and
- selling profit or loss is the difference between revenue and the cost of sale recognised in accordance with an entity's policy for outright sales to which PSAK 72 applies.

A manufacturer or dealer lessor must recognise selling profit or loss on a finance lease at the commencement date, regardless of whether the lessor transfers the underlying asset as described in PSAK 72.

Aside from this, the new guidance on identifying a lease (as described at the beginning of this edition of In Depth) also affects the lessor.

Modification of a lease

PSAK 30 is silent about how to account for the modification of a lease for lessors. To avoid diversity in practice, PSAK 73 includes specific rules:

Modification of an operating lease

The modification of an operating lease should be accounted for as a new lease by the lessor. Any prepaid or accrued lease payments are considered to be payments for the new lease (that is, they will be spread over the new term of the modified lease).

Modification of a finance lease

A lessor accounts for the modification of a finance lease as a separate lease if:

- the modification increases the scope of the lease; and
- the consideration for the lease increases by an amount commensurate with the stand-alone price for the increase in scope and any appropriate adjustments to that price to reflect the circumstances of the particular contract.

This mirrors the guidance for lessees.

If one of the above criteria is not met, the lessor has to assess whether the modification would have resulted in either an operating or a finance lease if it had been in effect at inception of the lease:

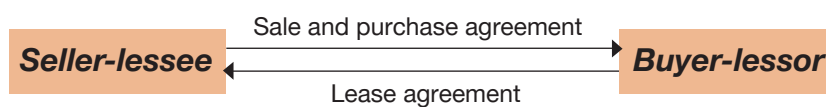
- If the lease would have been classified as an operating lease, the lessor accounts for the modification as a new lease (operating lease). The carrying amount of the underlying asset that has to be recognised is measured as the net investment in the original lease immediately before the lease modification.
- If the lease would have been classified as a finance lease, the lessor accounts for the lease modification in accordance with PSAK 71.

Sale and leaseback transactions

Determining whether the transfer is a sale

Aside from lessee accounting, the accounting for sale and leaseback transactions is one of the main areas in which the new lease standard changes the current guidance. The accounting for sale and leaseback transactions under PSAK 30 mainly depended on whether the leaseback was classified as a finance or an operating lease. Under PSAK 73 the determining factor is whether the transfer of the asset qualifies as a sale in accordance with PSAK 72. An entity must apply the requirements for determining when a performance obligation is satisfied in PSAK 72 to make this assessment.

Structure of a sale and leaseback



Transfer of the asset is a sale

If the buyer-lessor has obtained control of the underlying asset and the transfer is classified as a sale in accordance with PSAK 72, the seller-lessee measures a right-of-use asset arising from the leaseback as the proportion of the previous carrying amount of the asset that relates to the right of use retained. The gain (or loss) that the seller-lessee recognises is limited to the proportion of the total gain (or loss) that relates to the rights transferred to the buyer-lessor.

If the consideration for the sale is not equal to the fair value of the asset, any resulting difference represents either a prepayment of lease payments (if the purchase price is below market terms) or an additional financing (if the purchase price is above market terms). The same logic applies if the lease payments are not at market rates.

The buyer-lessor accounts for the purchase in accordance with applicable standards (such as PSAK 16 if the underlying asset is property, plant or equipment), and for the leaseback in accordance with PSAK 73.

Example (from the perspective of the seller-lessee)

A seller-lessee sells a building to an unrelated buyer-lessor for cash of CU2,000,000. The fair value of the building at that time is CU1,800,000; the carrying amount immediately before the transaction is CU1,000,000.

At the same time, the seller-lessee enters into a contract with the buyer-lessor for the right to use the building for 18 years, with annual payments of CU120,000 payable at the end of each year. The interest rate implicit in the lease is 4.5%, which results in a present value of the annual payments of CU1,459,200.

The transfer of the asset to the buyer-lessor has been assessed as meeting the definition of a sale under PSAK 72.

