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Out with the old and in with the new. The new – and hopefully improved – lease accounting standard from the International Accounting Standard Board (IASB) changes the way leases affect reported financial metrics as IAS 17 is replaced by IFRS 16. Operating leases have long appealed to businesses for their ability to avoid recognising assets and liabilities on financial statements. Now, after a decade of deliberation, there is a new IFRS accounting standard for leasing that brings these figures onto the balance sheet. What exactly does that mean, though? How does IFRS 16 differ from IAS 17? This lease accounting article should help clear things up, as we take a look at IAS 17 vs IFRS 16.

IFRS 16 Summary The most obvious and impactful difference is how operating leases will be brought onto the balance sheet. Under IAS 17, a lessee is not obligated to report assets and liabilities from operating leases on their balance sheet and they are instead referred to in the footnotes. This has typically provided financial statement users an inaccurate account of a company's outstanding expenses, forcing them to estimate the off-balance sheet obligations, which often results in overstatement. Similarly, it is difficult to compare businesses that lease assets with those that own them as a clear indication on the operating leases are left out of the equation. IFRS 16 changes this by requiring a lessee to recognise arising right of use (ROU) assets and lease liabilities on their balance sheet. Undoubtedly one of the biggest changes to leases accounting, the consequences of recognising operating leases will see a large difference in various financial metrics. See more: IFRS 16 Overview and Lease Accounting Summary IFRS 16 vs IAS 17

Operating lease accounting treatment IAS 17 - Operating leases off-balance sheet as a single expense. Finance leases on balance sheet IFRS 16 - Operating leases recognise assets and liabilities on balance sheet. Operating leases to report depreciation and interest separately. Why the difference? Improved comparability and transparency on balance sheet. Financial statement users can clearly see the effect of operating leases and have a useful basis for comparability with other companies. Currently, under IAS 17, it is difficult to compare companies who lease with those who buy. Potential impacts: Financial report impact – As operating leases will be capitalised, there will be a shift in financial metrics for businesses that have a particularly large number of this type of lease. Asset turnover, equity and operating expenses will likely see a decrease. Conversely, liabilities, reported debt, recorded assets, EBIT and EBITDA will all see an increase. Covenants and shareholder relationships – With a change in financial metrics, ratios and liabilities, companies will need to take extra care with their disclosures to explain the shift figures. This could lead to a possible breach of financial based agreements and contracts, both internally (performance KPIs and metric based compensation payments/bonuses) and externally (bank covenants, stakeholder relationships, investor relationships). Definition of a lease IAS 17 - Focus on whether lessor or lessee carries the risk and reward. Both lease and non-lease components accounted off balance sheet. IFRS 16 - More focus on who controls the ROU asset, linking with IFRS 15. Non-lease components still excluded, but lease components will need to be reported on. Why the difference? – Another change in lease classification affects accounting treatment. Lease agreements as IFRS 16 contain a new lease definition. The actual wording of the definition in IFRS 16 does not change too much from the IAS 17 one. However, there is a greater emphasis and weight surrounding how lease differs from a service. This is aimed at improving the comparability of financial statements, capturing useful material information on leases rather than additional components. Potential impacts - Lessees are required to identify and separate non-lease components (i.e., services components such as maintenance) to ensure only the necessary ones are accounted for on balance sheet. This means that Non-lease components will receive an increased focus in negotiation phases and their separation from a lease is more important. However, IFRS 16 does permit an accounting policy election (the practical expedient), whereby lessees can recognise the lease and non-lease comment as a 'single lease component' on the balance sheet. If lessees choose to utilise this election, this would in effect, increase the lease obligations stated on balance sheet. (Note, if this expedient is adopted, lessees are not permitted to account for the combined lease and non-lease component as a 'service'). Lessor interaction Lessor accounting remains largely unchanged under IFRS 16. However, with operating leases losing their off-balance sheet accounting treatment, the types of agreements lessees favour may shift, as companies focus more on the operational benefits of leasing over accounting ones. Lessors typically use operating leases as a tool to price more competitively. IAS 17 - Focus on lease type from an operational perspective. Many lessees used operating leases to avoid balance sheet recognition. Others prefer the reduced risk and reward, as well as the competitive pricing that operating leases offer. IFRS 16 - Lease type has a lower impact from an accounting standpoint, however, a greater focus is placed upon on the deal types that can be negotiated. Why? – Although lease accounting is removing the operating lease and finance lease classification for lessees, lessor accounting remains largely unchanged and the operational differences between operating leases and finance leases remain. Businesses may look for more inventive ways to lease to continue to get the most out of their assets. Potential