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STAFF PAPER

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Project	**Leases**		
Paper topic	Lessee Disclosure Requirements—IASB		
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Objective

1. The objective of this paper is to discuss lessee disclosure requirements in the final leases standard under the IASB lessee accounting model.

2. This paper is structured as follows:

   (a) Overview

   (b) Summary of Detailed Staff Recommendations

   (c) Comparison of IASB and FASB Staff Recommendations

   (d) Background

   (e) Summary of High-Level Feedback Received on the 2013 ED

   (f) Overall Disclosure Objective

   (g) Elimination of 2013 ED disclosure requirements

      (i) Overview

      (ii) Reconciliation of lease liabilities

      (iii) Reconciliation of ROU assets

(h) Quantitative Disclosure Table

(i) Maturity Analysis of Lease Liabilities

(j) Additional Qualitative Disclosures

(k) Staff Recommendations and Questions for the IASB

(l) Appendix A – Extracts from IFRS 7

(m) Appendix B – Example drafting for qualitative disclosure recommendations

(n) Appendix C – Illustrative examples relating to qualitative disclosure recommendations

Overview

3. Because this paper contains a considerable number of different disclosure topics, the staff think that it is useful to provide a high level overview of the analysis and recommendations that it contains.

4. The staff recommend retaining the overall disclosure objective in the 2013 ED, which was to enable users of financial statements (hereafter referred to as 'investors') to understand the amount, timing, and uncertainty of cash flows arising from leases. Feedback received on the 2013 ED demonstrated that it is difficult to establish a set of detailed disclosure requirements for lessees that would achieve this objective and, at the same time, address the following:

    (a) appropriately consider the cost concerns of preparers;

    (b) avoid an excessive amount of disclosure, or financial statements 'clutter'; and

    (c) avoid the use of 'boilerplate' statements (rather than providing useful information).

5. These concerns are particularly relevant for lessees with a high volume of leases with unique terms and conditions. For these lessees, achieving a level of disclosure that provides meaningful information to investors but is not excessive is challenging.

6. In order to address these concerns, the staff recommend a two-part disclosure package.

7. Firstly, we think that a lessee should be required to provide a minimum level of specific quantitative disclosures in order to meet the information needs of investors. This includes information about lease expenses and cash flows that we think investors would want to see for all lessees with material leasing activities. The staff recommend simplifying the presentation of these specific quantitative disclosures by generally requiring a lessee to present them in one table in the notes to the financial statements. These disclosures are described in paragraphs 47-110 of this paper.

8. Secondly, we think that for those lessees with more complex, unusual or otherwise significant lease arrangements, additional entity-specific disclosures would be necessary in order to provide investors with information that meets the overall disclosure objective described above in paragraph 4 of this paper. The staff recommend that a lessee should be required to disclose any additional qualitative information (beyond the mandatory quantitative disclosure requirements described in paragraph 7) that is necessary for an investor to understand the amount, timing, and uncertainty of cash flows arising from leases. This might include, for example, information about variable lease payment terms, extension options and termination clauses, residual value guarantees and sale and leaseback transactions. The staff recommend including guidance and Illustrative Examples demonstrating what this information *might* include for different types of lease portfolios in the final leases standard (Appendix B). However, judgement as to *how* to satisfy this qualitative disclosure objective would be made by each lessee. This requirement is described in paragraphs 111-129 of this paper.

Summary of Detailed Staff Recommendations

9. With regard to lessee disclosure requirements, the staff recommend that the IASB:

    (a) retain the overall lessee disclosure objective proposed in the 2013 ED, including the statement requiring a lessee to consider the level of detail necessary to satisfy the disclosure objective;

    (b) eliminate the 2013 ED requirements for a lessee to disclose reconciliations of opening and closing balances of its lease liabilities and right-of-use (ROU) assets;

    (c) require a lessee to disclose the following quantitative amounts in a single tabular disclosure:

        (i) Lease expense, split between amortisation of ROU assets and interest on lease liabilities;

        (ii) Lease expense, split by class of underlying asset;

        (iii) Short term lease expense;

        (iv) Small asset lease expense;

        (v) Variable lease expense;

        (vi) Sublease income;

        (vii) Total cash flow for leases;

        (viii) Additions to ROU assets;

        (ix) Weighted average remaining lease term; and

        (x) Gains or losses arising from sale and leaseback transactions.

    (d) require a lessee to disclose the closing carrying amount of its ROU assets by class of underlying asset. A lessee could include this disclosure within the quantitative disclosure table (described above in bullet (c)) *or* within the note relating to the balance sheet line item in which ROU assets are presented (eg the Property, Plant and Equipment note).

(e) eliminate the 2013 ED requirement for a lessee to disclose a maturity analysis of lease liabilities, showing the undiscounted cash flows on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years. Instead, the staff recommend that the final leases standard should require a maturity analysis for lease liabilities in accordance with paragraphs 39 and B11 of IFRS 7 (Appendix A). This would include an explicit statement that a lessee should disclose the maturity analysis of lease liabilities separately from the maturity analyses of other financial liabilities;

(f) eliminate the 2013 ED requirement for a detailed list of specific mandatory qualitative disclosures. Instead, the staff recommend that the final leases standard should require a lessee to disclose sufficient additional information (ie beyond that already described above), *if* needed, in order to satisfy a list of specified disclosure objectives. The staff's initial thoughts on the drafting of this disclosure requirement are set out in Appendix B. Judgement as to how these disclosure objectives are to be satisfied would then need to be made by individual lessees. We also recommend including illustrative examples in the final leases standard to demonstrate how lessees with different types of lease portfolio might comply with this qualitative disclosure requirement.

Comparison of IASB and FASB Staff Recommendations

10. Disclosure requirements under the FASB lessee accounting model have been analysed separately in Agenda Paper 3A/FASB Memo 303. The staff think that it is useful for the IASB to understand the differences in staff recommendations for lessee disclosure under the IASB and FASB lessee accounting models. The following table sets out a summary of the disclosures that would be required in the final leases standard based on the staff recommendations:

IASB DISCLOSURE PACKAGE (discussed in this paper)	**FASB DISCLOSURE PACKAGE (discussed in Agenda Paper 3A/FASB memo 303)**

Qualitative disclosures	**Qualitative disclosures**
Objectives-based disclosures	
	2013 ED requirements
	Disaggregation guidance
	Existence, and terms and conditions, of significant nonlease commitments taken on as a result of entering into lease contracts.

Quantitative disclosure table:		**Quantitative disclosure table:**	
Amortisation	X	Amortization	X
Interest	X	Interest	X
Lease expense	**X**	Type A lease expense	**X**
Property	X		
Other classes of underlying asset	X		
Lease expense	**X**		
		Type B lease expense	X
Short term lease expense†	X	Short term lease expense	X
Small asset lease expense	X		
Variable lease expense	X	Variable lease expense	X
Sublease income	X	Sublease income	X
Total lease expense	**X**	**Total lease expense**	**X**
Total cash flow for leases	X		
		Operating cash flows	X
		Financing cash flows	X
		Cash paid for amounts included in the measurement of lease liabilities	**X**
Additions to ROU assets	X		
		ROU assets obtained in exchange for lease liabilities	X
Weighted average remaining lease term	X	Weighted average remaining lease term (separately for Type A and Type B leases)	X
		Weighted average discount rate for Type B leases	X

Gains and losses on sale and leaseback transactions	X	Gains and losses on sale and leaseback transactions	X
Property*	X		
Other classes of underlying asset*	X		
Total ROU assets*	**X**		

* Alternative option to disclose this split within PPE note
† Additional footnote disclosure to state short term lease commitment if this is not reflected in the short term lease expense

Maturity analysis of lease liability	**Maturity analysis of lease liability**
Based on IFRS 7 requirements	
	No maturity analysis required

Background

11. The existing requirements in IAS 17 *Leases* do not include extensive lessee disclosure requirements. The 2013 ED proposed a greater level of detailed qualitative and quantitative disclosure requirements in response to investors' requests for additional financial information about leases.