Financing transaction

Since the consideration (CU2,000,000) exceeds the fair value (CU1,800,000) of the building, the agreement contains a financing transaction:

(1) Financing transaction			
Cash		CU 200,000	
	Financial liability		CU 200,000

Sale and Leaseback

The seller-lessee initially recognises a right-of-use asset as the proportion of the previous carrying amount (CU1,000,000) that reflects the right of use retained. The proportion is calculated by dividing the present value of the lease payment (CU 1,459,200) less the part of the lease payments that is just a repayment of the financing granted to the seller-lessee (CU 200,000) [= CU1,259,200] by the fair value of the asset (CU1,800,000).

$$\frac{\text{CU } 1,259,200}{\text{CU } 1,800,000} \times \text{CU } 1,000,000 \\ = \text{CU } 699,555$$

The gain on sale is calculated as a proportion of the total gain of CU 800,000 (purchase price less financing element less carrying amount of the building), representing the ratio between the rights fair value of the building less the right-of-use asset obtained by the building:

$$\frac{\text{CU } 1,800,000 - \text{CU } 1,259,200}{\text{CU } 1,800,000} \times \text{CU } 800,000 \\ = \text{CU } 240,355$$

(2) Sale and leaseback			
Cash		CU 1,800,000	
Right-of-use asset		CU 699,555	
	Building		CU 1,000,000
	Financial liability		CU 1,259,200
	Gain		CU 240,355

Transfer of the asset is not a sale

If the transfer is not a sale (that is, the buyer-lessor does not obtain control of the asset in accordance with PSAK 72), the seller-lessee does not de-recognise the transferred asset and accounts for the cash received as a financial liability. The buyer-lessor does not recognise the transferred asset and, instead, accounts for the cash paid as a financial asset (receivable).

Transition

PSAK 73 is effective for reporting periods beginning on or after 1 January 2020. Earlier application is permitted, but only in conjunction with PSAK 72. This means that an entity is not allowed to apply PSAK 73 before applying PSAK 72. The date of initial application is the beginning of the annual reporting period in which an entity first applies PSAK 73.

Definition of a lease

Entities are not required to reassess existing lease contracts but can elect to apply the guidance regarding the definition of a lease only to contracts entered into (or changed) on or after the date of initial application ('grandfathering'). This applies to both contracts that were not previously identified as containing a lease applying PSAK 30/ISAK 8 and those that were previously identified as leases in PSAK 30/ISAK 8. If an entity chooses this expedient it shall be applied to all of its contracts.

Acknowledging the potentially significant impact of the new lease standard on a lessee's financial statements, PSAK 73 does not require a full retrospective application in accordance with PSAK 25 but allows a 'simplified approach'. Full retrospective application is optional.

Simplified approach – lessee accounting

If a lessee elects the simplified approach, it does not restate comparative information. Instead, the cumulative effect of applying the standard is recognised as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the date of initial application.

Balance sheet item	Measurement
Lease previously classified as operating lease	
Lease liability	Remaining lease payments, discounted using the lessee's incremental borrowing rate at the date of initial application.
Right-of-use asset	Retrospective calculation, using a discount rate based on the lessee's incremental borrowing rate at the date of initial application. or Amount of lease liability (adjusted by the amount of any previously recognised prepaid or accrued lease payments relating to that lease). (The lessee can choose one of the alternatives on a lease-by-lease basis.)
Leases previously classified as finance leases	
Lease liability	Carrying amount of the lease liability immediately before the date of initial application.
Right-of-use asset	Carrying amount of the lease asset immediately before the date of initial application.

A lessee is not required to apply the new lessee accounting model to leases for which the lease term ends within 12 months after the date of initial application.

Simplified approach – lessor accounting

Lessor accounting stays largely the same as under PSAK 30. The only significant change is that, under PSAK 73, subleases must be classified either as finance or as operating leases, with reference to the right-of-use asset resulting from the head lease.

Hence, the lessor is not required to make any adjustments on transition except for the reassessment of operating subleases ongoing at the date of initial application. The analysis is made on the basis of the remaining contractual terms and conditions of the head lease and the sublease. If operating subleases are now classified as finance leases, the lessor accounts for the sublease as a new finance lease entered into on the date of initial application.

