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BUILT BY ACCOUNTANTS FOR ACCOUNTANTS

# ASC 842, IFRS 16, and GASB 87: The New Lease Accounting Standards

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LeaseQuery  
ASC 842 & IFRS 16  
Transition Guide  
12 Steps to Help You  
Comply with Confidence

# Agenda

- 01** | Understanding Leases
- 02** | Review of Previous Standard
- 03** | Overview of the New Lease Accounting Standards
- 04** | Impact of the Changes (ASC 842, IFRS 16, GASB 87)

What is in Scope?

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# Understanding a Lease

# What is a Lease?

## ASC 842

contract, or part of a contract, that conveys the right to control the use of identified property, plant or equipment (an identified asset) for a period of time in exchange for consideration [ASC 842-10-15-3]

## IFRS 16

A contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration [IFRS 16:9]

## GASB 87

contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction. [GASB No. 87, Paragraph 4]

CONTROL



ASC 842

IFRS 16

## Defining Control

1

The right to obtain *substantially all of the economic benefits* from use of the identified asset

2

The right to *direct the use* of the identified asset



GASB 87

## Defining Control

1

The right to obtain the *present service capacity* from use of the underlying asset as specified in the contract

2

The right to *determine the nature and manner of use* of the underlying asset as specified in the contract.



## Scope – Topic 842

Within Scope	Scope with Exceptions	Outside Scope
<ul style="list-style-type: none"><li>• Leases of assets</li><li>• Subleases</li></ul>	<ul style="list-style-type: none"><li>• Service contracts</li><li>• Short-term leases (less than or equal to 12 months with no purchase option)</li></ul>	<p>Leases of:</p> <ul style="list-style-type: none"><li>• Intangibles</li><li>• Natural resources and exploration (i.e. oil, gas, minerals, etc.)</li><li>• Biological assets</li><li>• Inventory</li><li>• Assets under construction</li></ul>

## Scope – IFRS 16

Within Scope	Scope with Exceptions	Outside Scope
<ul style="list-style-type: none"> <li>• Leases of assets</li> <li>• Subleases</li> </ul>	<ul style="list-style-type: none"> <li>• Service contracts</li> <li>• Short-term leases (less than or equal to 12 months with no purchase option)</li> <li>• Low value leases</li> </ul>	<p>Leases of:</p> <ul style="list-style-type: none"> <li>• Intangibles</li> <li>• Natural resources and exploration (i.e. oil, gas, minerals, etc.)</li> <li>• Biological assets</li> <li>• Service Concession Arrangements</li> <li>• Licenses of intellectual property granted by a lessor</li> <li>• rights held by a lessee under licensing agreements</li> </ul>

## Scope – GASB 87

Within Scope	Scope with Exceptions	Outside Scope
<ul style="list-style-type: none"> <li>• Nonfinancial assets (i.e. land, buildings, equipment, vehicles)</li> <li>• Sublease</li> </ul>	<ul style="list-style-type: none"> <li>• Leases with service components</li> <li>• Short-term leases (less than or equal to 12 months with no options)</li> <li>• Intangibles</li> </ul>	<p>Leases of:</p> <ul style="list-style-type: none"> <li>• Intangibles assets: Natural resources and exploration (i.e. oil, gas, minerals, etc.)</li> <li>• Biological assets</li> <li>• Inventory</li> <li>• Service concession arrangements</li> <li>• Supply Contracts</li> <li>• Leases financed with conduit debt</li> </ul>

# Comparison Chart

	ASC 842	IFRS 16	GASB 87
Control	the right to obtain <i>substantially all</i> of the economic benefits from use of the identified asset AND The right to <i>direct the use</i> of the identified asset	the right to obtain <i>substantially all</i> of the economic benefits from use of the identified asset AND The right to <i>direct the use</i> of the identified asset	The right to obtain the <i>present service capacity</i> from use of the underlying asset as specified in the contract AND The right to <i>determine the nature and manner of use</i> of the underlying asset as specified in the contract
Short Term lease	less than or equal to 12 months, with no purchase option	less than or equal to 12 months, with no purchase option	less than or equal to 12 months with no options
Low Value	No exception	\$5,000	No exception

- A tenant enters into a 7-year lease for office space in which it has exclusive use of the 6<sup>th</sup> floor.
  - ✓ ASC 842
  - ✓ IFRS 16
  - ✓ GASB 87
- A tenant enters into a 5-year lease for a building in which it has exclusive use of the building for 4 days, except Fri, Sat, & Sun. (*On the weekends the building is occupied by another tenant*)
  - ✗ ASC 842
  - ✗ IFRS 16
  - ✓ GASB 87
- A lessee enters into an agreement with a lessor for equipment worth \$500,000. According to the terms of the agreement, the lessee will pay \$5 each month over the course of 5 years.
  - ✓ ASC 842
  - ✓ IFRS 16
  - ✗ GASB 87

What's Changing?