12. The specific disclosure requirements in IAS 17 and proposed in the 2013 ED are discussed in the relevant sections below.

Summary of High-Level Feedback Received on the 2013 ED

13. Many of the comment letters received in response to the 2013 ED contained feedback on the proposed lessee disclosure requirements. Significant feedback was also received on the disclosures proposed in the 2013 ED during outreach meetings with investors and preparers.

14. The feedback received on the proposed lessee disclosure requirements is mixed. Feedback received and suggestions made with respect to particular individual disclosure requirements are presented in the relevant sections below.

15. There were, however, some areas of high-level feedback that are pervasive in the comments received and that apply to the entire disclosure package. These areas are summarised below.

Usefulness of Disclosures

16. The majority of investors that expressed views supported the proposed lessee disclosure requirements. They commented that the proposed disclosures would provide useful information relating to the assumptions made by management, the nature of leases, and changes in lease balance sheet amounts from period to period, particularly when compared to the information provided under existing IFRS. Many investors contend that no single amount can provide a complete picture of an entity's leasing activities. Accordingly, a comprehensive disclosure package is important for their analyses.

Complexity, Detail and Cost

17. Most preparers considered the disclosure proposals to be excessively complex and detailed. These constituents described the proposals as:

> …lengthy, onerous and will detract user attention from other areas of the financial statements **(CL 559)**;
>
> …voluminous and lack[ing in] practical application **(CL 411);** and
>
> …the combined effect of full disclosure would be to increase 'clutter' in the financial statements **(CL 138)**.

18. In general, preparers were primarily concerned about the costs of complying with the disclosure requirements.

19. In addition, some investors were concerned about the risk of material entity-specific disclosures being 'lost' within the mandatory disclosure requirements.

Increased Disclosure Requirements Compared to Existing Guidance

20. Some preparers commented on the extensive nature of the proposals compared to the existing requirements in IAS 17. These preparers questioned why an increase in disclosure requirements should be required if the proposed lessee accounting model provides the information that investors need. Many of these constituents noted that an improved lessee accounting model would lead them to expect a decrease in disclosure requirements rather than an increase.

21. Further, some preparers, as well as some academics and accounting firms, stated that, in their opinion, the proposed lessee disclosure requirements did not seem to reconcile with the IASB's efforts to address "disclosure overload" in other projects.

22. In contrast, many investors expressed a desire for additional disclosures that were not proposed in the 2013 ED (for example, quantitative sensitivity analyses).

Overall Disclosure Objective

Background and Feedback

23. IAS 17 does not include an overall disclosure objective.

24. The 2013 ED proposed an overall disclosure objective to enable investors to understand the amount, timing, and uncertainty of cash flows arising from leases. To achieve that objective, the 2013 ED proposed qualitative and quantitative disclosure requirements about (a) a lessee's leases; (b) the significant judgements made in applying the requirements in the 2013 ED to those leases; and (c) the amounts recognised in the financial statements relating to those leases.

25. The 2013 ED also included the following statement regarding the *application* of the lessee disclosure objective:

> A lessee shall consider the level of detail necessary to satisfy the disclosure objective and how much emphasis to

place on each of the various requirements. A lessee shall aggregate or disaggregate disclosures so that useful information is not obscured by including a large amount of insignificant detail or by aggregating items that have different characteristics.

26. Most constituents did not comment on the lessee disclosure objective itself. Nonetheless, some constituents, including many preparers, commented on the application statement set out in paragraph 25 above.

27. Many of these constituents supported the inclusion of the statement in the 2013 ED because they thought that entities should use judgement when considering the level of detail required to satisfy the disclosure objective and how much emphasis to place on each of the various requirements. However, some preparers and auditors suggested including a more explicit statement than was included in the 2013 ED. These constituents requested that the IASB explicitly state that the disclosures listed should not be regarded as mandatory in all situations and that entities should apply materiality in determining the extent to which disclosures are required. Although acknowledging the existing materiality provisions of IFRS, these constituents were concerned that, without a more explicit statement, entities and/or auditors would use the proposed lessee disclosure requirements as a 'checklist'. This could result in material information being 'lost' within other disclosures that may not be important to understanding the activities of a particular entity.

Staff Analysis

28. The staff think it is important to include an objective for the lessee disclosure requirements in the final leases standard. The disclosure objective would allow:

    (a) an entity to understand the purpose of the disclosure requirements and the extent to which information about leases should be presented; and

(b) investors to determine the type of information about leases they would receive in the notes to the financial statements and, therefore, how to best utilise that information for their analyses.

29. The staff think that the lessee disclosure objective accurately summarises the reasons why the disclosure requirements are needed. The objective also identifies the type of information investors can expect to extract from the disclosures. Accordingly, the staff do not think changes need to be made to the lessee disclosure objective proposed in the 2013 ED.

30. The staff acknowledge the feedback received that an explicit statement about materiality would be useful in applying the disclosure requirements. However, such statements are generally *not* included in any existing Standards. The staff do not think that the disclosure requirements proposed in the 2013 ED are so different from disclosure requirements in other standards that an explicit materiality statement is required for lessee disclosures. In particular, the staff note that IFRS 15 *Revenue from Contracts with Customers* includes a very similar statement to that in the 2013 ED regarding the application of the disclosure objective to the disclosure requirements, and does *not* contain any further guidance on materiality. The staff think that the inclusion of an explicit materiality statement in the final leases standard could set a precedent for including similar statements in future Standards. It could also risk implying that materiality does *not* apply to other existing Standards because it is not explicitly mentioned.

31. The staff think that implicit in the proposed overall disclosure objective is the notion that the level of detail in the disclosures should equate to the significance of an entity’s leasing activities. For example,, if leasing is a significant part of an entity’s business activities, the disclosures would be more comprehensive than for an entity whose leasing activities are less significant to its business activities. Activities that are immaterial would not be required to be disclosed by any Standard. Accordingly, the staff do not think that the IASB should include an

explicit statement that the proposed lessee disclosure requirements are not required in all circumstances. In addition, the staff think that concerns about the disclosure guidance comprising a ‘checklist’ are substantially addressed by the staff recommendations in this paper, particularly with respect to the proposed qualitative disclosure requirements.

Staff Recommendation

32. The staff therefore recommend that the IASB retain the lessee disclosure objective proposed in the 2013 ED, including the statement requiring a lessee to consider the level of detail necessary to satisfy the disclosure objective.

Elimination of Specific 2013 ED Disclosure Requirements

Overview

33. Many constituents considered the disclosure package proposed in the 2013 ED to be excessively complex and detailed. Feedback received from investors about the usefulness of the various disclosure proposals in the 2013 ED indicates that there are particular elements of the proposals for which the benefit for investors may not outweigh the associated costs.

34. In particular, this applies to the 2013 ED proposals for lessees to disclose reconciliations of opening and closing balances of lease liabilities and ROU assets. The staff think that these disclosures could be replaced with alternative requirements that would provide a better balance between benefit for investors and cost to preparers.

Reconciliation of Lease Liabilities

35. The 2013 ED proposed that a lessee should disclose a reconciliation of opening and closing balances of lease liabilities. This reconciliation would include interest on lease liabilities and other items such as:

    (a) Liabilities created due to leases commencing or being extended;

    (b) Liabilities extinguished due to leases being terminated;

    (c) Remeasurements relating to a change in an index or a rate used to determine lease payments;

    (d) Cash paid;

    (e) Foreign currency transaction gains or losses; and

    (f) Effects of business combinations.

36. This proposal was made on the basis that such a reconciliation provides investors with information about changes to lease liabilities during the reporting period which is useful to their analyses. There is no similar requirement in existing IFRS for finance lease liabilities.

