IFRS

STAFF PAPER

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IFRS® Interpretations Committee meeting

Project	**Sale and Leaseback in a Corporate Wrapper (IFRS 16)**
Paper topic	Initial consideration

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Introduction

1. The IFRS Interpretations Committee (Committee) received a submission about the applicability of the sale and leaseback requirements in IFRS 16 *Leases* to a transaction in which an entity sells its equity interest in a subsidiary that holds only a real estate asset and then leases that real estate asset back.

2. The objective of this paper is to:
   - (a) provide the Committee with a summary of the matter;
   - (b) present our research and analysis; and
   - (c) ask the Committee whether it agrees with our recommendation not to add a standard-setting project to the work plan.

Structure of the paper

3. This paper includes the following:
   - (a) background information (paragraphs 5–15);
   - (b) outreach (paragraphs 16–17);
   - (c) staff analysis (paragraphs 18–39); and

(d) staff recommendation (paragraphs 40–41).

4. There are two appendices to this paper:

(a) Appendix A—proposed wording of the tentative agenda decision; and

(b) Appendix B—submission.

Background information

The fact pattern and transaction

5. The submission describes a situation in which:

(a) an entity (Entity P) owns 100% of the equity in a subsidiary (Entity S)—Entity S holds only one asset (a building) and has no liabilities; and

(b) the building held by Entity S does not meet the definition of a business (as defined in IFRS 3 *Business Combinations*).

6. Entity P enters into a transaction in which:

(a) it sells all of its equity interest (ie shares) in Entity S to a third party and, as a consequence, loses control of Entity S;

(b) it enters into a contract to lease the building held by Entity S back for a period of time;

(c) the transfer of the building satisfies the requirements in IFRS 15 *Revenue from Contracts with Customers* to be accounted for as a sale of the building; and

(d) the sales price equals the fair value of the building and exceeds its carrying amount.

The question

7. In the transaction described in paragraph 6 above, Entity P *legally sells its equity interest* in the subsidiary and then *leases the building back*. Because Entity P sells the equity interest rather than the building itself, the submitter asks whether, in its

consolidated financial statements, Entity P applies the sale and leaseback requirements in IFRS 16 (paragraphs 98–103) and thus asks how the gain on the sale is calculated.

8. If the sale and leaseback requirements apply, paragraph 100(a) of IFRS 16[1] would require Entity P to:

   (a) measure the right-of-use (ROU) asset at the proportion of the previous carrying amount of the building that relates to the right of use it retains; and accordingly,

   (b) recognise only the amount of the gain that relates to the rights transferred to the buyer-lessor.

9. Entity P loses control of its subsidiary as a consequence of the transaction. Applying IFRS 10 *Consolidated Financial Statements*, Entity P would recognise the entire amount of the gain from the sale of its equity interest in the subsidiary.

Example

10. To illustrate, assume Entity P owns 100% of the equity in Entity S (a subsidiary), which has only one asset—a building. The building has a carrying amount of CU500 at the date of the transaction. The net assets of Entity S are also CU500 (ie Entity S has no liabilities).

11. Entity P enters into a transaction in which:

    (a) it sells all of its equity interest in Entity S to a third party for CU800, losing control of the subsidiary—CU800 equals the fair value of the building at the date of the transaction;

[1] Paragraph 100(a) of IFRS 16 states that 'the seller-lessee shall measure the right-of-use asset arising from the leaseback at the proportion of the previous carrying amount of the asset that relates to the right of use retained by the seller-lessee. Accordingly, the seller-lessee shall recognise only the amount of any gain or loss that relates to the rights transferred to the buyer-lessor'.

(b) it leases the building back for a period of time. All payments for the lease are fixed and at market rates. The present value of those lease payments is CU600; and

(c) the transfer of the building satisfies the requirements in IFRS 15 to be accounted for as a sale of the building.

