



June 28, 2018

Cliff: 369750

E-mail: johnstanford@ipsasb.org
John Stanford
Technical Director, IPSASB
International Public Sector Accounting Standards Board
277 Wellington St. West
Toronto, ON M5V 3H2

Dear John Stanford:

RE: IPSASB Exposure Draft 64: Leases

Thank you for the opportunity to provide comments on the exposure draft titled "Leases". The views expressed in this letter reflect the views of the Government of the Province of British Columbia, including central agencies, ministries and entities consolidated into the British Columbia Summary Financial Statements.

The Summary Financial Statements of the Province are prepared in accordance with Canadian Public Sector Accounting Board (PSAB) standards. We have a particular interest in the development of IPSASB's guidance as it may influence future PSAB standards.

Consideration of users of financial statements

We are encouraged by the proposed right-of-use model as it provides users with useful information. Our government is committed to transparency and accountability in our reporting and recognition of the right-of-use asset and associated liability is consistent with this requirement. Reporting certain operating leases on the statement of financial position may give users a better understanding of the financial impacts of leasing arrangements for the lessee. A right-of-use model has the potential for better understandability in distinguishing between a lease and the sale of an asset in the lessor's financial statements. A consistent treatment for lessors and lessees as proposed by this model could lead to simplified consolidation within the Government Reporting Entity (GRE).

However, we are concerned that right-of use assets may introduce ambiguity in the definition of assets. The usefulness of the information provided from this model is dependent on whether the creation of a right-of-use asset clearly meets the definition of an asset under generally accepted accounting standards. We are also concerned that from a cost-benefit perspective, the administrative costs associated with this added reporting requirement may exceed the benefits to our users, specifically, the exercise of analysing and updating existing leases if the standard requires retroactive adoption.

Accountability for substance of the transaction

Moving away from the current accounting of operating lease financing will be a significant change for the entities within our GRE. Despite these challenges, our government is committed to transparency in our financial reporting and clarifying financing obligations and accountability for the associated assets under lease will meet this mandate. We continue to believe the best representation of the substance of a transaction will come from consistent application of the definition of assets and liabilities.

Responses to specific questions posed in the consultation paper are attached. Should IPSASB have any comments or questions, please contact me at: 250 387-6692 or via e-mail: Carl.Fischer@gov.bc.ca, or Diane Lianga, A/Executive Director, Financial Reporting and Advisory Services Branch, at 778 698-5428 or by e-mail: Diane.Lianga@gov.bc.ca.

On behalf of the Government of British Columbia,

Sincerely,



Carl Fischer, CPA, CGA
Comptroller General
Province of British Columbia

Encl.

cc: Diane Lianga, A/Executive Director
Financial Reporting and Advisory Services
Office of the Comptroller General

Specific Matters for Comment

Specific Matter for Comment 1:

The IPSASB decided to adopt the IFRS 16 right-of-use model for lessee accounting (see paragraphs BC6–BC8 for IPSASB’s reasons). Do you agree with the IPSASB’s decision? If not, please explain the reasons. If you do agree, please provide any additional reasons not already discussed in the basis for conclusions.

We agree with the adoption of the right-of-use model for lessee accounting when the right-of-use assets and corresponding liabilities meet the definitions of assets and liabilities in currently accepted standards. Many organizations within the Province of BC’s reporting entity have no intention on retaining and holding the underlying leased asset, so clarity in the standard may be useful to avoid ambiguity.

The right-of-use model suggests that the current accounting treatment is failing to report the substance of the transaction for leasing arrangements; however, there is no evidence of this in the basis for conclusions. Both capital and operating models could be valid, and the choice of which to use should best reflect the substance of the transaction.

Specific Matter for Comment 2:

The IPSASB decided to depart from the IFRS 16 risks and rewards model for lessor accounting in this Exposure Draft (see paragraphs BC9–BC13 for IPSASB’s reasons). Do you agree with the IPSASB’s decision? If not, please explain the reasons. If you do agree, please provide any additional reasons not already discussed in the basis for conclusions.

We do not agree with the departure from IFRS 16 risks and rewards model for lessor accounting. IFRS has demonstrated that the existing lessor accounting was “generally accepted,” so they retained it. There is no evidence that suggests that the preparer and user communities of government financial statements believe that lessor accounting is not currently meeting their reporting needs. Symmetrical accounting between the lessor and lessee within the government does streamline financial reporting, but should only be appropriate as long as the substance of the transaction is reflected.