37. Many constituents raised cost and complexity concerns about the lease liabilities reconciliation proposed in the 2013 ED - it was one of the most pervasive areas of cost concern raised. Preparers stated that this reconciliation would be onerous and costly to prepare. Some of those preparers indicated that new system capabilities would be required to meet this disclosure requirement that otherwise may not be required to meet the recognition and measurement requirements.

38. Many IFRS constituents also thought that the disclosure requirements for lease liabilities should be consistent with those for all other financial liabilities and should not be more onerous. Lease liabilities are financial liabilities – ie lease liabilities meet the definition of financial liabilities in IFRS. The disclosure requirement for a lessee to present a reconciliation of the opening and closing balance of lease liabilities goes beyond the requirements of IFRS 7 *Financial*

Instruments: Disclosure, which does not contain such a reconciliation requirement. Constituents noted that because lease liabilities would now be recognised on a lessee's balance sheet and measured similarly to other similar financial liabilities, they could see no reason to have more extensive disclosures for lease liabilities than for other financial liabilities.

39. Although many investors supported disclosure of a reconciliation of the opening and closing balance of lease liabilities, they were generally interested in particular amounts that would be part of the reconciliation rather than the reconciliation as a whole. Investors were generally interested in:

    (a) *Liabilities created due to leases commencing or being extended*, which would depict new (and extended) leases entered into during the reporting period; and

    (b) *Cash paid*, which would help in analysing an entity's cash flows related to leases.

40. On the basis of this feedback, the staff think that investor needs can be satisfied through disclosures other than the reconciliation proposed in the 2013 ED that are less costly to prepare. In particular, the staff think that requiring disclosure of the two pieces of information described above would substantially satisfy the same information needs of investors as disclosure of a full reconciliation.

41. Accordingly, the staff recommend eliminating the 2013 ED proposal to require a lessee to disclose a reconciliation of the opening and closing balance of lease liabilities. The alternative disclosures that the staff think would meet the same investor information needs are included within the quantitative disclosure recommendations below.

Reconciliation of ROU Assets

42. The 2013 ED proposed that a lessee should disclose a reconciliation of opening and closing balances of ROU assets by class of underlying asset. This is similar

to existing IAS 16 *Property, Plant and Equipment* disclosure requirements and was proposed in order to provide comparable information about changes in ROU assets to that provided about owned assets.

43. Similar to the feedback received on the proposed reconciliation of lease liabilities, a number of preparers stated that a reconciliation of ROU assets would be costly to prepare. Unlike property, plant and equipment which can normally be grouped into items with similar economic useful lives or types of assets, the varied nature of lease contracts can make producing reconciliation disclosures a complex exercise.

44. Similar to the feedback received on the reconciliation of lease liabilities, many investors supported the disclosure of particular amounts that would be part of the reconciliation rather than the reconciliation as a whole. Investors were generally interested in:

    (a) Additions to ROU assets, which would provide information about new (and extended) leases entered into during the reporting period; and

    (b) Amortisation expense for the period, which would provide information about the income statement effect of leases.

45. On the basis of this feedback, the staff think that investor needs can be satisfied through disclosures other than the reconciliation proposed in the 2013 ED that are less costly to prepare. Furthermore, the staff think that the potential costs associated with preparing the reconciliation of the opening and closing balance of ROU assets outweigh the benefits.

46. Consequently, the staff recommend eliminating the 2013 ED requirement for a lessee to disclose a reconciliation of opening and closing balances of ROU assets. Alternative disclosures that the staff think would meet the same investor information needs are included within the quantitative disclosure recommendations below.

Quantitative Disclosure Table

Overview

47. The 2013 ED did not require a lessee to disclose comprehensive information about the total expense arising from its leasing activities. Regarding lease expense, the 2013 ED proposed only that a lessee should disclose costs recognised in the period relating to variable lease payments not included in lease liabilities.

48. Similarly, the 2013 ED did not require disclosure of total cash flow information relating to leases. The reconciliation of the opening and closing balance of lease liabilities would have required a lessee to disclose a cash paid figure for leases. However, this figure would not have captured lease cash flows that would not be included in the measurement of lease liabilities (ie cash flow information for variable lease payments and/or short-term leases). The 2013 ED also required disclosure of information about the acquisition of ROU assets in exchange for lease liabilities.

49. Investors noted that information about lease expenses and cash flows provides insight into the financial effect of an entity’s leasing activities and allows investors to better forecast future lease payments in the context of an entity’s business plans and strategy. Some constituents highlighted that the 2013 ED would not require a lessee to disclose information about leases in one place within the financial statements. They thought that this could compromise the usefulness of the proposed disclosures.

50. The staff think that it would be beneficial to investors if a lessee were required to disclose all quantitative information about leases together in one tabular disclosure and recommend that the IASB include this within the disclosure requirements of the final leases standard.

51. The remainder of this section discusses the quantitative disclosures that the staff recommend. The table below sets out how the staff envisage the proposed tabular disclosure to appear in the financial statements of a lessee:

Year Ended 31 December 20XY	**20XY** *CU'000*	**20XX** *CU'000*	***Para. Ref. for Staff Analysis***
Lease Expense:			
Amortisation of ROU assets	1,006	932	
Interest on lease liabilities	364	298	*53-57*
	1,370	1,230	
Property	1,109	998	
Other classes of underlying asset	261	232	*58-63*
	1,370	1,230	
Short term lease expense†	30	20	*64-66*
Small asset lease expense	10	10	*67-68*
Variable lease expense	60	60	*69-73*
Sublease income	(8)	(9)	*74-78*
Total Lease Expense	**1,462**	**1,311**	
Other Information:			
Total cash flow for leases	1,571	1,438	*79-80*
Additions to ROU assets	320	314	*81-84*
Weighted average remaining lease term	4.3 years	4.6 years	*85-89*
Gains on sale and leaseback transactions	94	-	*90-94*
Carrying amount of Property ROU assets*	6,101	5,625	
Carrying amount of other classes of ROU assets*	925	781	*95-98*
Total ROU assets*	7,026	6,406	

*Alternative option to disclose this split within PPE note
†Additional footnote disclosure to state short term lease commitment if this is not reflected in the short term lease expense

52. The tabular disclosure would include costs that a lessee has capitalised as part of the cost of another asset in the reporting period, as well as costs that a lessee has recognised as an expense in that period.

Lease Expense Split by Amortisation and Interest

53. The 2013 ED included requirements for lessees to disclose reconciliations of opening and closing balances of ROU assets and lease liabilities. As discussed above, the staff do not recommend maintaining these requirements in the final

leases standard. Instead, the staff think that the specific line items identified by investors as providing useful information should be included within the tabular quantitative disclosure requirement.

54. Two such items are:

    (a) the amortisation expense for the period that, under the 2013 ED proposals, would have appeared within the reconciliation of ROU assets; and

    (b) the interest expense for the period that, under the 2013 ED proposals, would have appeared within the reconciliation of lease liabilities.

55. The staff think that each of these items would often be obscured within other line-items (for example, within a general interest expense line-item or within various operating expense line-items depending on the nature of the underlying assets or the business within which they are employed). Even in those rare circumstances when a lessee might present these amounts separately in the income statement, the staff think it would be beneficial for investors to have all quantitative information about leases disclosed in one location in the financial statements.

56. Furthermore, the staff think that requiring this two-line breakdown of the lease expense within the tabular quantitative disclosure table provides a reasonable balance between:

    (a) providing investors with the most useful information from the reconciliations proposed in the 2013 ED; and

    (b) costs to lessees in producing these disclosures.

57. Consequently, the staff recommend requiring disclosure of lease expense, split into amortisation and interest, within the single tabular quantitative disclosure.

