



---

Project	<b>Leases</b>
Topic	<b>Revisited: Scope—Purchases/sales of the underlying asset</b>

---

## Background and purpose

1. The boards tentatively decided that an entity shall not apply the proposed new requirements for leases to contracts that meet the criteria for classification as a purchase or sale of an underlying asset. A contract is a purchase or sale of an underlying asset if, at the end of the contract, an entity transfers to another entity control of the underlying asset, or all but a trivial amount of the risks and benefits associated with the underlying asset. Such contracts do not meet the definition of a lease.
2. Subsequent to the scope decision, the boards tentatively decided that a lessor should:
  - (a) apply the performance obligation approach to leases that expose it to significant risks and benefits associated with the underlying asset.
  - (b) apply the derecognition approach to leases that do not expose it to significant risks and benefits associated with the underlying asset.
3. Since making the tentative decision on which approach to apply for lessor accounting, some board members have questioned the need to provide specific guidance in the leases requirements that distinguishes between purchases and sales and leases.
4. In addition, some constituents (both lessees and lessors) have commented that they think that the dividing line is now unnecessary and that it should be abolished to reduce the complexity of the leases requirements.

IASB/FASB Staff paper

5. The purpose of this paper is to analyse whether the specific guidance for purchases and sales is still required.
6. Based on the analysis in this paper, some staff recommend removing the specific guidance for purchases and sales, for both lessees and lessors. Other staff recommend retaining the specific guidance for purchases and sales, for both lessees and lessors.

**Analysis**

7. The boards tentatively decided that purchases or sales should be outside the scope of the leases requirements because they are not leases, but are instead purchases and sales of the underlying asset.
8. However, some constituents have argued that if the accounting for purchases and sales is similar to the accounting required for leases, providing specific guidance distinguishing between the two is not needed, and would introduce unnecessary complexity into any new leases requirements.
9. The appendix to this paper summarises the main differences between purchase accounting and lease accounting for lessees. The staff note that the required accounting for lessees is very similar to purchase accounting. There are, however, differences in presentation, and there could be significant differences in accounting, if a lease has options and contingencies. The staff also note that accounting differences are unlikely to be material in contracts that are sales and purchases, regardless of accounting approach (eg if there are significant variations in probable contract term or rentals which result in different accounting under lease and sale/purchase requirements, it is unlikely that the contract was a sale and purchase in the first place. That is, the contract is likely to be a lease.).

IASB/FASB Staff paper

10. There are, of course, significant differences between sale accounting and the accounting required under the performance obligation approach. However, the boards' decision to apply the derecognition approach to leases that do not expose the lessor to significant risks and benefits associated with the underlying asset means that all contracts that would otherwise be treated as sales if the purchase/sale guidance is retained would be accounted for under the derecognition approach to lessor accounting.
11. The appendix to this paper summarises the main differences between sales accounting and the derecognition approach to lessor accounting.
12. The staff note that the accounting under the derecognition approach is similar to sale accounting. Under the derecognition approach, the greater the rights transferred to the lessee, the more of the underlying asset is derecognised and profits earned, ie there is no bright line. Indeed, it is possible that the lessor would derecognise the entire asset and recognise income on the date of commencement of the lease, ie the accounting is identical to that required if the asset was sold on that date.
13. However, differences in presentation remain, as well as accounting differences for leases with options and contingencies.
14. The distinction between sale/purchase and lease is important when determining the accounting for a sale and leaseback transaction. The boards tentatively decided to apply similar criteria for determining whether the sale is, in fact, a sale, in order to determine whether it qualifies for sale and leaseback accounting.
15. Some staff think that keeping the guidance distinguishing between a lease and a purchase/sale increases complexity without any benefit. If the distinguishing guidance is retained, sellers/lessors will have five (four for US GAAP) accounting approaches to consider:
  - (a) purchase/sale;
  - (b) performance obligation;
  - (c) derecognition;

IASB/FASB Staff paper

- (d) simplified accounting for short-term leases; and
  - (e) IAS 40 *Investment Property* for investment properties carried at fair value (IFRS only).
16. However, it would be relatively straightforward for the seller/lessor to decide which of the five (four) models to apply; for example, there are no scenarios under which a lessor would have to decide between derecognition and simplified accounting for short-term leases.
17. Nevertheless, the sellers/lessors will likely have to incur additional costs to identify contracts that are sales and purchases, and will have to justify their decision to auditors.
18. It has been suggested that the distinguishing guidance could be removed for sellers/lessors only. This is because purchasers/lessees are not required to make a distinction between leases that transfer an insignificant amount of the risks and benefits, and those that transfer a significant amount. However, the staff do not see a conceptual justification for having the guidance apply to one side of the transaction only.