Impacts – Buy vs. lease becomes a more important decision if you rely on the off-balance sheet reporting capabilities of an operating lease. New types of lease arrangement may be created by lessors to keep leasing competitive. Greater focus on the operational benefits vs. accounting benefits, such as asset refresh, risk and reward etc. Accountant involvement Accounting departments will be greatly impacted by the new standard, especially in the first year of reporting. The way they interact with leasing within the company is likely to change as they need to know more information about operating leases and how their inclusion affects the financial reporting when accounting for leases under IFRS 16. IAS 17 - The accounting treatment of operating leases is less complex than the treatment of finance leases and the volume of operating leases is predominantly higher than that of finance leases. So, currently, accounting departments have a lower volume of the challenging calculations to make. IFRS 16 - Under the new standard, however, as all leases will be treated under the same accounting treatment, accounting departments will have a higher volume of complex amortisation calculations to perform. Why? – As operating leases have not needed to appear on balance sheet, accountants have had a less challenging interaction with them. The difference will be particularly for internal accountants, where the company does not have many finance leases. Potential Impact – Much greater interaction between accountants and other departments involved in leasing, mainly in the first year of application. Must ensure figures within procurement, for example, match those of the accountants. More strain on small accountancy teams, especially with IFRS 15 and IFRS 9 occurring at a similar time. Measuring PV and rate IAS 17 - Finance leased assets and liabilities are measured at the fair value of the leased property or, if lower, the PV of the minimum lease payments. The discount rate to be used in calculating the PV of the minimal lease payments is the implicit rate if known, otherwise, the lessee's borrowing rate. Any initial direct costs of the lessee are added to the value of the asset. IFRS 16 - Measures the lease liabilities at the PV of the lease payments that are not paid at the date discounted using the implicit rate if known, otherwise, the incremental borrowing rate. There is no reference to the fair value and the measurement does not relate to the minimal lease payments. Instead, the lease payments that are not paid, IFRS 16 is more specific as to the definition of the payment to be included in the measurement of the lease liability. Lease payments included in lease liability include: a) Fixed payments; b) variable lease payments dependent on an index or a rate, initially measured using the index or rate at the date of commencement; c) amortisations expected to be payable by the lessee under residual value guarantees; d) the exercise price of a purchase option if the lessee is reasonably certain to exercise the option; and e) payments of penalties for terminating the lease. The measurement of leased assets differs to IAS 17 whereby any lease incentives received may be deducted and lease payments made at or before commencement date may be added; as too can an estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset, restoring the underlying asset to the condition required by the terms and conditions of the lease. Why the difference? – One of the main aims of IFRS 16 is to provide a consistent view of lease obligations in financial statements. To achieve this, the definitions of the leased asset and liability measures need to be specifically defined to ensure a consistent measurement approach. Potential Impact – The biggest impact is in the measurement of operating lease liabilities and assets which did not previously have to be performed. This can be an onerous task and the data collation exercise is key to ensuring all relevant measurement components are captured before the measurement and recording task can begin. Disclosures IAS 17 - Disclosures cover the specific requirement of finance leases separate from operating leases. IFRS 16 - Disclosures do away with the separate presentation of finance and operating leases for lessees and instead requires disclosures of the right of use assets and liabilities. There are also additional disclosures to specifically state whether the lessee has elected not to apply IFRS 16 to short-term and low-value leases. Specifically, disclosures are required for short-term and low-value lease express if these elections have been made, so too are variable lease payments not included in the measurement of lease liabilities. Why? – As IFRS 16 requires all the lessee leases to be shown on balance sheet, the distinction between finance and operating leases is mute. It, therefore, makes sense to redefine the disclosure requirements to give more information on the leasing activity to achieve the goal of lessees reporting on a level playing field. Potential Impact – When collating and measuring lease data it is important to bear in mind the disclosure requirements and ensure you capture the data in such a fashion to enable you to fulfil the disclosure requirement analysis with ease. To get an overview of the changes to IFRS 16 and to gain a greater understanding of the associated impacts, follow this link. If you're looking for a more comprehensive understand of the new standards and want to know what your company can do to prepare in advance, just click the link below. Warning: this article contains general information about the new lease accounting standards only, and should NOT be viewed in any way as professional advice or service. The Publisher will not be responsible for any losses or damages of any kind incurred by the reader whether directly or indirectly arising from the use of the information found within this article.