Lease Expense Split by Asset Type

58. Members of the IASB's investor advisory body, the Capital Markets Advisory Committee (CMAC), have provided feedback that disclosure that could be used to estimate 'whole asset' information would be useful to them. Ie information that would enable them to understand what a lessee's balance sheet would look like if leased assets had instead been purchased. They noted that, in particular, equity analysts often calculate an estimate of this information when determining the capital employed in an entity, to obtain comparability between entities that lease and own assets. In cases for which a ROU asset does not comprise substantially all of the economic benefits embedded in the underlying asset, investors would not obtain this whole asset information from the amounts recognised on the balance sheet.

59. Disclosure of 'whole asset' information was not proposed in the 2013 ED, nor is it a disclosure requirement in IAS 17. However, the staff understand that meaningful comparisons between entities that lease assets and those that purchase assets can be difficult in the absence of any such disclosure.

60. One way to achieve this objective would be to include a requirement for lessees to disclose the value of underlying assets for all of their leases. However, the staff think that this potentially would be extremely costly for lessees, particularly because in many cases a lessee would not have access to the necessary information.

61. CMAC members also identified that a disclosure of lease expense split by asset type would be helpful in enabling investors to estimate whole asset information that they would then use in their analyses. This is because investors are generally able to estimate the typical economic life of a class of asset. However, because they are generally *not* able to do this for a whole lease portfolio (with a mix of underlying assets), they are not able to use the total lease expense figure to estimate whole asset information.

62. The staff think that requiring disclosure of lease expense split by asset type provides a reasonable balance between the information needs of investors and costs for preparers for the following reasons:

    (a) Feedback from CMAC members that the ability to estimate whole asset information with some reliability is useful. Under the existing disclosure requirements in IAS 17, it is difficult for investors to estimate this in a meaningful way;

    (b) A breakdown of lease expense by asset type would require a lessee to disclose only one figure per class of underlying asset, although that figure would be made up of two pieces—amortisation and interest for each class of underlying asset. Because this information could be obtained from a lessee's general ledger system (by setting up sub-expense accounts), the staff think that a lessee could provide this information without incurring excessive costs.

63. Consequently, the staff recommend including within the tabular quantitative disclosure requirement for lessees disclosure of a breakdown of the lease expense by class of underlying asset.

Short-term Lease Expense

64. At the March 2014 joint board meeting, the boards tentatively decided to retain the recognition and measurement exemption for short-term leases that was proposed in the 2013 ED. The boards also decided to require disclosure of the amount of expense relating to short-term leases recognised in the reporting period.

65. The staff recommend that this disclosure should be included within the single quantitative disclosure table. This is to ensure that a lessee would provide in one location a complete picture of an entity's leasing activities.

66. At the March 2014 joint board meeting, the boards also tentatively decided that if the short-term lease expense does not reflect a lessee's short-term lease

commitments, a lessee should disclose that fact and the amount of its short-term lease commitments. The staff think that this disclosure, if required, should be shown as a footnote to the quantitative disclosure table.

Small Asset Lease Expense

67. At the March 2014 joint board meeting, the IASB tentatively decided to permit a recognition and measurement exemption for leases of small assets in the final leases standard. This would permit a lessee to account for leases that qualify for the exemption in the same manner as (a) existing operating leases and (b) short-term leases.

68. The staff think that the small asset lease expense should be included within the tabular quantitative disclosure requirement to ensure that a lessee would provide an accurate figure for total lease expense. Disclosure of the small asset lease expense would also provide investors with useful information about the extent of an entity's small asset leases and whether, for example, potentially material values of leased assets would be captured by the exemption.

Variable Lease Expense

69. At the April 2014 joint board meeting, the boards tentatively decided that a lessee should include only variable lease payments that depend on an index or a rate in the initial measurement of lease assets and lease liabilities. This means that a lessee would recognise all other variable lease payments (other than those that are capitalised as part of another asset) in its income statement in the period in which those payments are incurred.

70. The 2013 ED proposed that a lessee should disclose costs recognised in the period relating to variable lease payments that are not included in the lease liability. Constituents did not express concerns about the cost of providing this disclosure.

71. The staff think disclosure of variable lease expense continues to remain relevant to achieving the objective of the lessee disclosures. Variable lease payments are likely to vary from period to period because they often depend on a lessee's performance or use. Furthermore, an investor is unable to gain an understanding of the variable lease expense incurred in a period from the income statement or statement of cash flows, because such amounts are generally combined with other operating expenses. Disclosure of the variable lease expense incurred in the period allows an investor to better understand the total expense and cash flows arising from an entity's leasing activities.

72. Requiring the disclosure of variable lease expense for all reporting periods presented would allow investors to perform trend analysis to project the variable lease expense in future periods. Also, although variable lease payments would not be included in the measurement of a lessee's lease liabilities, the disclosure of variable lease expense would provide investors with some of the information needed to capitalise variable lease payments should they wish to do so.

73. Consequently, the staff think that a lessee should include variable lease expenses within the tabular quantitative disclosure requirement. Similar to short-term lease expenses and small asset lease expenses, the staff think that inclusion of variable lease expenses would ensure that a lessee provides a complete picture of its leasing activities in one location.

Sublease Income

74. Existing IFRS requires the disclosure of the total future minimum sublease payments expected to be received under non-cancellable subleases at the end of the reporting period. The 2013 ED did not propose any specific quantitative disclosure requirements in respect of subleases. However, it proposed a requirement to include information relating to subleases within the disclosure of qualitative information about the nature of an entity's leases.

75. The staff think that information about subleases is relevant to investors because it helps provide an accurate depiction of an entity's leasing activities. However, the staff think that the 2013 ED proposal could be improved by including a specific quantitative requirement rather than qualitative information. This view is based on the following:

    (a) general feedback from investors that quantitative disclosure is generally *more* useful than qualitative disclosure;

    (b) feedback from preparers during fieldwork that, after the initial year of transition, qualitative disclosure is often *more* costly to comply with than a quantitative requirement because it cannot be system-generated;

    (c) a specific quantitative disclosure requirement would have the advantage of allowing comparability across entities.

76. The staff think that the most useful quantitative information relating to sublease activity would be a requirement for the disclosure of sublease income (both sublease interest income on Type A leases and sublease rental income on Type B leases). The staff think that *not* including sublease income would provide an inaccurate figure when presenting total lease expense. Including only the expense component of a lease and not showing the income that arises from a sublease would overstate the actual net lease expense of a lessee.

77. The staff note that disclosure of sublease income (rather than future minimum sublease payments) represents a change from existing IFRS disclosure requirements in respect of subleases. However, the staff think that the disclosure of sublease income would generally be less costly to provide than the existing requirement to disclose future sublease payments expected to be received. It would also often provide investors with a fair representation of the level of sublease income expected in future years. When this is not the case, and the effect of future sublease income is considered to be material, the staff think that preparers would be prompted to disclose this information under the qualitative disclosure proposals recommended in this paper.

78. Consequently, the staff recommend including a requirement for a lessee to include sublease income within the proposed quantitative lease disclosure table.

Total Cash Flow for Leases

79. At the June 2014 joint board meeting, the IASB decided to require a lessee to disclose a single figure for lease cash flows in the financial statements. This disclosure is not an existing requirement of IAS 17, however investors have consistently provided feedback that a single lease cash flow figure provides useful information.

80. The staff think that a lessee should include this disclosure of lease cash flows within the single tabular quantitative disclosure requirement. This is because the staff think that it is beneficial to provide all information about lease expenses and cash flows together in one location.

Additions to Right of Use Assets

81. The 2013 ED included requirements for lessees to disclose reconciliations of opening and closing balances of ROU assets and lease liabilities. As discussed above, the staff do not recommend maintaining these requirements in the final leases standard. Instead, the staff think that the specific line items identified by investors as providing useful information should be included within the tabular quantitative disclosure requirement.

82. One such item is additions to ROU assets which, under the 2013 ED proposals, would have been included within the reconciliation of ROU assets.