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# Overview of the New Lease Accounting Standards

# What's Changing?

- All leases will be classified on the **Balance Sheet**
  - more accurate representation of lessees' assets and liabilities
  - greater transparency about the lessee's obligations and activities
- New **Disclosures**

# Previous Standards: Lease Classification

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1. **Ownership** - Does ownership transfer to the lessee at the end of the term?
2. **Bargain Purchase Option** - Is there an option to purchase the leased item for a bargain ( typically \$1) at the end of the lease term?
3. **Lease term** - the lease period is greater than or equal to 75% of the useful life of the asset
4. **Present Value** - PV of minimum lease payment is greater than 90% of the Fair Value of the leased item.



# Impact of Changes

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# ASC 842

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## Nomenclature

- ❖ Operating lease
- ❖ Finance lease

1. **Ownership** - Does ownership transfer to the lessee at the end of the term?

2. **Bargain Purchase Option** - Is there an option to purchase the leased item for a bargain (typically \$1) at the end of the lease term?

3. **Lease term** - the lease term is a *major part* of the remaining economic life of the asset

4. **Present Value** - PV of minimum lease payment and residual value guaranteed by the lessee equals or exceeds *substantially all* of the Fair Value

5. **Specialized Use** – asset has no alternative use to the lessor at the end of the lease term

# IFRS 16

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## Nomenclature

- ❖ Finance lease

“IFRS 16 eliminates the classification of leases as either operating leases or finance leases for a lessee. Instead all leases are treated in a similar way to **finance leases** applying IAS 17. Leases are ‘capitalised’ by recognizing the present value of the lease payments and showing them either as lease assets (right-of-use assets) or together with property, plant and equipment.”

# GASB 87

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## Nomenclature

### ❖ Finance lease

“The accounting and financial reporting guidance for leases in this Statement is based on the foundational principle that **leases are financings**. In a lease transaction, a lessee receives the legal right to use an underlying asset (the asset that is subject to the lease, such as a vehicle or building) at the commencement of the lease term. In exchange, the lessee promises to make payments over time for the right to use that underlying asset. Therefore, the lessee has financed the acquisition of that legal right.”

## Balance Sheet Impact



**Lease  
Liability**

**ROU  
Asset**

# Lease Liability

## QUICK TIP

- 1) Rate Implicit in the Lease
  - 2) Incremental Borrowing rate
- \*\*Nonpublic entities can elect the risk free rate**



- present value of the **lease payments** not yet paid, discounted using the **discount rate for the lease** at lease commencement, including:

- Fixed Payments (including in-substance fixed) less any incentives
- Variable payments that depend on an index or rate (i.e. CPI)
- The exercise price of a purchase option if reasonably certain to be exercised
- Payments of penalties for terminating a lease
- Fees paid by the lessee to the owners of a special-purpose entity for structuring the transaction
- Amounts it is probable the lessee will owe under residual value guarantees
- Any other payments reasonably certain of being required



## Comparison Chart

	ASC 842	IFRS 16	GASB 87
Lease classification	Operating Lease Finance Lease	Finance Lease	Finance Lease
Lease Liability			
Treatment of payments w/ index/rate	initially measured using the index or rate as of the commencement of the lease term	initially measured using the index or rate as of the commencement of the lease term, and <b>reassess liability upon change</b>	initially measured using the index or rate as of the commencement of the lease term

## ROU Asset

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- measured including the following:
  - amount of the initial measurement of the **lease liability**
  - Any **lease payments** made to the **lessor** at or before the commencement date, minus any lease incentives received
  - Any **initial direct costs** incurred by the **lessee**
  - estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset



# Comparison Chart

	ASC 842	IFRS 16	GASB 87
<b>Lease classification</b>	Operating Lease Finance Lease	Finance Lease	Finance Lease
<b>Lease Liability</b>			
Treatment of payments w/ index/rate	initially measured using the index or rate as of the commencement of the lease term	initially measured using the index or rate as of the commencement of the lease term, and reassess liability upon change	initially measured using the index or rate as of the commencement of the lease term
<b>ROU Asset</b>			
Specifics	Same	estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset	Same

## Income Statement Impact



**Operating  
Expense**

**Interest  
Expense**

# Comparison Chart

	ASC 842	IFRS 16	GASB 87
<b>Lease classification</b>	Operating Lease Finance Lease	Finance Lease	Finance Lease
<b>Operating Expense – Operating Lease Liability</b>			
Rent Expense	Recognize lease costs on a straight-line basis	None	None
<b>Interest Expense – Finance Lease Liability</b>			
	Interest on lease liability based on the rate determined in the lease	Interest on lease liability based on the rate determined in the lease	Interest on lease liability based on the rate determined in the lease

## Comparison Chart

	ASC 842	IFRS 16	GASB 87
Lease classification	Operating Lease Finance Lease	Finance Lease	Finance Lease
Operating Expense – ROU Asset/Lease Asset			
Depreciation	Amortize the ROU asset on a straight-line basis	Amortize the ROU asset on a straight-line basis	Amortize in a systematic and rational manner

# Thank you.

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