

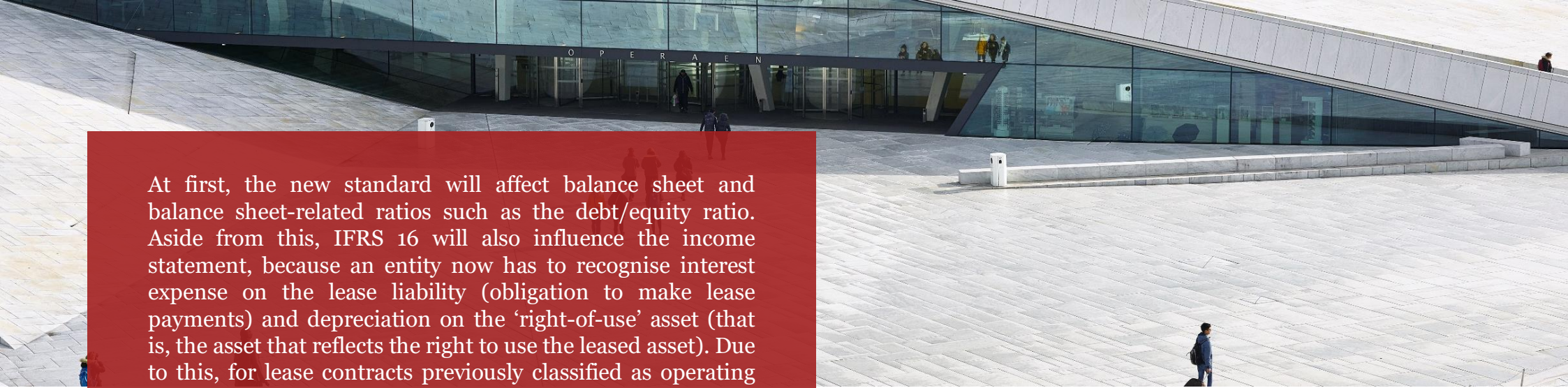


12 July 2018

## *IFRS 16 – a new era of lease accounting!*

### *At a glance...*

In January 2016 the International Accounting Standards Board (IASB) issued IFRS 16, 'Leases', and thereby started a new era of lease accounting – at least for lessees! Whereas, under the previous guidance in IAS 17, 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 IAS 17, 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, IFRS 16 will also influence the income statement, because an entity now has to recognise interest expense on the lease liability (obligation to make lease payments) and depreciation on the 'right-of-use' asset (that is, the asset that reflects the right to use the leased asset). Due to this, 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 IAS 17.

Another consequence of the changes in presentation is that EBIT and EBITDA will be higher for companies that have material operating leases. IFRS 16 takes effective for annual periods beginning on or after 1 January 2019, companies should now review the impacts of IFRS 16 on their EBIT and EBITDA as the impact would be significant for specific companies with loans' covenants relating to EBIT and EBITDA.

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 IFRS 16 adds significant new, enhanced disclosure requirements.

<b>Disclosure requirements for lessees*</b>
<b>Right-of-use asset</b>
<ul style="list-style-type: none"> <li>• Depreciation charge (by class of underlying asset)</li> <li>• Carrying amount (by class of underlying asset)</li> <li>• Additions</li> </ul>
<b>Lease liabilities</b>
<ul style="list-style-type: none"> <li>• Interest expense</li> <li>• Maturity analysis in accordance with paragraph 39 and B11 of IFRS 7</li> </ul>
<b>Recognition and measurement exemptions</b>
<ul style="list-style-type: none"> <li>• Expense relating to short-term leases</li> <li>• Expense relating to leases of low-value assets</li> </ul>
<b>Other disclosures relating to income statement</b>
<ul style="list-style-type: none"> <li>• Expense relating to variable lease payments not included in lease liabilities</li> <li>• Income from subleasing right-of-use assets</li> <li>• Gains or losses arising from sale and leaseback transactions</li> </ul>
<b>Total cash outflow for leases</b>
<b>Future cash outflows from...</b>
<ul style="list-style-type: none"> <li>• Variable lease payments</li> <li>• (includes key variables on which payments depend and how they affect them)</li> <li>• Extension options and termination options</li> <li>• Residual value guarantees</li> <li>• Leases not yet commenced to which the entity is committed</li> <li>• Short-term lease commitments</li> </ul>
<b>Qualitative disclosures</b>
<ul style="list-style-type: none"> <li>• Nature of the lessee's leasing activities</li> <li>• Restrictions or covenants imposed by leases</li> <li>• Sale and leaseback transactions</li> </ul>

<b>Disclosure requirements for lessors*</b>
<b>Selling profit or loss</b>
<ul style="list-style-type: none"> <li>• Finance income on the net investment in the lease</li> <li>• Lease income relating to variable lease payments not included in the measurement of the lease receivable</li> <li>• Qualitative and quantitative explanation of the significant changes in the carrying amount of the net investment in the lease</li> <li>• 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</li> </ul>
<b>Operating lease</b>
<ul style="list-style-type: none"> <li>• Lease income, separately disclosing income relating to variable lease payments that do not depend on an index or rate</li> <li>• Maturity analysis of lease payments for a minimum of each of the first five years plus a total amount for the remaining years</li> <li>• Disclosure requirements in IAS 36, IAS 38, IAS 40 and IAS 41 for assets subject to operating leases</li> <li>• Disclosure requirements in IAS 16 for items of property, plant and equipment subject to an operating lease</li> </ul>
<b>Qualitative disclosures for all leases</b>
<ul style="list-style-type: none"> <li>• Nature of the lessor's leasing activities</li> <li>• Management of the risk associated with any rights that the lessor retains in underlying assets</li> </ul>
<b>Relevant requirements of IFRS 7</b>

\* These tables cover the major disclosure requirements; depending on the particular facts and circumstances, additional disclosures might be necessary.

## Contact us

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. For further information, please reach out to us.



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