83. Investors indicated that this figure is one of the most useful items of disclosure that would be provided by a reconciliation of ROU assets. This is because it provides investors with useful information about new (and extended) leases entered into during the reporting period, which helps to assess the entity's use of and reliance on leased assets to operate its business. It also better enables

investors to compare entities that lease assets with those that purchase them, particularly with regard to capital expenditure.

84. Consequently, the staff recommend including additions to ROU assets within the tabular quantitative disclosure requirement. Additions to ROU assets would include modifications to leases, and exercise of extension options not previously included in the lease term, as well as ROU assets arising from new leases.

Weighted Average Remaining Lease Term

85. Neither existing IFRS nor the 2013 ED included any specific disclosure requirements in respect of lease term.

86. Some investors have indicated that disclosure of weighted average remaining lease term would be beneficial for their analysis because it would allow them to better understand a lessee's renewal risk exposure and the timing of future lease payments. This disclosure would also provide investors with a clearer picture as to how long capitalised lease obligations would allow a lessee to operate at current levels.

87. The disclosure of weighted average remaining lease term would be additional to existing requirements, and the disclosure proposals of the 2013 ED. However, the staff think that the introduction of a specific requirement for disclosure of the weighted average remaining lease term has the following advantages:

    (a) the requirement is expected to result in more comparable information about lease terms than is provided today within the qualitative disclosures;

    (b) this approach responds to investor feedback that an average lease term provides more useful information than the range that is sometimes disclosed today;

    (c) the requirement is also expected to eliminate the use of "boilerplate" statements about lease term that are sometimes disclosed today.

88. The staff acknowledge that there would be incremental costs associated with disclosing weighted-average remaining lease term figures because these are not required to be disclosed under existing requirements. However, the staff think those costs are manageable because a lessee would not necessarily require additional information beyond that already accumulated and maintained in applying existing requirements—ie a lessee should be able to calculate the weighted average remaining lease term based on the data used to provide existing maturity analysis information. The staff think that the benefits associated with requiring a lessee to disclose weighted-average remaining lease terms outweigh the costs of doing so.

89. Consequently, the staff recommend including the weighted average remaining lease term within the tabular quantitative disclosure requirement recommended in this paper.

Gains and Losses Arising from Sale and Leaseback Transactions

90. Existing IFRS requires the disclosure requirements for lessees and lessors to be applied equally to sale and leaseback transactions.

91. In addition to the disclosures required for lessees, the 2013 ED proposed that a transferor entering into a sale and leaseback transaction should disclose any gains or losses arising from the transaction separately from gains or losses on disposal of other assets.

92. Constituents did not provide any specific feedback regarding the sale and leaseback disclosures proposed in the 2013 ED.

93. The staff continue to think that the proposal in the 2013 ED for a seller-lessee to disclose gains or losses arising from sale and leaseback transactions separately from gains or losses on the disposal of other assets is useful. It would allow investors to better understand the unique characteristics of sale and leaseback transactions (ie the seller-lessee retains physical possession of the underlying asset

in a sale and leaseback, which is typically not the case in the disposal of other assets) and the effect that such transactions have on a lessee's financial performance.

94. The staff recommend that the IASB retain the proposal in the 2013 ED that a seller-lessee should be required to disclose any gains or losses arising from sale and leaseback transactions separately from gains or losses on disposal of other assets. The staff think that this disclosure should be included within the tabular quantitative disclosure requirement proposed in this paper.

Right of Use Assets by Asset Type

95. As discussed earlier in the paper, the staff do not recommend retaining 2013 ED proposal for a lessee to disclose a reconciliation of opening and closing balances of ROU assets. The 2013 ED proposal would have required disclosures by lessees *by class of underlying asset.* Although the staff do not think the benefits of preparing the reconciliation outweigh the costs to preparers, we think that disclosure of a breakdown of the closing carrying value of ROU assets *by class of underlying asset* would provide useful information to investors without a significant cost burden for preparers.

96. Disclosure of ROU assets by class of underlying assets enables investors to understand the nature of an entity's leasing portfolio (eg what proportion of the portfolio comprises property leases). This disclosure would also be consistent with the existing requirement in IAS 17 for finance leases, which requires a lessee to disclose the net carrying amount at the reporting date for each class of underlying asset.

97. The staff think that, for this disclosure *only*, a lessee should have a choice of either presenting the information within the leases quantitative disclosure table *or* including it within the note relating to the balance sheet line item in which ROU assets are presented (eg the Property, Plant and Equipment note). The staff think that this is appropriate for two reasons:

(a) The proposed breakdown of ROU assets by class of underlying asset is a balance sheet disclosure. Accordingly, the staff do not think that its omission from the single quantitative disclosure table would compromise the benefit for investors of presenting all lease expenses and cash flows together in one note.

(b) Permitting this option is likely to be useful to entities who include ROU assets within Property, Plant and Equipmenton the balance sheet. An entity could present the breakdown of ROU assets by class of underlying asset on the basis of the same classifications used for Property, Plant and Equipment disclosures. Including this ROU asset breakdown within the Property, Plant and Equipment note would facilitate the reconciliation of the note to the carrying amount of Property, Plant and Equipment reported on the balance sheet.

98. Consequently, the staff recommend that the IASB require a lessee to disclose the closing carrying amount of ROU assets by class of underlying asset. This disclosure could be included within the quantitative disclosure table *or* within the note relating to the balance sheet line item in which ROU assets are presented (eg the Property, Plant and Equipment note).

Maturity Analysis of Lease Liabilities

Background

99. Existing IFRS leases guidance requires that, for both operating and finance leases, a lessee should disclose a maturity analysis showing the total future minimum lease payments for each of the following periods:

(a) Not later than one year;

(b) Later than one year but not later than five years;

(c) Later than five years.

For finance leases, a lessee is also required to disclose the present value of those future minimum lease payments.

100. These disclosure requirements in IAS 17 are *in addition* to the requirements of IFRS 7 relating to financial liabilities. IFRS 7 requires an entity to disclose a maturity analysis for all financial liabilities, and use its judgement to determine an appropriate number of time bands.

101. Under existing IFRS, the lease-specific maturity analysis requirements of IAS 17 are prescribed in more detail than those of IFRS 7, which apply to all financial liabilities. This is because IAS 17 mandates the time bands that an entity should disclose whereas IFRS 7 requires an entity to use judgement in determining the appropriate number of time bands (Appendix A of this paper sets out the IFRS 7 requirements in this respect). In complying with the disclosure requirements of IAS 17, an entity is also likely to comply with the requirements of IFRS 7. The reverse is not necessarily true. In practice, therefore, a lessee generally discloses the maturity analysis for lease liabilities in accordance with the requirements of IAS 17, without any further consideration of the appropriate time bands referred to in IFRS 7.

102. The 2013 ED proposed that a lessee should disclose a maturity analysis of lease liabilities, showing the undiscounted cash flows on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years. The 2013 ED also required a lessee to reconcile these undiscounted cash flows to the lease liabilities recognised in the balance sheet. These requirements were proposed to *replace* the maturity analyses required by IFRS 7.

Feedback

103. Investors have stated that the maturity analysis helps (a) when analysing liquidity risk; and (b) estimate an entity's future cash outflows. Investors also supported the reconciliation between the undiscounted lease payments and the lease liabilities

recognised on the balance sheet. However, many preparers were concerned about the incremental costs of preparing this reconciliation.

104. In addition, many IFRS constituents noted that the requirements of the ED were more granular than those of IAS 17 in that they require disclosure of cash flows on an annual basis for each of the first five years. IFRS constituents also observed that the proposals represented a departure from the general maturity analysis disclosure requirements of IFRS 7 in that they eliminate an entity's ability to apply judgement in determining the appropriate time bands. These constituents generally thought that the maturity analysis for leases should be consistent with that for all other financial liabilities. However, some of the IFRS investors making this comment also noted that, in their view, there should be more prescriptive disclosure requirements in this respect for all financial liabilities, rather than a less prescriptive requirement for leases. This would ensure greater comparability in the information disclosed by lessees.

