



FRS 116 Leases

ZOOM TALK ON 11 SEPTEMBER 2020





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FRS 116: Introduction

- FRS 116 issued on 30 June 2016
- To supersede FRS 17, INT FRS 15, INT FRS 27, INT FRS 104
- Effective date: 1 January 2019



FRS 116: Introduction

➤ Basic changes:

- Lease accounting: “Purchase or rent” vs “Right of use” model
- FRS 17:
 - “Purchase or rent” model for both Lessee and Lessor
- FRS 116:
 - “Right of use” model for Lessee
 - “Purchase or rent” model for Lessor



FRS 116: Introduction

- Under “ROU” model, FRS 116 requires lessee to capitalize all leases
 - except (i) short term leases and (ii) leases with low value underlying asset
- No major changes for lessor



FRS 116: Introduction

❖ Balance Sheet

- “Right of use” asset, and
- Lease liability

❖ Income Statement

- Depreciation expense, and
- Interest expense

❖ Cash Flow

- Principal payment: financing;
- Interest payment: operating/ financing



FRS 116: Definition

➡ Definition of lease:

- A contract that conveys the right to use an asset for a period of time in exchange for consideration
- Two important elements
 - There is an identified asset; and
 - Customer controls the use of the asset



FRS 116: Definition

- ❖ 1. There is an identified asset when:
 - 1.1 the asset is explicitly specified in the contract, and
 - 1.2 the supplier does not have a substantive right (practical ability and economic benefits) to substitute the asset throughout the period of use

- ❖ 2. Customer controls the use of the asset when the customer has the right to:
 - 2.1 obtain substantially all the economic benefits from the use of the asset throughout the period of use, and
 - 2.2 direct the use of the asset throughout the period



FRS 116: Lessee Accounting: Initial recognition & measurement

■ Initial recognition and measurement

- On commencement date, lessee should recognize (i) "Right of use" asset and (ii) lease liability
 - = pv of lease payments discounted using the implicit rate (if known), else lessee's incremental borrowing rate



FRS 116: Lessee Accounting: Initial recognition & measurement

- “Lease payments” for lease liability comprises
 - ❑ Fixed lease payments
 - ❑ Variable lease payments
 - ❑ Amount expected to pay under Guaranteed Residual Value (GRV)
 - ❑ Option exercise price (reasonably certain)



FRS 116: Lessee Accounting: Initial recognition & measurement

- “Lease payments” for Right of use comprises
 - ❑ Lease payments for lease liability
 - ❑ Less lease incentive
 - ❑ Add initial direct cost
 - ❑ Add dismantlement costs