12. If the sale and leaseback requirements in IFRS 16 apply, Entity P would:

(a) measure the ROU asset at CU375[2], calculated as:

$$\underset{(\textit{carrying amount of the building})}{\text{CU500}} \times \frac{\underset{(\textit{present value of expected lease payments})}{\text{CU600}}}{\underset{(\textit{fair value of the building})}{\text{CU800}}}$$

(b) recognise a gain of CU75, calculated as:

$$\underset{(\textit{gain on sale of the building})}{\text{CU300}} \times \frac{\underset{(\textit{value of rights transferred to the buyer-lessor})}{\text{CU200}}}{\underset{(\textit{fair value of the building})}{\text{CU800}}}$$

13. The resulting entries at the date of the transaction would be as follows:

Dr. Cash		CU800	
Dr. ROU asset		CU375	
	Cr. Building		CU500
	Cr. Liability		CU600
	Cr. Gain on sale		CU75

[2] IFRS 16 does not specify how an entity determines the proportion of the previous carrying amount of the asset sold that relates to the right of use retained. In this example, we assume Entity P determines it is appropriate to calculate that proportion by comparing the present value of expected lease payments at market rates to the fair value of the building.

14. If IFRS 10 is applied to account for the loss of control of the subsidiary and the sale and leaseback requirements are not applied, Entity P would:

    (a) applying paragraph 25 of IFRS 10, derecognise the building (the only asset) and recognise a gain of CU300, calculated as CU800 (fair value of the consideration received for the equity interest in Entity S) – CU500 (carrying amount of the building); and

    (b) applying paragraphs 22−28 of IFRS 16, account for the lease (as a standalone lease) by recognising a ROU asset and lease liability both at CU600.[3]

15. The resulting entries at the date of the transaction would be as follows:

Dr. Cash		CU800	
Dr. ROU asset		CU600	
	Cr. Building		CU500
	Cr. Liability		CU600
	Cr. Gain on sale		CU300

Outreach

16. The purpose of any outreach we perform is to understand:

    (a) the prevalence of the transaction or fact pattern submitted; and

    (b) the accounting applied to that transaction or fact pattern.

17. We decided not to perform outreach on this request because:

    (a) we are aware through outreach performed in 2019 on other submissions and other available information that (i) single asset entities—holding real estate—are common in some jurisdictions (often structured in that way for

[3] It is assumed that CU600 represents the present value of lease payments, discounted at the lessee's incremental borrowing rate (and that the rate implicit in the lease cannot be readily determined).

tax reasons)[4]; and (ii) sale and leaseback transactions are common.[5] When sale and leaseback transactions occur, they often relate to high-value items of property, plant and equipment and are often highly structured. Accordingly, we concluded that the transaction described in the submission could be prevalent (either now or in the future) and could have a material effect on those affected.

(b) the submission relates to the application of IFRS 16 and, in the light of its effective date (annual reporting periods beginning on or after 1 January 2019), there is likely to be limited observable practice at this time with respect to the particular transaction described in the submission.

Staff analysis

Scope

IFRS 10

18. IFRS 10 includes requirements that apply when a parent loses control of a subsidiary. Paragraph 25 of IFRS 10 states:

> If a parent loses control of a subsidiary, the parent:
>
> (a) derecognises the assets and liabilities of the former subsidiary from the consolidated statement of financial position.
>
> (b) recognises any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant IFRSs. That fair value shall be regarded as the fair value on initial recognition of a financial asset in accordance with IFRS 9 or, when appropriate, the cost

[4] See paragraphs 11–14 of Agenda Paper 6 of the Committee's June 2019 meeting

[5] See paragraphs 13–16 of Agenda Paper 5 of the Committee's November 2019 meeting

> on initial recognition of an investment in an associate or joint venture.
>
> (c) recognises the gain or loss associated with the loss of control attributable to the former controlling interest.

19. In the transaction described in the submission (as illustrated in paragraphs 5–6 of this paper), Entity P controls Entity S before the transaction and, therefore, Entity S is a subsidiary of Entity P. Entity P loses control of Entity S by selling its 100% equity interest. Accordingly, the loss of control requirements in IFRS 10 apply to the transaction.

IFRS 16

20. Paragraph 98 of IFRS 16 states:

> If an entity (the seller-lessee) transfers an asset to another entity (the buyer-lessor) and leases that asset back from the buyer-lessor, both the seller-lessee and the buyer-lessor shall account for the transfer contract and the lease applying paragraphs 99–103.