Staff Analysis

105. The staff think that there are some clear advantages to requiring a lessee to disclose the specific maturity analysis time bands proposed in the 2013 ED in respect of lease liabilities. Most notably, this disclosure requirement would provide useful information to investors and ensure comparability across the maturity disclosures provided by different lessees. Feedback from investors on the maturity analysis proposals was generally positive.

106. On the other hand, the staff understand the concerns of those constituents who question why there is anything special or different about lease liabilities that means they require a more prescriptive disclosure requirement than all other financial liabilities.

107. With respect to satisfying investor needs of understanding liquidity risk and estimating future cash flows, the staff think that the existing requirements of IFRS 7 should achieve this (or, if not, an improvement should be made to IFRS 7 so that

the improvement is applied to *all* financial liabilities and not only lease liabilities). If the level of detail in the maturity time bands mandated by the 2013 ED was necessary for a particular lease portfolio, the judgement required by IFRS 7 in respect of maturity analyses should require the lessee to disclose this level of detail. On the other hand, for a lessee with a portfolio of long term leases, the annual commitments for the first five years (as required by the 2013 ED) may not provide investors with particularly useful information. In such a case, application of the judgement required by IFRS 7 would likely give rise to a different, and potentially more useful, set of time bands.

108. The main drawback of basing maturity analysis requirements for leases on the existing guidance of IFRS 7 is the potential effect on comparability. This is because, under the requirements of IFRS 7, different lessees are likely to disclose different maturity analyses. Nonetheless, given that investors have identified understanding liquidity risk and future cash flows as the reasons for needing a maturity analysis, the staff think that a balance needs to be found between achieving comparability and achieving the most useful information for investors in each individual case. In other words, liquidity profiles and future cash flow requirements are likely to be different for different entities and might be best represented by different sets of time bands.

109. Relying on the requirements of IFRS 7 would change the existing requirements in IAS 17 and the proposals in the 2013 ED in two ways:

(a) IFRS 7 requires judgement as to which time bands should be disclosed. The staff note that in a scenario for which the specific IAS 17 time bands provide the most useful information to investors, then applying the judgement required by IFRS 7 should lead a lessee to disclose this level of detail. Conversely, in a scenario for which an alternative set of time bands would provide the most useful information to investors, this should be disclosed. The staff acknowledge that, in some cases, application of IFRS 7 would result in a less comprehensive maturity analysis than today. However, we also think that there would be circumstances in which this approach would result in *more* disclosure than the existing requirements of IAS 17. This should be the case in situations for which more detailed disclosure provides useful information to investors.

(b) IFRS 7 requires disclosure of *undiscounted* commitments only and not a reconciliation to amounts reported on the balance sheet. The staff think that adopting this approach for leases is appropriate because it is consistent with the disclosure requirements for all other financial liabilities. In addition, we do not believe that the reconciliation itself provides any useful information to investors. At the June 2014 joint board meeting, the IASB tentatively decided to require a lessee to either present lease liabilities as a separate line item on the balance sheet or disclose this figure in the notes to the financial statements. This means that both the present value of lease liabilities *and* undiscounted maturities would be disclosed – the staff do not think that specific disclosure of a reconciling amount between the two provides any additional useful information.

Staff Recommendation

110. The staff recommend that the IASB eliminate the 2013 ED proposal to require a lessee to disclose a maturity analysis of lease liabilities, showing the undiscounted cash flows on an annual basis for each of the first five years and a total of the amounts for the remaining years. Instead, the staff recommend that the final leases standard should require a maturity analysis for lease liabilities in accordance with paragraphs 39 and B11 of IFRS 7 (see Appendix A of this paper). The staff also recommend inclusion of an explicit statement that a lessee should disclose this maturity analysis of lease liabilities separately from the maturity analyses of other financial liabilities.

Additional Qualitative Disclosures

Background

111. The qualitative disclosure requirements under IAS 17 require a lessee to disclose a general description of a lessee's leasing arrangements, including:

 (a) the basis on which contingent rental payments are determined;

 (b) the existence of renewal or purchase options and escalation clauses; and

 (c) restrictions imposed by leasing agreements (such as those concerning dividends, additional debt, and further leasing).

112. The 2013 ED proposed that a lessee provide the following qualitative disclosures:

 (a) Information about the nature of its leases (and subleases), including:

  (i) A general description of those leases;

  (ii) The basis, and terms and conditions, on which variable lease payments are determined;

  (iii) The existence, and terms and conditions, of options to extend or terminate the lease. A lessee should provide narrative disclosure about the options that are recognised as part of the ROU assets and lease liabilities and those that are not;

  (iv) The existence, and terms and conditions, of residual value guarantees provided by the lessee; and

  (v) The restrictions or covenants imposed by leases.

 (b) Information about leases that have not yet commenced, but that create significant rights and obligations for the lessee.

 (c) Information about significant assumptions and judgements made in applying the requirements of the leases standard, which may include the following:

(i) The determination of whether a contract contains a lease;

(ii) The allocation of the consideration in a contract between leases and nonlease components; and

(iii) The determination of the discount rate.

(d) The main terms and conditions of any sale and leaseback transactions.

(e) Whether an accounting policy election was made for the short-term lease exemption.

Feedback

113. Those investors that commented on the qualitative disclosure requirements proposed in the 2013 ED generally found them to provide useful information – particularly those requiring a lessee to disclose information about the basis on which variable lease payments are determined and the existence of renewal options.

114. However, there was some concern from preparers about the application and usefulness of these disclosures. These preparers stated that for a diverse lease portfolio presenting qualitative disclosures might be so generic that it would be impossible to provide any meaningful information. For example, a retailer consulted during outreach noted that it has over 6,000 leases of retail stores – a large proportion of these leases have unique terms and conditions.

115. Some constituents, including a few investors, added that the qualitative disclosure requirements could result in “boilerplate” statements rather than entity specific information for lessees that have large lease portfolios. Such disclosures would not be beneficial and would lengthen the notes to the financial statements. These constituents did not consider the qualitative disclosure requirements proposed in the 2013 ED as an effective way to achieve compliance with the overall lessee disclosure objective.

116. In addition, some preparers expressed concern that the qualitative disclosure requirements did not meet the cost-benefit test. These constituents assert that compiling, summarising, and providing the qualitative disclosures proposed in the 2013 ED would be costly for preparers and, at the same time, would not provide useful information to investors—especially when the qualitative disclosures result in generic statements.

117. As an alternative to the lessee qualitative disclosure requirements, some constituents suggested that the IASB take a principles-based approach to the qualitative disclosure requirements, noting that judgement should be applied by lessees and external auditors to determine the appropriate level of qualitative disclosures.

118. Some investors noted that they need better qualitative disclosures to understand the underlying economics of a lessee's business. Instead of the same mandatory qualitative disclosures for every lessee, they would prefer disclosures that are relevant to the particular lessee, which could vary from entity to entity. Some investors stated that qualitative information must be adequately quantified and sufficiently disaggregated to provide useful information for their analyses.

Staff Analysis

Overview

119. The overall lessee disclosure objective is to enable investors to understand the amount, timing, and uncertainty of cash flows arising from leases. Although quantitative disclosures are essential to achieving this objective, the staff think that qualitative disclosures are also needed to allow an investor to have a complete understanding of an entity's leasing activities when those activities are important to the entity's operations. This is because we think that qualitative disclosures should be used to explain any entity-specific information which is necessary to complement the quantitative information.

120. Nonetheless, the staff understand that it is difficult to provide relevant qualitative disclosures for entities with a large volume of diverse leases. In that case, it is likely to be costly to accumulate and disclose the terms and conditions of different agreements, when those terms and conditions are significantly different. Aiming for consistent and comparable qualitative disclosure across different lessees also has the potential to lead to the continued use of "boilerplate" statements reported as a concern in the feedback from both preparers and investors. In addition, we think that the information which investors would like to see consistently across all entities would be adequately addressed by the proposed quantitative disclosure package.