FRS 116: Lessee Accounting: Initial recognition & measurement

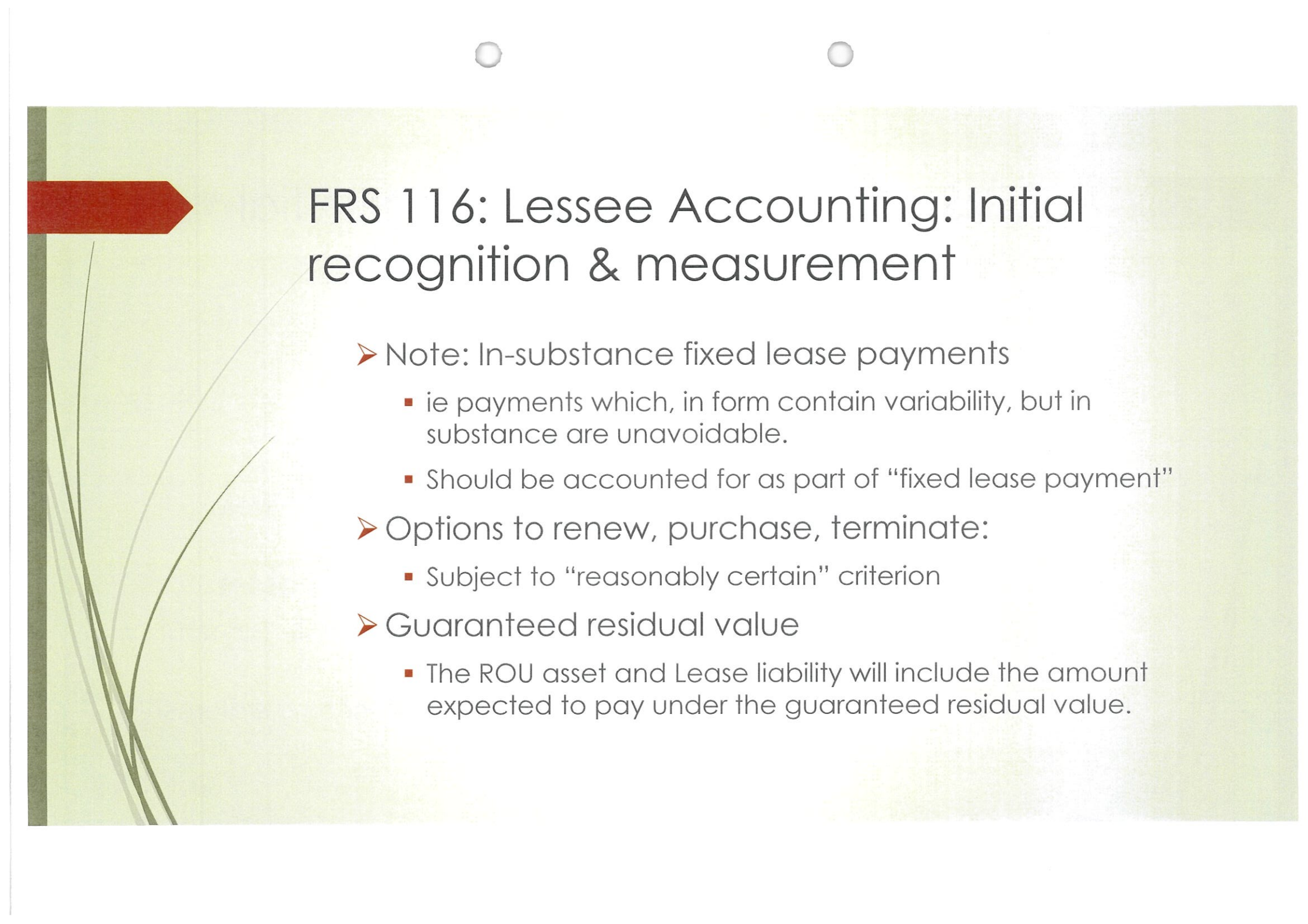
- For Lessor, “lease payments” do not include payment for non-lease components (eg administrative, repair and maintenance, etc)
- For Lessee, “lease payments” do not include payment for non-lease components (eg administrative, repair and maintenance, etc). However, as practical expedient, lessee may choose to account for the payment for non-lease components as part of the lease.



FRS 116: Lessee Accounting: Initial recognition & measurement

➤ Variable lease payments:

- Depend on index:
 - ☐ Use the index at commencement date
 - ☐ Subsequent change accounted for prospectively
- Linked to future performance or use of asset
 - ☐ Not accounted for at commencement date (do not meet definition of liability-FRS37)
 - ☐ Any additional payment charged to Income Statement when incurred



FRS 116: Lessee Accounting: Initial recognition & measurement

- Note: In-substance fixed lease payments
 - ie payments which, in form contain variability, but in substance are unavoidable.
 - Should be accounted for as part of “fixed lease payment”
- Options to renew, purchase, terminate:
 - Subject to “reasonably certain” criterion
- Guaranteed residual value
 - The ROU asset and Lease liability will include the amount expected to pay under the guaranteed residual value.