International Accounting Standard 17 (IAS 17) provides guidelines for accounting treatment and disclosures related to leases. The purpose of IAS 17 is to ensure that the lessee and lessor account for their lease transactions accurately and consistently across various reporting periods. IAS 17 applies to all leases, except for the following: Leases for mineral rights, oil, natural gas and similar non-regenerative resources. Licensing agreements for items like films, patents, copyrights, and trademarks. Leases of living animals. Leases of assets under construction. According to IAS 17, leases are classified into two types: finance leases and operating leases. The classification of a lease depends on the substance of the transaction rather than its legal form. Finance Lease A finance lease is a lease that transfers substantially all the risks and rewards incidentally to ownership of the leased asset to the lessee. According to IAS 17, a lease is classified as a finance lease if it meets one or more of the following criteria: Ownership of the asset is transferred to the lessee at the end of the lease term. The lease term covers a major part of the economic life of the asset. The present value of minimum lease payments amounts to at least substantially all of the fair value of the leased asset. The leased asset is of such a specialized nature that only the lessee can use it without significant modifications. For a finance lease, the lessee recognizes the leased asset and the lease liability in its balance sheet at the inception of the lease. The leased asset is depreciated over its useful life, and interest expense is recognized on the lease liability using the effective interest method. For an operating lease, the lessee recognizes the lease payments as an expense on a straight-line basis over the lease term. Disclosures For both finance leases and operating leases, the lessee is required to disclose the following in its financial statements: The nature of its lease arrangements. The amounts recognized in its financial statements and the basis for recognizing them. A maturity analysis of its lease liabilities. The total of future minimum lease payments under non-cancelable leases. The total of future sublease rentals expected to be received. For a finance lease, the lessor recognizes the lease receivable and unearned finance income at the inception of the lease. The lease receivable is reduced as lease payments are received, and finance income is recognized using the effective interest method. For an operating lease, the lessor recognizes lease income on a straight-line basis over the lease term. Disclosures For both finance leases and operating leases, the lessor is required to disclose the following in its financial statements: The nature of its lease arrangements. The gross investment in the lease. The unearned finance income. The future minimum lease payments under non-cancelable leases. The contingent rent receivable. The amount of any allowance for uncollectible amounts. IAS 17 provides guidance on accounting for leases and ensures consistent and accurate reporting across various reporting periods. The classification of leases, accounting treatment for lessees and lessors, and disclosures required in financial statements are all outlined in IAS 17. Q.1. What is IAS 17? IAS 17 is an International Accounting Standard that provides guidelines for accounting treatment and disclosures related to leases. Q.2. What types of leases does IAS 17 cover? IAS 17 covers all leases, except for leases for mineral rights, oil, natural gas, and similar non-regenerative resources, licensing agreements for items like films, patents, copyrights, and trademarks, leases of living animals, and leases of assets under construction. Q.3. How are leases classified under IAS 17? Lessees are classified into two types: finance leases and operating leases. The classification of a lease depends on the substance of the transaction rather than its legal form. Q.4. What is a finance lease? A finance lease is a lease that transfers substantially all the risks and rewards incidentally to ownership of the leased asset to the lessee. Q.5. What is an operating lease? An operating lease is a lease other than a finance lease. It does not transfer substantially all the risks and rewards incidentally to ownership of the leased asset to the lessee. Q.6. What is the accounting treatment for lessees under IAS 17? For a finance lease, the lessee recognizes the leased asset and the lease liability in its balance sheet at the inception of the lease. The leased asset is depreciated over its useful life, and interest expense is recognized on the lease liability using the effective interest method. For an operating lease, the lessee recognizes the lease payments as an expense on a straight-line basis over the lease term. Q.7. What disclosures are required for lessees under IAS 17? For both finance leases and operating leases, the lessee is required to disclose the nature of its lease arrangements, the amounts recognized in its financial statements and the basis for recognizing them, a maturity analysis of its lease liabilities, the total of future minimum lease payments under non-cancelable leases, and the total of future sublease rentals expected to be received. Q.8. What is the accounting treatment for lessors under IAS 17? For a finance lease, the lessor recognizes the lease receivable and unearned finance income at the inception of the lease. The lease receivable is reduced as lease payments are received, and finance income is recognized using the effective interest method. For an operating lease, the lessor recognizes lease income on a straight-line basis over the lease term. Q.9. What disclosures are required for lessors under IAS 17? For both finance leases and operating leases, the lessor is required to disclose the nature of its lease arrangements, the gross investment in the lease, the unearned finance income, the future minimum lease payments under non-cancelable leases, the contingent rent receivable, and the amount of any allowance for uncollectible amounts. Q.10. Why is IAS 17 