121. Consequently, the staff think that the overarching objective of the qualitative disclosure requirements is for lessees to disclose any *material* entity-specific information which is not covered by the information in the financial statements and the quantitative disclosure package. We think that this information will be different for different entities and we do not think that requiring specific mandatory qualitative disclosures (as was proposed in the 2013 ED) is the most effective way of achieving this objective.

122. Instead, the staff recommend that the qualitative disclosure requirements in the final leases standard should be based on a requirement for preparers to disclose sufficient information to satisfy a list of specified disclosure objectives (Appendix B). Judgement as to *how* these disclosure objectives are to be satisfied would then need to be made by individual lessees. The staff's initial thoughts on the drafting of this qualitative disclosure requirement are set out in Appendix B. Illustrative Examples demonstrating how lessees with different types of lease portfolios might comply with this qualitative disclosure requirement are set out in Appendix C.

Quality of disclosure

123. The staff think that an objectives based approach to qualitative disclosure has the potential to increase the quality of the information that is disclosed compared to existing requirements and what was proposed in the 2013 ED. This is because

this approach would instruct lessees to focus their disclosure efforts on qualitative information that significantly affects an investor's ability to understand the nature, timing, and uncertainty of lease cash flows, rather than potentially on disclosing information solely to meet a stated disclosure requirement. This point is best explained by way of example. Although the below analysis refers to one specific example from the 2013 ED, the staff note that a similar analysis could be applied to all of the specific qualitative disclosure requirements proposed in the 2013 ED.

124. The 2013 ED contained a requirement for disclosure of "the basis, and terms and conditions, on which variable lease payments are determined". The staff think that this disclosure is difficult to comply with in a meaningful way. This is because:

(a) A lessee with only a small number of leases containing variable payment terms would be able to comply with this disclosure requirement by providing a summary of the specific terms and conditions associated with each of those leases. However, in such a case, the existence of these terms and conditions is unlikely to be material and therefore disclosing them may distract attention from other, more significant, items of disclosure.

(b) Conversely, a lessee might have a very large number of leases with variable payment terms (in some cases those who provided comment letters on the 2013 ED reported hundreds or even thousands of leases with unique terms). In these cases, it would not be possible to comply with a requirement to disclose the terms and conditions of all of those leases. If a lessee attempted to do so it would result in an extremely lengthy disclosure which would be unlikely to meet the needs of investors. Preparing such a disclosure would also require a substantial amount of time and cost. The staff think it is likely that in these cases the lessee may conclude that compliance with the specific disclosure requirement is not possible and therefore disclose nothing, or just a "boilerplate" statement, regarding the existence of variable payment terms.

125. The staff think that, in this example, a requirement of compliance with an objective (to provide sufficient information to enable investors to understand the use of variable payment terms) would result in a better quality of disclosure than would be the case under the proposals in the 2013 ED. In complying with this requirement, the staff think that:

(a) A lessee with only a small number of leases containing variable payment terms would either disclose nothing (if these were judged to be immaterial) or would disclose the specific terms and conditions of these leases;

(b) A lessee with a large number of relevant leases would still conclude that it is impossible to disclose the specific variable payment terms associated with each of its leases. However, the staff think that an objectives based requirement would prevent such a lessee from disclosing nothing, or just a "boilerplate" statement. This is because such a lessee would be unable to conclude that compliance with this requirement is impossible. Instead, the lessee would need to consider what disclosure would give useful information to enable investors to understand its use of variable payment terms. Such a lessee might conclude that disclosure of *why* it uses variable payment terms and what its objectives are in negotiating such terms would satisfy this objective. Alternatively, if particular variable payment terms are consistent across the whole lease portfolio (or particular subsets of leases), the lessee might conclude that either (a) disclosure of a 'typical' set of variable payment terms or (b) a tabular disclosure of variable payment terms would best satisfy the objective.

126. The staff think that the outcome of applying an objectives-based approach would be a more concise and relevant set of qualitative disclosures than was proposed in

the 2013 ED. We think that this applies to all of the specific qualitative requirements proposed in the 2013 ED, and applies to both high and low volume lease portfolios.

Effect on costs

127. The staff have also considered the effect on costs of an objectives-based approach to qualitative disclosure requirements in the final leases standard. Materiality applies to all specific disclosure requirements in IFRS. This means that an entity is generally *not* expected to incur costs in complying with disclosure requirements that are immaterial, and this should hold true for any specific qualitative disclosure requirements included in the final leases standard. On this basis, it might be expected that an objectives-based approach would *not* give rise to any cost relief for lessees as compared to the inclusion of a list of specific mandatory disclosures.

128. Notwithstanding the above, the staff understand that, in practice, the existence of a list of specific disclosure requirements means that entities often spend time either generating these disclosures *or* demonstrating why they do not need to be prepared. Similarly, the audit of disclosures is often based on the use of a 'disclosure checklist'. Such checklists mean that auditors can spend time ensuring compliance with the checklist *or* gathering evidence as to why specific checklist items are not disclosed. The staff think that this can result in less time being spent considering how best to satisfy overall disclosure objectives because resources are necessarily focussed elsewhere.

129. The staff think that a qualitative disclosure requirement that is based on specific objectives would re-direct the focus so that time is spent in determining how best to satisfy the disclosure needs of investors for each lessee. Although costs would still be incurred in preparing qualitative disclosures, the staff think that this approach would enable that cost to be more effectively spent in producing meaningful qualitative disclosures, the volume of which is more weighted towards the importance and significance of the information for investors. In other words,

the staff think that this approach would lead to more significant qualitative disclosures when a lessee has significant leasing arrangements with more complex features, and little (if any) disclosure when the opposite is true. In that way, we think that the approach would help to ensure that costs incurred by lessees are weighted to reflect the significance of the information for investors.

Staff Recommendations and Questions for the IASB

Questions: Lessee Disclosure Requirements

Overall Disclosure Objective

1. Does the IASB agree with the staff recommendation that the final leases standard should retain the lessee disclosure objective proposed in the 2013 ED that the disclosures should enable investors to understand the amount, timing and uncertainty of cash flows arising from leases?

2. Does the IASB agree with the staff recommendation that the final leases standard should retain the statement in the 2013 ED requiring a lessee to consider the level of detail necessary to satisfy the disclosure objective?

Elimination of 2013 ED Disclosure Requirements

3. Does the IASB agree with the staff recommendation to eliminate the requirements proposed in the 2013 ED for a lessee to disclose reconciliations of its opening and closing balances of lease liabilities and ROU assets?

Quantitative Disclosure Table

4. Does the IASB agree with the staff recommendation to require a lessee to disclose the following quantitative amounts in a single tabular disclosure:

   (a) Lease expense, split between amortisation of ROU assets and interest on the lease liabilities;

   (b) Lease expense, split by class of underlying asset;

   (c) Short term lease expense

(d) Small asset lease expense;

(e) Variable lease expense;

(f) Sublease income;

(g) Total cash flow for leases;

(h) Additions to ROU assets;

(i) Weighted average remaining lease term;

(j) Gains and losses arising from sale and leaseback transactions

5. Does the IASB agree with the staff recommendation to require a lessee to disclose the closing carrying amount of ROU assets by class of underlying asset? This disclosure should be included within the quantitative disclosure table *or* within the note relating to the balance sheet line item in which ROU assets are presented (eg the Property, Plant and Equipment note).

Maturity Analysis of Lease Liabilities

6. Does the IASB agree with the staff recommendation to:

(a) eliminate the requirement proposed in the 2013 ED for a lessee to disclose a maturity analysis of the lease liability, showing the undiscounted cash flows on an annual basis for each of the first five years and a total of the amounts for the remaining years;

(b) introduce a requirement for a lessee to disclose a maturity analysis for lease liabilities in accordance with paragraphs 39 and B11 of IFRS 7. This would include an explicit statement that a lessee should disclose the maturity analysis of lease liabilities separately from the maturity analyses of other financial liabilities.