FRS 116: Lessee Accounting: Subsequent measurement

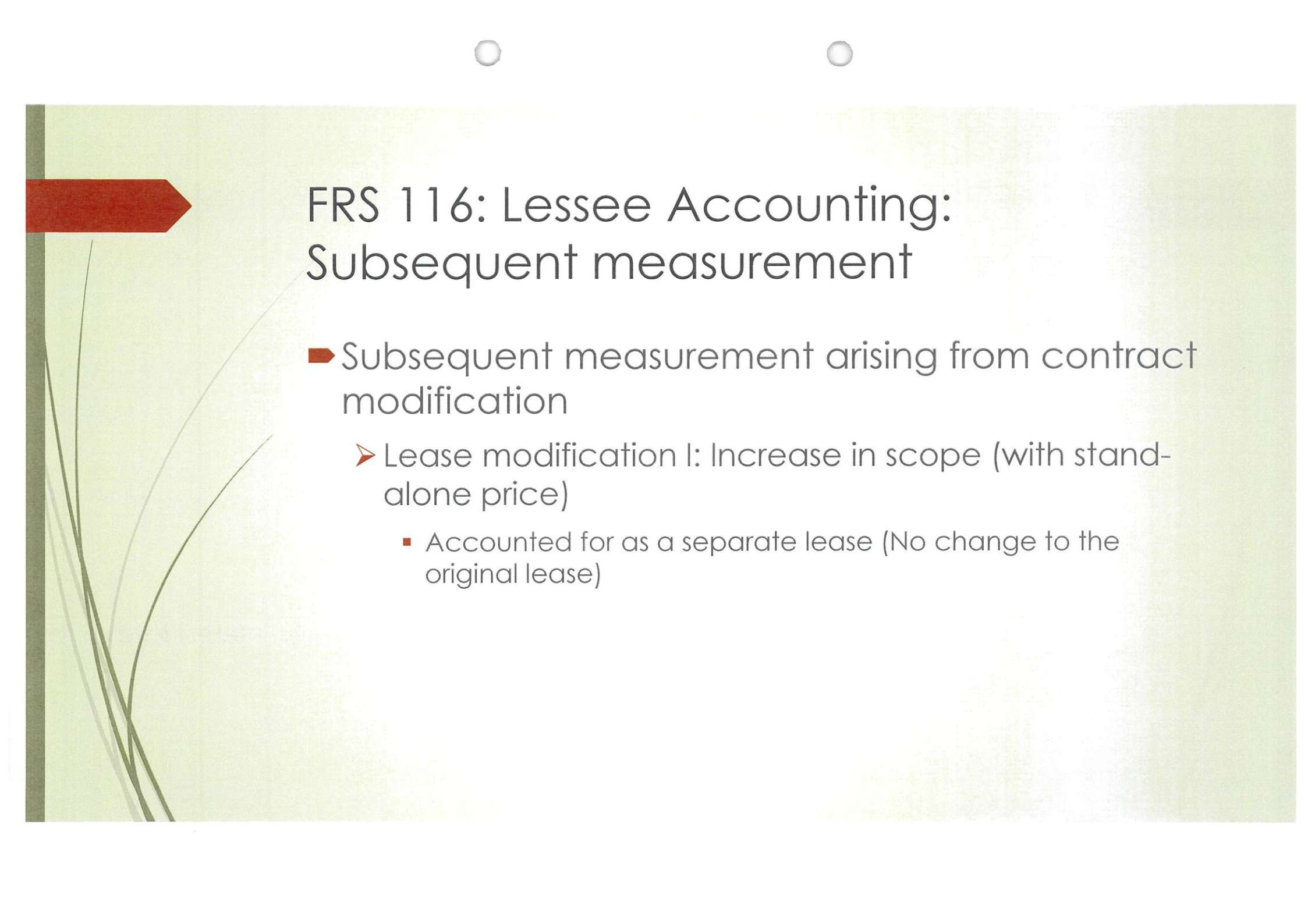
■ Subsequent measurement

➤ Right of use asset

- May apply cost model or revaluation model of FRS16
- (If ROU asset accounted for as Investment property, apply FRS 40)

➤ Lease liability

- Increased by interest (calculated using effective interest rate method)
- Reduced by lease payment