21. In the transaction described in the submission, Entity P *transfers* the building (through the sale of its equity interest in Entity S) and leases that building back. Accordingly, the transaction is a sale and leaseback transaction as described in paragraph 98 of IFRS 16.

22. The fact that Entity P legally sells its equity interest in Entity S and then leases the building held by Entity S back does not, in our view, affect the applicability of the sale and leaseback requirements in IFRS 16. Entity P has *transferred* the building to the third party by selling its equity interest in Entity S—a consequence of the transaction is that Entity P loses control of the building held by Entity S (and thus derecognises the building in its consolidated financial statements) and the third party buyer obtains control of the building.

23. In addition, we note that the economic effect of the transaction is the same as if Entity P had directly sold its interest in the building held by Entity S and then leased the building back. Paragraph BC261 of IFRS 16 states (emphasis added):

> …The IASB observed that, in considering whether a transaction should be accounted for as a sale and leaseback transaction, an entity should consider not only those transactions structured in the form of a legal sale and leaseback, but should also consider other forms of transactions for which the *economic effect is the same* as a legal sale and leaseback…

24. Accordingly, the sale and leaseback requirements in IFRS 16 apply to the transaction.

Can the transaction be in the scope of both IFRS 10 and IFRS 16?

25. As discussed above, in our view Entity P's loss of control of Entity S is in the scope of IFRS 10 and the transaction is also a sale and leaseback transaction to which the sale and leaseback requirements in IFRS 16 apply. This is similar to the situation that arises when a sale and leaseback transaction involves the sale of an item of property, plant and equipment (PPE) that the selling entity leases back—for such a transaction, the transfer of the item of PPE is in the scope of the derecognition requirements in IAS 16 *Property, Plant and Equipment* and the transaction is also a sale and leaseback transaction to which IFRS 16's sale and leaseback requirements apply. Similarly, a sale and leaseback transaction that involves the sale of investment property that the selling entity leases back is in the scope of the derecognition requirements in IAS 40 *Investment Property* and also IFRS 16's sale and leaseback requirements.

26. In contrast, in June 2019 the Committee discussed a transaction that involves the sale of a parent's equity interest in a subsidiary that held only a real estate asset. In that transaction, the entity—as part of its ordinary activities—entered into a contract with a customer to sell the real estate by selling its 100% equity interest in the single asset subsidiary. The Committee considered whether IFRS 10 *or* IFRS 15 would apply to the transaction. This question arose because paragraph 5(c) of IFRS 15 excludes from its scope contractual rights and obligations within the scope of IFRS 10. Because of this explicit scope requirement, the transaction is within the scope of either IFRS 10

or IFRS 15; it could not be within the scope of both IFRS 10 and IFRS 15.[6] In contrast IFRS 16 does not exclude from its scope contractual rights and obligations within the scope of IFRS 10.

Applying the applicable requirements in IFRS 10 and IFRS 16

27. This section illustrates how, in our view, the entity applies the applicable requirements in IFRS 10 and IFRS 16. We have used the example described in paragraphs 10–11 of this paper to illustrate how an entity applies those requirements.

Step 1—Loss of control of the subsidiary

28. As part of the transaction, Entity P loses control of Entity S (a subsidiary). It therefore applies IFRS 10 to account for the loss of control. Paragraph 25 (see paragraph 18 of this paper) and paragraphs B97–B99 of IFRS 10 specify the accounting when an entity loses control of a subsidiary. Paragraph B98 states:

> If a parent loses control of a subsidiary, it shall:
>
> (a) derecognise:
>
> (i) the assets (including any goodwill) and liabilities of the subsidiary at their carrying amounts at the date when control is lost; and
>
> (ii) the carrying amount of any non-controlling interests in the former subsidiary at the date when control is lost (including any components of other comprehensive income attributable to them).
>
> (b) recognise:
>
> (i) the fair value of the consideration received, if any, from the transaction, event or circumstances that resulted in the loss of control;

[6] See paragraphs 20–26 of Agenda Paper 6 of the Committee's June 2019 meeting

(ii) if the transaction, event or circumstances that resulted in the loss of control involves a distribution of shares of the subsidiary to owners in their capacity as owners, that distribution; and

(iii) any investment retained in the former subsidiary at its fair value at the date when control is lost.