important? IAS 17 is important as it provides a standardized framework for accounting treatment and disclosures related to leases. It ensures that lessees and lessors account for their lease transactions accurately and consistently across various reporting periods. Future Connect Training's Management Accounts training can help in understanding IAS 17 in several ways. Here are some of them: Understanding basic accounting principles: The Management Accounts training program covers basic accounting principles that form the foundation of financial reporting. Having a solid understanding of these principles can help individuals comprehend the concepts and requirements of IAS 17 more easily. Understanding the classification of leases: IAS 17 requires leases to be classified into finance leases and operating leases. The Management Accounts training program can help individuals understand the differences between the two types of leases, including the criteria used to classify them. Understanding the accounting treatment for lessees: IAS 17 provides specific accounting treatment for lessees, including the recognition of leased assets and lease liabilities, depreciation of leased assets, and recognition of interest expenses. The Management Accounts training program can help individuals understand these accounting treatments and how they are applied in practice. Understanding disclosures: IAS 17 requires both lessees and lessors to disclose specific information related to their lease arrangements. The Management Accounts training program can help individuals understand the nature of these disclosures and how to prepare them accurately. Overall, Future Connect Training's Management Accounts training can provide individuals with a solid understanding of basic accounting principles and specific accounting treatments related to leases, which can be invaluable in understanding and applying the requirements of IAS 17. Superseded by IFRS 16 Leases. IAS 17 classifies leases into two types: a finance lease if the lease transfers substantially all the risks and rewards incidental to ownership; and an operating lease if the lease does not transfer substantially all the risks and rewards incidental to ownership. IAS 17 prescribes lessee and lessor accounting policies for the two types of leases, as well as disclosures. Leases in the financial statements of lessees—operating leases Lease payments under an operating lease are recognised as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit. Leases in the financial statements of lessors—finance leases At the commencement of the lease term, lessees recognise finance leases as assets and liabilities in their statements of financial position at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. Any initial direct costs of the lessee are added to the amount recognised as an asset. Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents are charged as expenses in the periods in which they are incurred. A finance lease gives rise to depreciation expense for the recognised lease assets as well as finance expense for each accounting period. Leases in the financial statements of lessors—operating leases Lessors present assets subject to operating leases in their statements of financial position according to the nature of the asset. Lessors depreciate the leased assets in accordance with IAS 16 and IAS 38. Lease income from operating leases is recognised in income on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which the benefit derived from the leased asset is diminished. Leases in the financial statements of lessors—finance leases Lessors recognise assets held under a finance lease in their statements of financial position and present them as a receivable at an amount equal to the net investment in the lease. The recognition of finance income is based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease. Manufacturer or dealer lessors recognise selling profit or loss in accordance with the policy followed by the entity for outright sales. This article is relevant to Papers F7 and P2 Complex lease terms mean that it is often difficult to determine how they should be classified. This article examines IAS 17 and sheds some light on the matter: Leases are classified currently under IAS 17. Leases, as finance or operating leases at inception, depending on whether substantially all the risks and rewards of ownership transfer to the lessee. Under a finance lease, the lessee has substantially all of the risks and reward of ownership. Situations that would normally lead to a lease being classified as a finance lease include the following: the lease transfers ownership of the asset to the lessee by the end of the lease term the lease term is for the major part of the economic life of the asset, even if title is not transferred at the inception of the lease, the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset and the leased asset is of a specialised nature such that only the lessee can use it without major modifications being made if the lessee is entitled to cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee gains or losses from fluctuations in the fair value of the residual fall to the lessee the lessee has the ability to continue to lease for a secondary period at a rent that is substantially lower than market rent All other leases are operating leases. The lease classification is made at the inception of the lease but a lessee and lessor may agree to change the provisions of the lease. However, changes in estimates for example, changes in the residual value of a leased property, or changes in circumstances such as default by the lessee, do not give rise to a new classification of a lease. If the changes would have resulted in a different lease classification, had they been applied originally, then the revised lease agreement is treated as a new lease over the remaining lease term. The original accounting entries are not retrospectively amended. Often lease indicators may not always point in the same direction causing lease classification to be difficult. Leases of specialised assets will usually be structured