Specific Matter for Comment 3:

The IPSASB decided to propose a single right-of-use model for lessor accounting consistent with lessee accounting (see paragraphs BC34–BC40 for IPSASB’s reasons). Do you agree with the requirements for lessor accounting proposed in this Exposure Draft? If not, what changes would you make to those requirements?

We do not agree with the proposed single right-of-use model for lessor accounting. The basis for conclusions states that the existing “risk and rewards ownership model” (in IPSAS 13 and in IFRS 16 lessor accounting) is not based on control; however, the IPSAS conceptual framework 5.6 defines control as “the ability to use the resource so as to derive the benefit of the service potential or economic benefit”. We do not see any significant difference between the existing risk and rewards model and the IPSAS conceptual framework 5.6. As the substance of the transaction has not changed, it is difficult to agree with the decision for the lessor to not derecognize the underlying asset because it is easier for

Specific Matters for Comment

users to understand that when a government leases assets to external entities, those assets are no longer available to the government, therefore reducing the tangible capital assets in the financial statements.

The proposed guidance is not clear on where control over the asset lies. We highlight the following statements regarding the control aspect:

- AG48 states, “Obtaining legal title does not in itself determine how to account for the transaction.”
- BC9 states, “Transactions that do transfer control are sales or purchases within the scope of other standards (for example IPSAS 9).”
- IPSAS 9 says that revenue should be recognized when the entity has transferred the “significant risks and rewards of ownership.”
- BC88 states that a lease is “in substance a sale of an unrecognized right-of-use asset,” implying that control does change hands.

If legal title does not define control, and the characteristics of finance leases or sales transactions do not define control, further guidance is required to identify the control point in a transaction. One of the key qualitative characteristics of the financial statements is that the statements are reliable by representing the substance of the transaction rather than its legal form. Our concern with the right-of-use model is that it represents the transaction based on its legal form (ownership of asset) rather than the substance of transaction (leasing).

Specific Matter for Comment 4:

For lessors, the IPSASB proposes to measure concessionary leases at fair value and recognize the subsidy granted to lessees as a day-one expense and revenue over the lease term consistent with concessionary loans (see paragraphs BC77–BC96 for IPSASB’s reasons). For lessees, the IPSASB proposes to measure concessionary leases at fair value and recognize revenue in accordance with IPSAS 23 (see paragraphs BC112–BC114 for IPSASB’s reasons). Do you agree with the requirements to account for concessionary leases for lessors and lessees proposed in this Exposure Draft? If not, what changes would you make to those requirements?

We agree that a concessionary lease receivable is similar in nature to a concessionary loan receivable.

Other Matters

Consideration of users of financial statements

We are encouraged by the proposed right-of-use model as it provides users with useful information. Our government is committed to transparency and accountability in our reporting and recognition of the right-of-use asset and associated liability is consistent with this requirement. Reporting certain operating leases on the statement of financial position may give users a better understanding of the financial impacts of leasing arrangements for the lessee. A right-of-use model has the potential for better understandability in distinguishing between a lease and the sale of an asset in the lessor's financial statements. A consistent treatment for lessors and lessees as proposed by this model could lead to simplified consolidation within the Government Reporting Entity (GRE).

However, we are concerned that right-of use assets may introduce ambiguity in the definition of assets. The usefulness of the information provided from this model is dependent on whether the creation of a right-of-use asset clearly meets the definition of an asset under generally accepted accounting standards. We are also concerned that from a cost-benefit perspective, the administrative costs associated with this added reporting requirement may exceed the benefits to our users, specifically, the exercise of analysing and updating existing leases if the standard requires retroactive adoption.

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In addition to our replies to the Specific Matters for Comment, we have the following other comments:

- AG24, which appears to contradict AG19 (b) (i). You can consider predetermined decisions in either of AG19(b)(i) or (ii), but AG24 then restricts it:
 - AG24: “unless the conditions in paragraph AG19 (b) (ii) exist, an entity shall not consider decisions that are predetermined before the period of use.”
- AG32 is unclear about whether the entity making the assessment about the lessee is the lessor or the lessee. If it refers to the lessor we do not see how the lessor could reasonably obtain all of this knowledge about the lessee, particularly in a third party lessee. For example, determination by the lessor as to the underlying assets importance to the lessee's operations.
- We do not agree that a cancellation clause (AG37) related to appropriations should only be considered if there is reasonable uncertainty that the appropriation will not be made. Governments retain the discretion to authorize appropriations in future years. As long as this discretion exists, no assets or liabilities should be recorded.