(c) reclassify to profit or loss, or transfer directly to retained earnings if required by other IFRSs, the amounts recognised in other comprehensive income in relation to the subsidiary on the basis described in paragraph B99.

(d) recognise any resulting difference as a gain or loss in profit or loss attributable to the parent.

29. Applying paragraph B98, Entity P derecognises the building held by Entity S and recognises the fair value of any consideration received. In the transaction described in the submission, Entity P receives cash and a lease (ROU asset and lease liability) as consideration for the transaction. Accordingly, Entity P records the following:

Dr. Cash		CU800	
Dr. ROU asset[7]		CU600	
	Cr. Building		CU500
	Cr. Liability[8]		CU600
	Cr. Gain on sale[9]		CU300

Step 2—Applying the sale and leaseback requirements

30. Paragraphs 98–103 of IFRS 16 apply to all sale and leaseback transactions. In the fact pattern described in the submission, the transfer of the building satisfies the

[7] Measured at fair value applying paragraph B98 of IFRS 10—in this example, it is assumed that the fair value of the ROU asset is the same as the fair value of the liability.

[8] Measured at fair value—in this example, assume Entity P calculates the fair value as the present value of expected lease payments (at market rates).

[9] Calculated as the difference between the consideration received (cash of CU800 plus net lease consideration (ROU asset and lease liability) of zero) less the carrying amount of the building of CU500.

requirements in IFRS 15 to be accounted for as a sale. Paragraph 100 of IFRS 16 states:

> If the transfer of an asset by the seller-lessee satisfies the requirements of IFRS 15 to be accounted for as a sale of the asset:
>
> (a) the seller-lessee shall measure the right-of-use asset arising from the leaseback at the proportion of the previous carrying amount of the asset that relates to the right of use retained by the seller-lessee. Accordingly, the seller-lessee shall recognise only the amount of any gain or loss that relates to the rights transferred to the buyer-lessor. …

31. Applying paragraph 100(a), Entity P measures the ROU asset arising from the leaseback at the proportion of the previous carrying amount of the building that relates to the right of use it retains.[10] As noted in paragraph 12 of this paper, Entity P has determined it is appropriate to calculate that proportion by comparing the present value of expected lease payments to the fair value of the building. Entity P therefore measures:

    (a) the ROU asset at CU375 (as illustrated in paragraph 12(a) above); and

    (b) the gain that relates to the rights transferred to the buyer-lessor at CU75 (as illustrated in paragraph 12(b) above).

32. Applying Step 1, the entity has measured the ROU asset at CU600 and the gain at CU300 (see paragraph 29 above). To meet the sale and leaseback requirements in

[10] Paragraph BC266 explains the Board's rationale for this requirement and states that, in a sale and leaseback transaction, the seller-lessee economically has transferred its interest in the value of the asset at the end of the leaseback and has retained the right to use the asset for the period of the leaseback.

IFRS 16, Entity P adjusts the measurement of both the ROU asset and the gain to the amounts specified by paragraph 100(a). Accordingly, Entity P records the following:

Dr. Gain on sale		CU225[11]	
	Cr. ROU asset		CU225[12]

Outcome of applying Step1 and Step 2

33. As a consequence of applying Step 1 and Step 2, in combination Entity P accounts for the transaction as follows:

Dr. Cash		CU800	
Dr. ROU asset		CU375	
	Cr. Building		CU500
	Cr. Liability		CU600
	Cr. Gain on sale		CU75

34. We note that the outcome of applying the above steps is the same as the outcome that results in situations in which an entity enters into a sale and leaseback transaction for an item of property, plant or equipment or an investment property—in these situations an entity applies the derecognition requirements in IAS 16 or IAS 40 and also applies the sale and leaseback requirements in IFRS 16.[13]

Summary

35. In the transaction described in the submission, the entity:

(a) applies paragraphs 25 and B97–B99 of IFRS 10 to account for the loss of control of the subsidiary; and

[11] Calculated as CU600 less CU375 (measurement applying paragraph 100(a) of IFRS 16).

[12] Calculated as CU300 less CU75 (amount determined applying paragraph 100(a) of IFRS 16).

[13] Paragraphs 68 and 69 of IAS 16 and paragraphs 67 and 69 of IAS 40 include references to the sale and leaseback requirements in IFRS 16.