**Recommendation**

19. One of the main reasons for initially excluding purchases and sales from the leases requirements was that, at the time, the boards opted for a performance obligation approach to accounting by lessors for all leases. This would have resulted in very different accounting for economically-similar transactions, and had prompted the scope exclusion. The boards have since opted for a hybrid approach, under which sales or purchases classified as leases would be accounted for under the derecognition approach, which is very similar to sale accounting.
20. However, it can be argued that purchases and sales are not leases, and should not be accounted for as such. The staff who support retaining the guidance distinguishing purchases and sales from leases believe that removing that

IASB/FASB Staff paper

distinction opens the door for structuring opportunities just based on how the contract is labelled. In addition, even if accounting for the two is similar, it is not identical, and presentation is different.

21. For these reasons, some staff believe that the guidance distinguishing purchases and sales from leases should be retained.
22. Other staff think that, on balance, keeping the guidance would further increase the complexity of the new leases requirement, whilst not adding much value. Those staff therefore recommend that the specific guidance distinguishing purchases and sales from leases should be removed from the proposed new leases requirements.

**Question 1**

The staff ask the boards to decide either:

- that the specific guidance distinguishing purchases and sales from leases should be kept in the leases requirements, or
- that the specific guidance distinguishing purchases and sales from leases should be removed from the leases requirements.

The staff have split views.

## IASB/FASB Staff paper

## Appendix 1

*Analysis of differences in lease and purchase accounting for lessees*

Area	Lease accounting	Purchase/sale accounting
Presentation	The right-of-use asset is an intangible asset, but it is presented separately within PP&E. All balance sheet and income statement items would be presented separately and identified as part of a lease transaction.	The asset would be presented as PP&E according to its nature.
Liability	Subsequent measurement of the liability will be on an amortised-cost basis only. Lessees will have to reassess their liability throughout the lease term.	It may be possible to elect to fair value the liability.
Asset	Subsequent measurement of the right-of-use asset will be amortisation over the lease term. There could be remeasurements as a result of changes in contingent rentals and options <sup>1</sup> .	Subsequent measurement of the underlying asset will be depreciation over the estimated life of the underlying asset.
Options to extend and terminate	Payments during optional periods may be included in the obligation to pay rentals.	Optional payments would be excluded from the liability.
Contingencies	Contingent payments are included in the obligation to pay rentals <sup>1</sup> .	Contingent payments may be excluded from the liability.

---

<sup>1</sup> It is unlikely that contracts with significant contingent rentals would be a sale and purchase of the underlying asset.

IASB/FASB Staff paper

*Analysis of differences in accounting for lessors – derecognition approach*

<b>Area</b>	<b>Lease accounting</b>	<b>Purchase/sale accounting</b>
Presentation	Receivable in financing. Residual asset in PP&E. All items would be separately identified as part of a leasing arrangement.	Receivable would be presented in the financing section. There is no residual asset.
Asset	Receivable + residual asset. If risks and benefits retained by the lessor are trivial, the residual asset will be small. There could be a reassessment of the receivable.	Receivable only.
Income	Equal to the receivable recognised.	Recognised for the full value of the asset.
Options to extend and/or terminate	Payments during optional periods may be included in the measurement of the receivable.	Optional payments would be excluded from the receivable.
Contingent rentals	Only recognised if can be measured reliably. Reliability is not specifically defined.	Only recognised if can be reasonably estimated, defined as the entity having past and relevant experience (as per the Revenue Recognition ED).

Deleted: ¶  
 =====Section Break (Next Page)=====