as finance leases. If an asset is specialised, then this implies that no other entity has a use for the asset. Consequently the lessor will only achieve its return on investment through the lease payments and it will structure the lease as a finance lease accordingly. If a lessor can sell or lease non-specialised assets to other parties at the end of the lease and is willing to accept the financial risk on this then this could be an indicator of an operating lease. Assets of a non-specialised may become specialised. For example, leased plant and equipment may be permanently installed in a building and its removal at the end of the lease may be impractical or too expensive for the lessor. Often specialised assets may have a significant remaining life at the end of the lease and sometimes this remaining life may be the major part of the economic life of the asset and therefore this indicator will point to it being an operating lease. However, it may be appropriate to disregard this indicator. Normally for there to be an operating lease, the lessor's net investment in the finance lease is not dependent on some future event. However, it is not an interest payment as it is not connected with the passage of time therefore time value of money is not an issue. Contingent rent is commonly connected with an increase or decrease in future sales by the lessee or increase or decrease in the use of asset or inflation or deflation. Under IAS 17, contingent rents are excluded from minimum lease payments and are accounted as expense/income in the period in which they are incurred/earned. If a lease contains a clean break clause, where the lessee is free to walk away from the lease agreement after a certain time without penalty, then the lease term for accounting purposes will normally be the period between the commencement of the lease and the earliest point at which the break option is exercisable by the lessee. If a lease contains an early termination clause that requires the lessee to make a termination payment to compensate the lessor such that the recovery of the lessor's remaining investment in the lease was assured, then the termination clause would normally be disregarded in determining the lease term. Similarly the same principle applies, if the lease agreement states that the lease can only be terminated in remote circumstances, with the permission of the lessor or on entering a new lease agreement for the same or equivalent asset. The IASB is preparing a standard that may clarify and change some of the above aspects of lease accounting. The current models lead to a lack of comparability and undue complexity because of the distinction between finance and operating leases. As a result, many users of financial statements adjust the amounts presented in the statement of financial position to reflect the assets and liabilities arising from operating leases which makes the deliberations of companies regarding classification of leases somewhat a futile exercise. 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Understanding IAS 17 Leases IAS 17 Key IAS 17 Leases Definition inception date of lease: The earlier of lease agreement and the date of commitment by the parties. The type of lease is identified at the date of inception. Interest rate implicit in lease: That makes present value of lease payment and UN-guaranteed value equal to fair value and (any) initial direct costs of lessor. Economic and Useful life: Economic life is the total life of an asset excepted to be economically usable by one or more users. Useful life is the Period over which an asset is expected to be available for use by an entity. Residual Value: this may be Guaranteed or UN-guaranteed ; Guaranteed: A guarantee made to a lessor by a party unrelated to lessor that the value of an asset at the end of lease will be at least a specified amount. UN-Guaranteed: is that portion of residual value of asset, the realization of which is not assured by a party related to the lessor. Lease Receipts and Payments: The term lease Payments refer to the payments that a lessee expects to make over a lease term or the Receipts that a lessor expects over the lease with a significant part of the assets life remaining, there needs to be some realisation of funds through sale or further rentals. However, in the case of a specialised asset this will not normally occur, because it is of value only to the lessee. In these cases, the asset will normally transfer to the lessee at the end of the lease for a nil or nominal amount. Therefore is relying on a subsequent lease or sale to do so. This is an indicator of an operating lease as there will be no compelling commercial reason why the lessee should extend the agreement. The absence of any option to extend the lease does not provide evidence either way as to an operating or a finance lease and other factors will need to be considered to determine the classification. In some cases, fluctuations in the fair value of the residual interest in the leased asset are passed back to the lessee. This indicates that the lessee is bearing the residual value risk, and the lessor's return on investment is effectively fixed. These indicators provide evidence of a finance lease. If the lease also requires the lessee to make good to the lessor any shortfall between the sale proceeds and a fixed 'residual' amount, then again this is evidence of the lessor's return being fixed. Where the lessor retains the proceeds of the eventual sale of the asset, the lessor is bearing the residual value risk and where the sale proceeds are significant, then this could be evidence of an operating lease. Issues sometimes arise in lease contracts where an asset is held on a finance lease and then it is all or partially sub-let to another party on identical terms and conditions. This can occur where several entities intend to share leased accommodation and arrange for one entity to lease the whole asset and then sub-let the relevant parts to the others. The issue that arises here is whether the lead entity should recognise the finance leases on a gross basis in its accounts or whether it