(b) applies paragraph 100(a) of IFRS 16, measuring the ROU asset and gain recognised on the transaction as specified in that paragraph.

Other considerations

36. Some might suggest that recognising only the amount of any gain or loss on the sale that relates to the rights transferred to the buyer-lessor contradicts paragraph B98(d) of IFRS 10, which requires an entity to 'recognise any resulting difference as a gain or loss in profit or loss…'—in the transaction described in the submission, that difference specified by paragraph B98(d) of IFRS 10 would represent the full amount of the gain on sale of the building (CU300 in the example described in paragraph 11). It could be viewed that an entity is unable to simultaneously apply both IFRS 10 and IFRS 16 to the transaction described in the submission.

37. However, in our view the requirements are not contradictory and both sets of requirements are applicable to the transaction. In particular, we note that:

   (a) as illustrated above, an entity first applies the loss of control requirements in IFRS 10 and then overlays the sale and leaseback requirements in IFRS 16. In our view, overlaying the sale and leaseback requirements with the loss of control requirements does not mean that an entity no longer complies with (or that it contradicts) the loss of control requirements in IFRS 10. It means simply that there is another aspect to the loss of control transaction—ie the leaseback—which results in adjustments to some of the amounts that would otherwise result from applying the loss of control requirements in isolation.

   (b) there are other transactions that similarly are within the scope of more than one IFRS Standard and for which similarly one set of requirements applies as an overlay to another in calculating the gain or loss recognised on a transaction. For example, in 2018 the Committee discussed *Contributing Property, Plant and Equipment to an Associate* (IAS 28). Paragraph 68 of IAS 16 requires an entity to recognise the gain or loss arising from the derecognition of an item of PPE in profit or loss, and paragraph 71 of that

Standard specifies how to calculate that gain or loss (as the difference between the net disposal proceeds and the carrying amount of the item of PPE). However, paragraph 28 of IAS 28 *Investments in Associates and Joint Ventures* requires an entity to recognise gains and losses resulting from transactions between an entity and its associate or joint venture *only to the extent* of unrelated investors' interests in the associate or joint venture. The Committee's conclusion in that agenda decision confirms that on contributing an item of PPE to an associate (and consequently derecognising that item of PPE), an entity eliminates (or does not recognise) any gain or loss related to its own interest in the associate. The entity therefore recognises only the amount of any gain or loss that relates to unrelated investors' interests in the associate. In reaching conclusions on that submission, the Committee did not view the requirements in IAS 16 and IAS 28 as being contradictory.

Staff conclusion

38. In the transaction described in the submission, the entity:

(a) applies paragraphs 25 and B97–B99 in IFRS 10 to account for the loss of control of the subsidiary; and

(b) applies paragraph 100(a) of IFRS 16, measuring the ROU asset and gain recognised on the transaction as specified in that paragraph.

Question 1 for the Committee
1. Does the Committee agree with our analysis of the application of the requirements in IFRS Standards to the transaction described in the submission?

Should the Committee add a standard-setting project to the work plan?

Is it necessary to add or change requirements in IFRS Standards to improve financial reporting?[14]

39. Based on our analysis, we conclude that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine the accounting for a transaction in which it sells its equity interest in a subsidiary that holds only a real estate asset—losing control of that subsidiary—and leases the real estate asset back.

Staff recommendation

40. Based on our assessment of the work plan criteria in paragraph 5.16 of the *Due Process Handbook* (discussed in paragraph 39 of this paper), we recommend that the Committee does not add a standard-setting project to the work plan. Instead, we recommend publishing a tentative agenda decision that outlines how an entity accounts for the transaction described in the submission applying IFRS Standards.

41. Appendix A to this paper sets out the proposed wording of the tentative agenda decision. In our view, the proposed agenda decision (including the explanatory material contained within it) would not add or change requirements in IFRS Standards.[15]

Questions 2 and 3 for the Committee
2. Does the Committee agree with our recommendation not to add a standard-setting project to the work plan? 3. Does the Committee have any comments on the proposed wording of the tentative agenda decision in Appendix A to this paper?

[14] Paragraph 5.16(b) of the *Due Process Handbook*.

