May 17, 2021

Mr. Ian Carruthers
Chairman,
International Public Sector Accounting Standards Board.

Dear Ian Carruthers,

Sub: Comment on Exposure Draft 75, *Leases*

We are pleased to provide comments on the Exposure Draft 75 on *Leases* issued by the International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants (IFAC). Our comments on the Exposure Draft 75 are enclosed with this letter.

Please feel free to contact us, in case any further clarification in this regard is required.

Thanking you,

Yours sincerely,

(CA. Dheeraj Kumar Khandelwal)
Chairman, Committee on Public &
Government Financial Management
The Institute of Chartered Accountants of India
Ph: 011-30110459 (CP&GFM Secretariat)
E-mail Id: cpf.aslb@icai.in; caslb@icai.in

Encl.: As above

Comments on Exposure Draft (ED) 75, 'Leases' issued by the International Public Sector Accounting Standard Board (IPSASB)

Specific Matter for Comment 1:

The IPSASB decided to propose an IFRS 16-aligned Standard in ED 75 (see paragraphs BC21–BC36). Do you agree with how the IPSASB has modified IFRS 16 for the public sector (see paragraphs BC37–BC60)? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

ICAI's View

We agree with the approach of IPSASB to adopt IFRS 16, '*Leases*' that has been modified in the context of the public sector. We are in concurrence with the following major departures made by IPSASB from IFRS 16:

1. **Use of Public sector specific terminologies**
   We agree with the departures made by IPSASB relating to the usage of terminologies specific to public sector.

2. **Consideration of both "Economic Benefits" or "Service Potential" for identifying a lease**
   We agree with the said departure. Reasons are stated in our response to the Specific Matter for Comment 3.

3. **Non-inclusion of specific requirements for manufacturer or dealer lessors**
   Public Sector generally do not play role as manufacturer or dealer lessor, therefore, the deletion of this concept is fine in the context of the public sector.

Accounting for lessors and lessees

With regard to accounting of lessee, the IPSASB, aligned with IFRS 16, prescribes the lessee to recognise right-of-use asset (lessee's right to use an underlying asset over the lease term) and lease liability (present obligation to make lease payments) that meets the definition of assets and liabilities as per IPSASB's Conceptual Framework. The said assets and liabilities to be measured by the lessee at cost (determined with reference to the present value of the lease payments). In exceptional cases (short-term lease and leases for which underlying asset is of low value), the lessee shall recognise the lease payments as an expense on either straight-line basis over the lease term or another systematic basis if that basis is more representative of the pattern of lessee's benefits.

The control of underlying asset remains with the lessor so it is to be recognised in the books of lessor and only right to use underlying asset is to be recognised in the books of lessee. However, present IPSAS 13 prescribes classification of lease into operating or financing lease and the underlying assets to be recognised by the lessee in case of finance lease (but not in case of operating lease) which leads to the assets and liabilities associated with lease remaining off-balance sheet in the books of lessee in case of operating lease; it's a lacuna in existing lessee's accounting system.

We principally agree with the IPSASB to adopt the 'right-of-use' model for lessee accounting that provides more complete and useful information to the investors and other users of the financial statements.

With regard to accounting of lessor, the IPSASB, aligned with IFRS 16, has prescribed separate accounting for operating lease and finance lease. According to ED 75:

- Under finance lease, initially lessor to recognise assets held under a finance lease (to be presented as receivable) in the statement of financial position at an amount equal to net investment in the lease. Subsequently, lessor to recognise finance revenue over the lease term on a systematic and rational basis.
- Under operating lease, lessor to recognise lease payments as revenue on either straight-line basis over the lease term or another systematic basis if that basis is more representative of the pattern in which benefit from the use of the underlying asset is diminished.

We agree with the above-mentioned accounting for lessors prescribed by lessor. In case of finance lease, ED 75 proposes to recognise underlying assets in the form of receivable which is better than the approach of present IPSAS 13 that prescribes recognition of both, underlying assets and receivable, that leads to artificial inflation of assets which is misleading for the investors and other users of financial statements.

It has been noticed that the examples of lessee accounting have been covered in detail in appendix (illustrative examples). It is suggested that the illustrative examples of lessor accounting may also be incorporated in the appendix.

Specific Matter for Comment 2:

The IPSASB decided to propose the retention of the fair value definition from IFRS 16 and IPSAS 13, *Leases*, which differs from the definition proposed in ED 77, *Measurement*[1] (see paragraphs BC43– BC45). Do you agree with the IPSASB's decision? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

ICAI's View

For the purpose of applying the requirements of lessor's accounting, ED 75, Leases, defines *fair value* as an amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. However, ED 77, '*Measurement*' prescribes *fair value* as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

It is suggested that the definition of 'fair value' should be in concurrence with the IPSASB's Measurement project (ED 77) and IPSASB's Conceptual Framework. IPSASB's Conceptual Framework uses the term 'market value' (entity specific) instead of 'fair value' (market specific). One uniform definition should exist in IPSASB's framework. Using different definitions will create confusion to the preparers of financial statements.

---

[1] The fair value definition under development in ED 77, *Measurement* is aligned with the fair value definition in IFRS 13 *Fair Value Measurement.*

Specific Matter for Comment 3:

The IPSASB decided to propose to refer to both "economic benefits" and "service potential", where appropriate, in the application guidance section of ED 75 on identifying a lease (see paragraphs BC46–BC48). Do you agree with the IPSASB's decision? If not, please explain your reasons. If you agree, please provide any additional reasons not already discussed in the Basis for Conclusions.

ICAI's View

We agree with the IPSAS's proposal to consider both "economic benefits" or "service potential" for identification of lease of an underlying asset.

We may mention that the primary reason for holding asset in the public sector is generally for their service potential rather than their ability to generate cash flows as it enables an entity to achieve its service delivery objectives. The IPSASB's 'The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities' defines an asset as a resource presently controlled by the entity as a result of a past event and a resource provides benefits to an entity in the form of a service potential or the ability to generate economic benefits. *The service potential or ability to generate economic benefits can arise directly from the resource itself or from the rights to use the resources.* Therefore, the lessee's right to use an underlying asset meets the definition of asset.

Although the lessor transfers the right to use the underlying asset to the lessee at the commencement date, the lessor has the right to the underlying asset at the end of the lease term (and retains some rights to the underlying asset during the lease term; for example, the lessor retains title to the asset). Consequently, the lessor retains some of the rights embodied in the underlying asset. Therefore, the lessor's rights retained in the underlying assets also meet the definition of an asset as per IPSAS's Conceptual Framework.