FRS 116: Lessee Accounting: Subsequent measurement

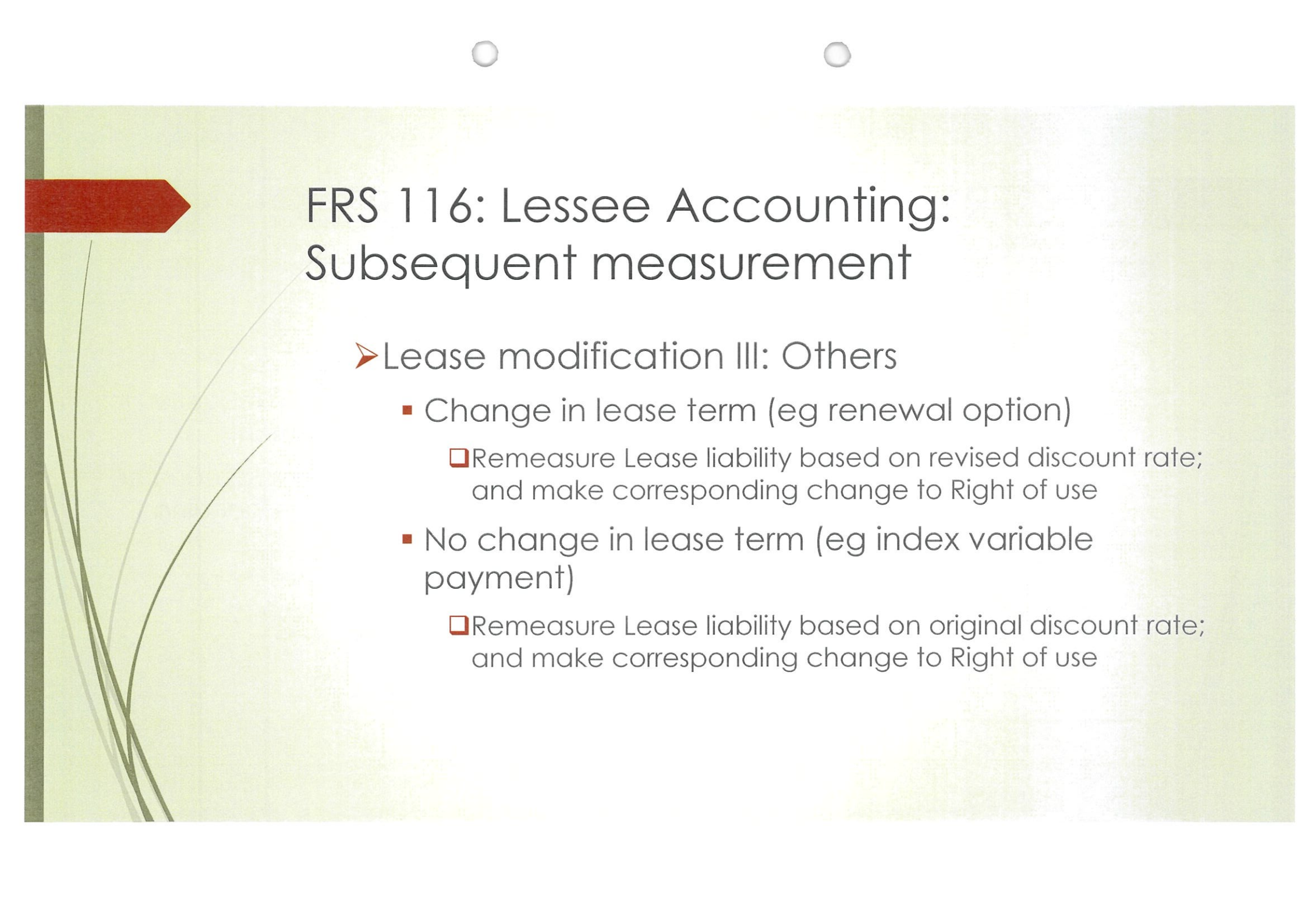
- Subsequent measurement arising from contract modification
 - Lease modification I: Increase in scope (with stand-alone price)
 - Accounted for as a separate lease (No change to the original lease)



