

IAS 17 Leases.

A lease is a contract between lessor and lessee for the hire of an asset.

Leases are classified into 2 types:

- Operating lease
- Finance lease

Lessor: the entity who owns the asset and leases it out, eg Hertz

Lessee: the entity who lease the asset to use eg you lease a car, you are the lessee.

IAS 17 requires entities to account for the substance of a lease not the legal form.

OPERATING LEASE

Charge as an expense in the Income statement and disclose details in the notes.

FINANCE LEASE

Finance Lease: transfers all the risks and rewards of ownership of the asset to the lessee. Lessor might own asset but substance means that the lessee has effectively bought it and the lease payments are the equivalent of a loan.

If you see some of the following then it is a finance lease;

- Ownership transfers to lessee
- Lessee can purchase
- Lease contract for all useful life
- Payments=value
- Specialised asset

- Lease can carry on at minimum value after end.

In Statement of Financial Position show the asset under Non-Current Assets and Finance Lease obligation under Non-Current Liabilities. Depreciate the asset and reduce the lease obligation as you pay it off.

Asset: fair value or present value of minimum lease payments.

Liability: equal to asset value.

Depreciate asset over its useful life (shorter of life and lease term) so value will reduce.

Pay lease payments: this is divided between capital and interest. You have to allocate the interest which keeps increasing your liability. 2 methods, sum of digits or or actuarial (% on balance).