Simplified approach – sale and leaseback

Sale and leaseback transactions entered into before the date of initial application are not reassessed. In the case of a finance leaseback, the seller-lessee continues to amortise any gain on sale over the term of the lease. In the case of an operating leaseback, any deferred gain or loss due to off-market terms is accounted for as an adjustment to the leaseback right-of-use asset.

Retrospective application

If an entity chooses not to use the simplified approach, it has to apply PSAK 73 retrospectively to each prior reporting period in accordance with PSAK 25, Accounting Policies, Changes in Accounting Estimates and Errors.

Appendix

Disclosure requirements for lessees*

Right-of-use asset
Depreciation charge (by class of underlying asset) Carrying amount (by class of underlying asset)
Lease liabilities
Interest expense Maturity analysis in accordance with paragraph 39 and PP11 of PSAK 60
Recognition and measurement exemptions
Expense relating to short-term leases Expense relating to leases of low-value assets
Other disclosures relating to income statement
Expense relating to variable lease payment not included in lease liabilities Income from subleasing right-of-use assets Gains or losses arising from sale and leaseback transactions
Total cash outflow for leases
Future cash outflow from
Variable-lease payments (include key variables on which payments depend and how they affect them)
Extension options and termination options Residual-value guarantee Leases not yet commenced to which the entity committed
Short-term lease commitments
Qualitative disclosures
Nature of the lessee's leasing activities Restrictions or covenants imposed by leases Sale and leaseback transactions

* This table covers the major disclosure requirements; depending on the particular facts and circumstances, additional disclosures might be necessary.

Disclosure requirements for lessors*

Finance lease
Selling profit or loss
Finance income on the net investment in the lease
Lease income relating to variable lease payments not included in the measurement of the lease receivable
Qualitative and quantitative explanation of the significant changes in the carrying amount of the net investment in the lease
Maturity analysis of lease receivable for a minimum of each of the first five years plus a total amount for the remaining years; reconciliation to the net investment in the lease
Operating lease
Lease income, separately disclosing income relating to variable lease payments that do not depend on an index or rate
Maturity analysis of lease payments for a minimum of each of the first five years plus a total amount for the remaining years
Disclosure requirements in PSAK 48, PSAK 19, PSAK 13 and PSAK 69 for assets subject to operating leases
Disclosure requirements in PSAK 16 for items of property, plant and equipment subject to an operating lease
Qualitative disclosure for all leases
Nature of the lessor's leasing activities
Management of the risk associated with any rights that the lessor retains in underlying assets
Relevant requirement of PSAK 60

* This table covers the major disclosure requirements; depending on the particular facts and circumstances, additional disclosures might be necessary.

Comparison of PSAK 73 and PSAK 30/ISAK 8 – overview of the main differences

Issue	PSAK 73	PSAK 30/ ISAK 8
Definition of a lease	Right to use an asset, that is: <ul style="list-style-type: none"> Identified asset, and Right to control the use 	In general similar to PSAK 73, but different detailed guidance
Separating lease components	Separate component, if: <ul style="list-style-type: none"> Separate benefit for lessee, and Not highly interrelated with other component 	No specific guidance (except for lease of land and building)
Combinations of contract	Combine contract if certain criteria are met	No comprehensive guidance (see ISAK 24)
Exemptions		
Short-term lease (lessee)	Lease term \leq 12 months (provided there is no purchase option)	No
Low-value assets (lessee)	No explicit absolute threshold but based on the value of the asset when it is new	No
Lessee accounting		
Balance sheet	Right-of-use asset and lease liability for almost every lease	Operating lease: No asset or liability recognised (only accruals or prepayments) Finance lease: Lease asset and lease liability
Variable lease payment	Part of the lease liability if they depend on index/rate	Not part of the lease liability
Income statement	Single approach <ul style="list-style-type: none"> Right-of-use asset: depreciation Lease liability: effective interest rate method Variable lease payment not included in lease liability (that is, not depending on index/rate) 	Operating lease: Lease payment on a straight-line basis Finance lease: Leased asset: depreciation Lease liability: effective interest rate method Variable lease payments not included in lease liability