FRS 116: Lessee Accounting: Subsequent measurement

➤ Lease modification II: Decrease in scope

- Proportionately reduce LL and ROU to reflect the reduction in scope, any difference charge to Income Statement
- Re-measure LL (based on revised lease payments discounted using the revised discount rate), and make corresponding adjustment to ROU



FRS 116: Lessee Accounting: Subsequent measurement


➤ Lease modification III: Others

- Change in lease term (eg renewal option)
 - ❑ Remeasure Lease liability based on revised discount rate; and make corresponding change to Right of use
- No change in lease term (eg index variable payment)
 - ❑ Remeasure Lease liability based on original discount rate; and make corresponding change to Right of use



FRS 116: Lessee Accounting: Exemptions

- For (i) short term leases and (ii) leases with low value underlying asset
 - Lessee may elect to recognize lease payments as expense (ie accounted for as operating lease)
 - Short term lease
 - A lease that, at the commencement date, has a lease term of 12 months or less (and does not contain a purchase option)



FRS 116: Lessee Accounting: Exemptions

- Leases with low value underlying asset (general guide)
 - Asset with a value, when new, in the order of magnitude of US\$5,000 or less
 - Small items of office furniture or equipment
 - Not highly dependent on or highly interrelated to other underlying assets
 - Cannot sublease
 - Election done on lease-by-lease basis



FRS 116: Lessor Accounting

- As per FRS 17

- Operating leases and finance leases

- ❑ Same test

- ❑ Same accounting treatment

- ❑ Enhanced disclosure: additional qualitative and quantitative information about the leasing activities



FRS 116: Transitions

- Transition from “FRS17 Operating lease” to “FRS116 Lease”, lessee may choose to transit using one of the following two methods:
 - Retrospectively to each prior reporting period presented
 - Retrospectively with cumulative effect recognized as an adjustment to Beginning retained profits of the annual reporting period that begins as the date of initial application

FRS 116: Transitions

➡ Under the restricted retrospective method, a lessee may choose

➤ (a):

- Recognise lease liability = pv of the **remaining lease payments** discounted using the lessee's incremental borrowing rate (IBR) at the date of initial application
- Recognise ROU asset = pv of **all lease payment** from commencement date but discounted using the lessee's IBR at the date of initial application, less accumulated depreciation
- The difference between ROU and LL adjusted to Beginning retained profits



FRS 116: Transitions

➡ Under the restricted retrospective method, a lessee may choose (*cont'd*)

➤ (b):

- Recognise ROU asset and LL = pv of the **remaining lease payments** discounted using the lessee's incremental borrowing rate at the date of initial application
- (Prepayment/accrued lease payments, if any, adjusted against ROU asset)



Example

- Tenancy agreement for office premise
- Lease term: From 15 Sep 2017 to 14 Sep 2022 (5 years)
- Lease payment: S\$20,000 per month
- Discounting rate: 5.50%
- Financial year end: 31 December 2019



Amendment to FRS116: Covid-19 related rent concession (Issued: 28 May 2020; Effective date: 1 Jun 2020)

- A practical expedient allows lessees to elect not to carry out an assessment to decide whether a Covid-19-related rent concession received is a lease modification. The lessee is permitted to account for the rent concession as if the change is not a lease modification.
- The practical expedient applies only to rent concessions
 - **(1)** occurring as a direct consequence of Covid-19 & **(2)** only if **all** 3 conditions are met:
 - a) The rent concession must result in lease payments that are substantially the same or less than the original consideration for the lease immediately before the concession was provided.
 - b) Any reduction in lease payments affects only payments originally due on or before 30 June 2021. (Eg.- No rental for nine months from 1 Oct 2020 to 30 Jun 2021 but increased rental from 1 Jul 2021 onward)
 - c) There is no substantive change to other terms and conditions of the lease.



Thank you!