Additional Qualitative Disclosure Requirements

7. Does the IASB agree with the staff recommendation to:

(a) eliminate the list of mandatory qualitative disclosure requirements that was proposed in the 2013 ED;

(b) introduce a requirement for a lessee to disclose sufficient additional information (beyond that described above) to satisfy a list of particular disclosure objectives (Appendix B);

(c) include illustrative examples in the final leases standard to demonstrate how lessees with different types of lease portfolio might comply with the qualitative disclosure requirement?

Appendix A – Extracts from IFRS 7

A1 Extracts from IFRS 7 referred to in this paper are presented below:

IFRS 7 - Liquidity risk

39 An entity shall disclose:

(a) a maturity analysis for non-derivative financial liabilities (including issued financial guarantee contracts) that shows the remaining contractual maturities.

(b) a maturity analysis for derivative financial liabilities. The maturity analysis shall include the remaining contractual maturities for those derivative financial liabilities for which contractual maturities are essential for an understanding of the timing of the cash flows (see paragraph B11B).

(c) a description of how it manages the liquidity risk inherent in (a) and (b).

Application Guidance

B11

In preparing the maturity analyses required by paragraph 39 (a) and (b), an entity uses its judgement to determine an appropriate number of time bands. For example, an entity might determine that the following time bands are appropriate:

(a) not later than one month;

(b) later than one month and not later than three months;

(c) later than three months and not later than one year; and

(d) later than one year and not later than five years.

Appendix B – Example Drafting for Qualitative Disclosure Recommendations

B1 This appendix sets out the staff's initial thoughts on the drafting of the qualitative disclosure requirements and application guidance based on the staff recommendations described in paragraphs 111-129:

Disclosure

XX In addition to the quantitative disclosure requirements in paragraphs [x-x], a lessee shall disclose additional information about its leasing activities as necessary in order to meet the disclosure objective in paragraph [XX] of this standard. This may include, but is not limited to, disclosing information which enables users of financial statements to understand:

(a) the nature of leased assets;

(b) future cash outflows to which the lessee is potentially exposed that are not reflected in the measurement of the lease liability. This may include exposure arising from:

(i) the use of variable lease terms (see paragraph B1);

(ii) the use of extension options and termination clauses (see paragraph B2);

(iii) residual value guarantees (see paragraph B3);

(iv) leases not yet commenced to which the entity is committed;

(c) restrictions or covenants imposed by leases;

(d) sale and leaseback transactions (see paragraph B4).

Application Guidance

B1 Examples of additional information relating to variable lease payments that, depending on the circumstances, might be relevant to satisfying the disclosure objective in paragraph [X] includes information which enables users to understand:

(a) why these payments are used and their prevalence;

(b) the relative magnitude of variable lease payments to fixed lease payments;

(c) key variables upon which variable lease payment depend and how payments are expected to vary in response to changes in those key variables;

(d) any other operational and financial effect of these terms for the lessee.

B2 Examples of additional information relating to extension options and termination clauses that, depending on the circumstances, might be relevant to satisfying the disclosure objective in paragraph [X] includes information which enables users to understand:

(a) why these contract terms are used and their prevalence;

(b) the relative magnitude of lease payments associated with these contract terms that are and are not included in the measurement of the lease liability;

(c) any other operational and financial effect of these terms for the lessee.

B3 Examples of additional information relating to residual value guarantees that, depending on the circumstances, might be relevant to satisfying the disclosure objective in paragraph [X] includes information which enables users to understand:

(a) why these guarantees are provided and their prevalence;

(b) the nature of leased assets for which these guarantees are provided;

(c) how the residual risk is managed;

(d) any other operational and financial effect of these guarantees for the lessee.

B4 Examples of additional information relating to sale and leaseback transactions that, depending on the circumstances, might be relevant to satisfying the disclosure objective in paragraph [X] includes information which enables users to understand:

(a) why these transactions were entered into;

(b) key terms of sale and leaseback transactions;

(c) any lease payments not included in the measurement of the lease liability;

(d) the cash flow effect of sale and leaseback transactions for the lessee.

Appendix C – Illustrative Examples Relating to Qualitative Disclosure Recommendations

C1 The following examples illustrate how lessees with different types of lease portfolios might comply with the qualitative disclosure requirements recommended in this paper with respect to their variable lease payment terms. These examples illustrate *only* the qualitative disclosures discussed in paragraphs 111-129 of this paper.

Example 1—Lessee with a high volume of leases with a wide range of different terms

Entity X is a retailer that has a high volume of store property leases. These leases contain a wide range of different variable payment terms. Lease terms are negotiated and monitored by local management.

<u>Example Qualitative Disclosure</u>

Variable payment terms

Many of the property leases within the group contain variable payment terms. Local management are accountable for store margins and as such, lease terms are negotiated on an individual basis and contain a wide range of terms. Variable payment terms are used for a variety of reasons, including minimising the fixed cost base for newly established stores or for reasons of margin control and operational flexibility. Variable lease payment terms vary widely across the group:

- The majority of variable lease terms are based on a range of percentages of either store sales or EBITDAR;
- Lease payments based on variable terms range from 0% - 100% of total lease payments on an individual property;
- Some variable payment terms include minimum or cap clauses.

The overall financial effect of using variable payment terms is to concentrate rental costs in stores with higher sales. This facilitates the management of margins across the group.

The variable rent expense of £1,352m (20XX: £1,269m) is considered to be a fair representation of the level of variable rent expenses that are expected to be incurred in future years.

Example 2—Lessee with a high volume of leases with *some* consistent terms

Entity Y is a retailer that has a high volume of store property leases. Many of these leases contain variable payment terms linked to sales from the store. Group policy dictates the circumstances in which variable terms are used and all lease term negotiations must be approved centrally. Lease payments are monitored centrally.

Example Qualitative Disclosure

Variable payment terms

Many of the property leases within the group contain variable payment terms which are linked to the volume of sales made from the store. These terms are used where possible in order to match lease payments with stores generating higher cash flows. For individual stores, up to 100% of lease payments are on the basis of variable terms and there is a wide range of sales percentages used to calculate variable payments. In some cases, variable payment terms also contain minimum annual payments and caps.

Variable lease payments and terms for 20XX are summarised below:

	Number of stores	**Fixed payments 20XX**	**Variable payments 20XX**	**Total payments 20XX**
	No.	**CU'm**	**CU'm**	**CU'm**
Fixed rent only	1,490	1,153	-	1,153
Variable rent with no minimum	2,949	-	2,466	2,466
Variable rent with minimum	986	150	412	562
Variable rent with minimum and cap	140	41	19	60
	5,565	1,344	2,897	4,241

A 1% increase in sales across all stores in the group would be expected to increase total lease payments by approximately 0.6%-0.7%.

Example 3—Lessee with a high volume of leases with *some* consistent terms

Entity Z is a retailer that operates a number of different branded stores – A, B, C and D. Entity Z has a high volume of property leases. Group policy is to negotiate variable payment terms for newly established stores.

Example Qualitative Disclosure

Variable payment terms

Some of the property leases within the group contain variable payment terms that are linked to sales generated from the store. Variable terms are used where possible in newly established stores in order to link rental payments to store cash flows and minimise fixed costs. Fixed and variable rental payments by store brand are summarised below:

	Number of stores	Fixed payments 20XX	Variable payments 20XX	Total payments 20XX	Estimated impact on total rent of a 1% Increase in sales
	No.	CU'm	CU'm	CU'm	CU'm
Brand A	4,522	3,854	120	3,974	0.03%
Brand B	965	865	105	970	0.11%
Brand C	124	26	163	189	0.86%
Brand D	652	152	444	596	0.74%
	6,263	4,897	832	5,729	0.15%