Comparison of PSAK 73 and PSAK 30/ISAK 8 – overview of the main differences

Issue	PSAK 73	PSAK 30/ ISAK 8
Cash flow statement	<ul style="list-style-type: none"> Part of lease payment that represents principal portion: Cash flow resulting from financing activities Part of lease payment that represent interest portion: Operating cash flow or cash flow resulting from financing activities (depending on entity's policy) Payment for short-term leases, for lease of low-value assets and variable lease payments not included in lease liability: Operating cash flow 	Operating lease: operating cash flow Finance lease: similar to PSAK 73
Lessor accounting		
Balance sheet	<ul style="list-style-type: none"> Classification as finance or operating lease Finance lease: de-recognition of the underlying asset, recognition of a lease receivable at amount equal to the net investment in the lease Operating lease: continue to recognise the underlying asset 	
Income statement	Finance lease: interest measured using the effective interest rate method Operating lease: lease payments on straight-line basis	
Subleases	Classification of sublease refers to right-to-use asset	Classification of sublease refers to leased asset
Modifications	<ul style="list-style-type: none"> Adjustment of existing lease, or Accounted for as a separate lease, depending on kind of modification 	No specific guidance
Sale and leaseback	Distinction base on whether transfer is sale	Distinction based on classification of leaseback

Impact on lessee's key performance indicators

KPI	Calculation	Effect of PSAK 73
Gearing (debt to equity ratio)	Liabilities/equity	Increase (because most leases previously accounted for as operating leases will now on be on balance sheet)
EBIT	Earning before interest and tax	Increase (because the depreciation added is lower than the lease expense eliminated from operating income)
EBITDA	Earning before interest, tax and amortisation	Increase (because lease expense is eliminated from EBITDA)
Operating cash flow		Increase (because some or all of the operating lease payment are moved to financing)
Asset turnover	Sales/total assets	Increase (because some or all of the operating lease payment are moved to financing)
ROCE	EBIT/Equity plus financial liabilities	Depends on the characteristic of the lease portfolio (EBIT as well as financial liabilities will increase)
Leverage	Net debt/EBITDA	Depends on the characteristics of the lease portfolio (EBITDA as well as net debt will increase)

PwC Indonesia contacts

For further help, please contact:

Jumadi
Partner
jumadi.anggana@id.pwc.com

Irwan Lau
Director
irwan.lau@id.pwc.com

Akuntina Novriani
Senior Manager
akuntina.novriani@id.pwc.com

Elina Mihadja
Manager
elina.mihadja@id.pwc.com

Dariya Karasova
Advisor
dariya.m.karasova@id.pwc.com

Djohan Pinnarwan
Partner
djohan.pinnarwan@id.pwc.com

Helen Cuizon
Advisor
helen.cuizon@id.pwc.com

Jenifer Flitman
Advisor
jenifer.flitman@id.pwc.com

Arryu Amin
Manager
aryu.amin@id.pwc.com

Jasmin Maranan
Advisor
jasmin.maranan@id.pwc.com

Dwi Jayanti
Senior Manager
dwi.jayanti@id.pwc.com

Ponco Widagdo
Senior Manager
ponco.widagdo@id.pwc.com

Roymond Wong
Manager
roymond.wong@id.pwc.com

PwC Indonesia

Jakarta
WTC 3
Jl. Jend. Sudirman Kav. 29-31
Jakarta 12920 - INDONESIA
T: +62 21 5212901
F: +62 21 52905555 / 52905050
www.pwc.com/id

Surabaya
Pakuwon Center
Tunjungan Plaza 5, 22nd Floor, Unit 05
Jl. Embong Malang No.1,3,5
T: +62-31 99245759
Surabaya 60261 INDONESIA
www.pwc.com/id



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