should not get off the transactions in its accounts. In this case the entity should currently look at the de-recognition requirements of IAS 39, Financial Instruments: Recognition and Measurement. The treatment will depend on the terms of the individual transaction. If the two transactions are separate to the extent that the lead entity is liable to pay its rentals under the head-lease regardless of whether it actually receives its sub-lease rentals, then the de-recognition requirements will not be met and it will need to account for the two leases on a gross basis. A contingent rent is such amount that is paid as part of lease payments but is not fixed or agreed in advance at the inception of lease rather the amount to be paid is dependent on some future event. However, it is not an interest payment as it is not connected with the passage of time therefore time value of money is not an issue. Contingent rent is commonly connected with an increase or decrease in future sales by the lessee or increase or decrease in the use of asset or inflation or deflation. Under IAS 17, contingent rents are excluded from minimum lease payments and are accounted as expense/income in the period in which they are incurred/earned. If a lease contains a clean break clause, where the lessee is free to walk away from the lease agreement after a certain time without penalty, then the lease term for accounting purposes will normally be the period between the commencement of the lease and the earliest point at which the break option is exercisable by the lessee. If a lease contains an early termination clause that requires the lessee to make a termination payment to compensate the lessor such that the recovery of the lessor's remaining investment in the lease was assured, then the termination clause would normally be disregarded in determining the lease term. Similarly the same principle applies, if the lease agreement states that the lease can only be terminated in remote circumstances, with the permission of the lessor or on entering a new lease agreement for the same or equivalent asset. The IASB is preparing a standard that may clarify and change some of the above aspects of lease accounting. The current models lead to a lack of comparability and undue complexity because of the distinction between finance and operating leases. 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Lease Receipts and Payments: The term lease Payments refer to the payments that a lessee expects to make over a lease term or the Receipts that a lessor expects over the lease with a significant part of the assets life remaining, there needs to be some realisation of funds through sale or further rentals. However, in the case of a specialised asset this will not normally occur, because it is of value only to the lessee. In these cases, the asset will normally transfer to the lessee at the end of the lease for a nil or nominal amount. Therefore is relying on a subsequent lease or sale to do so. This is an indicator of an operating lease as there will be no compelling commercial reason why the lessee should extend the agreement. The absence of any option to extend the lease does not provide evidence either way as to an operating or a finance lease and other factors will need to be considered to determine the classification. In some cases, fluctuations in the fair value of the residual interest in the leased asset are passed back to the lessee. This indicates that the lessee is bearing the residual value risk, and the lessor's return on investment is effectively fixed. These indicators provide evidence of a finance lease. If the lease also requires the lessee to make good to the lessor any shortfall between the sale proceeds and a fixed 'residual' amount, then again this is evidence of the lessor's return being fixed. Where the lessor retains the proceeds of the eventual sale of the asset, the lessor is bearing the residual value risk and where the sale proceeds are significant, then this could be evidence of an operating lease. Issues sometimes arise in lease contracts where an asset is held on a finance lease and then it is all or partially sub-let to another party on identical terms and conditions. This can occur where several entities intend to share leased accommodation and arrange for one entity to lease the whole asset and then sub-let the relevant parts to the others. The issue that arises here is whether the lead entity should recognise the finance leases on a gross basis in its accounts or whether it should not get off the transactions in its accounts. In this case the entity should currently look at the de-recognition requirements of IAS 39, Financial Instruments: Recognition and Measurement. The treatment will depend on the terms of the individual transaction. If the two transactions are separate to the extent that the lead entity is liable to pay its rentals under the head-lease regardless of whether it actually receives its sub-lease rentals, then the de-recognition requirements will not be met and it will need to account for the two leases on a gross basis. A contingent rent is such amount that is paid as part of lease payments but is not fixed or agreed in advance at the inception of lease rather the amount to be paid is dependent on some future event. However, it is not an interest payment as it is not connected with the passage of time therefore time value of money is not an issue. Contingent rent is commonly connected with an increase or decrease in future sales by the lessee or increase or decrease in the use of asset or inflation or deflation. Under IAS 17, contingent rents are excluded from minimum lease payments and are accounted as expense/income in the period in which they are incurred/earned. If a lease contains a clean break clause, where the lessee is free to walk away from the lease agreement after a certain time without penalty, then the lease term for accounting purposes will normally be the period between the commencement of the lease and the earliest point at which the break option is exercisable by the lessee. 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