[15] Paragraph 8.4 of the *Due Process Handbook* states: 'Agenda decisions (including any explanatory material contained within them) cannot add or change requirements in IFRS Standards. Instead, explanatory material explains how the applicable principles and requirements in IFRS Standards apply to the transaction or fact pattern described in the agenda decision.'

Appendix A—proposed wording of the tentative agenda decision

Sale and Leaseback in a Corporate Wrapper (IFRS 16 *Leases*)

The Committee received a request about the applicability of the sale and leaseback requirements in IFRS 16 to a transaction in which an entity sells its equity interest in a subsidiary that holds only a real estate asset and then leases that real estate asset back. In the fact pattern described in the request:

a) an entity owns 100% of the equity in a subsidiary—the subsidiary holds only one asset (a building) and has no liabilities; and

b) the building held by the subsidiary does not meet the definition of a business (as defined in IFRS 3 *Business Combinations*).

The entity enters into a transaction in which:

a) it sells all of its equity interest in the subsidiary to a third party and, as a consequence, loses control of the subsidiary.

b) it enters into a contract to lease the building held by the subsidiary back for a period of time.

c) the transfer of the building satisfies the requirements in IFRS 15 *Revenue from Contracts with Customers* to be accounted for as a sale of the building.

d) the sales price equals the fair value of the building and exceeds its carrying amount.

The request asked whether, in its consolidated financial statements, the entity applies the sale and leaseback requirements in paragraphs 98-103 of IFRS 16 and, accordingly, recognises only the amount of the gain that relates to the rights transferred to the buyer-lessor.

Paragraph 98 of IFRS 16 states 'if an entity (the seller-lessee) transfers an asset to another entity (the buyer-lessor) and leases that asset back from the buyer-lessor, both the seller-lessee and the buyer-lessor shall account for the transfer contract and the lease applying paragraphs 99–103'.

In the transaction described in the request, the entity:

(a) transfers the building to the third-party buyer-lessor (through the sale of its equity interest in the subsidiary) and leases the building back. The transaction results in the entity losing control of the subsidiary, and consequently control of the building, which the buyer-lessor obtains. The transaction is therefore a sale and leaseback transaction as described in paragraph 98 of IFRS 16 to which the requirements in paragraphs 99-103 of IFRS 16 apply.

(b) loses control of the subsidiary—accordingly, the loss of control requirements in IFRS 10 *Consolidated Financial Statements* also apply to the transaction.

Consequently, the Committee concluded that, in the transaction described in the request, the entity:

(a) applies paragraphs 25 and B97-B99 of IFRS 10 to account for the loss of control of the subsidiary—in particular, paragraph B98 of IFRS 10 requires the entity to derecognise the building held by the subsidiary and recognise the fair value of the consideration received; and

(b) applies paragraph 100(a) of IFRS 16. The entity therefore (i) measures the right-of-use asset arising from the leaseback at the proportion of the previous carrying amount of the building that relates to the right of use it retains; and (ii) recognises only the amount of any gain that relates to the rights transferred to the buyer-lessor. The entity also recognises a liability at the date of the transaction, the initial measurement of which is a consequence of how the right-of-use asset is measured—and the gain on the sale and leaseback transaction determined—applying paragraph 100(a).

Illustrative example

Entity P owns 100% of the equity in Entity S (a subsidiary). Entity S holds only one asset—a building—at a carrying amount of CU500. The net assets of Entity S are also CU500 (ie Entity S has no liabilities). Entity P enters into a transaction in which:

(a) it sells all of its equity interest in Entity S to a third party for CU800, losing control of the subsidiary—CU800 equals the fair value of the building at the date of the transaction;

(b) it leases the building back for a period of time. All payments for the lease are fixed and at market rates. The present value of the lease payments is CU600; and

(c) the transfer of the building satisfies the requirements in IFRS 15 to be accounted for as a sale of the building.

Applying paragraph B98 of IFRS 10, Entity P derecognises the building held by Entity S and recognises the fair value of the consideration received.

Applying paragraph 100(a) of IFRS 16, Entity P measures the right-of-use asset arising from the leaseback at the proportion of the previous carrying amount of the building that relates to the right of use it retains. Entity P determines that it is appropriate to calculate that proportion by comparing the present value of the expected lease payments to the fair value of the building. On this basis, the proportion of the building that relates to the right of use retained is 75%, calculated as CU600 (present value of the expected lease payments) ÷ CU800 (fair value of the building). Consequently, the proportion of the building that relates to the rights transferred is 25%, calculated as (CU800 – CU600) ÷ CU800.

Applying paragraph 100(a), Entity P:

(a) measures the right-of-use asset at CU375, calculated as CU500 (carrying amount of the building) × 75% (proportion of the building that relates to the right of use it retains); and

(b) recognises a gain of CU75 at the date of the transaction, which is the gain that relates to the rights transferred to the buyer-lessor. This gain is calculated as CU300 (total gain on sale of the building (CU800 – CU500)) × 25% (proportion of the building that relates to rights transferred).

At the date of the transaction, Entity P accounts for the transaction as follows:

Dr. Cash	*CU800*	
Dr. Right-of-use asset	*CU375*	
Cr. Building		*CU500*
Cr. Liability		*CU600*
Cr. Gain on rights transferred		*CU75*

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for the entity to determine its accounting for the transaction described in the request. Consequently, the Committee [decided] not to add a standard-setting project to the work plan.

Appendix B—submission

B1. We have reproduced the submission below, and in doing so deleted details that would identify the submitter of this request.

Issue

Accounting for the sale of a real estate entity with a leaseback

General fact pattern

Parent (P) wholly owns 100% of Subsidiary (S). S was established some time ago and only holds a real estate asset which does not constitute a business (as defined in IFRS 3).

P sells 100% of its shares in S to a third party (A) and leases the real estate asset back from S. Under IFRS 10, P loses control over S at the time the shares are transferred. The transfer of the real estate asset would meet the requirements to be accounted for a sale by P (the seller-lessee) and would follow the accounting requirements in paragraph 100 of IFRS 16.

The sales price exceeds the carrying amount of the transferred asset, resulting in a gain from the sale.

Question

Does the sale and leaseback guidance in IFRS 16 apply, or does the IFRS 10 guidance relating to the accounting for loss of control of a subsidiary apply?

Current practice

We have identified two potential accounting treatments for such a fact pattern.

View 1

Proponents of View 1 are of the view that the IFRS 16 sale and leaseback guidance applies since there has been a transfer of an asset from P to S. They believe that IFRS 16 is applicable irrespective of whether the transfer is executed through an asset or share deal, since the substance is the same in this fact pattern.

This View is consistent with IFRS 16 paragraph BC261 which notes that “The IASB observed that, in considering whether a transaction should be accounted for as a sale and leaseback transaction, an entity should consider not only those transactions structured in the form of a legal sale and leaseback, but should also consider other forms of transactions for which the economic effect is the same as a legal sale and leaseback ”.

Under IFRS 16, the gain from the sale and leaseback is recognised in accordance with paragraph 100(a), resulting in the seller-lessee recognising the amount of any gain only to the extent that it relates to the rights transferred to the buyer-lessor.

View 2

Proponents of View 2 argue that the IFRS 16 sale and leaseback guidance does not apply as this transaction is legally the sale of shares, which should be accounted for in accordance with IFRS 10.

Under IFRS 10, paragraph 25(a), P derecognises the assets and liabilities of S, and recognises the gain associated with the loss of control.

P subsequently follows the lessee guidance in IFRS 16, paragraph 22 to account for the lease it has entered into with S.

Reasons for the Interpretations Committee to address the issue

Sale and leaseback accounting is widespread and for those entities affected, the difference in accounting models (ie recognising a gain upfront versus spreading it) could be significant. Where the amount of the gain is material, it could significantly affect financial performance both in the period of the sale and leaseback transaction occurs, and in subsequent periods during the term of the lease. We believe that financial reporting would be improved if the applicable accounting model was made clear. This would result in greater comparability amongst entities would also limit any structuring opportunities designed to achieve a particular accounting outcome. We believe that this issue is narrow in scope and can be resolved in a cost effective and efficient manner by the IFRIC within the confines of IFRS standards and the Conceptual Framework for Financial Reporting. We are unaware of any current or planned IASB project that will directly address this issue.