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## Post-implementation review of IFRS 16 Leases ('PIR of IFRS 16')

### Cover Note

#### Objective

- 1 The objectives of this session are to:
  - (a) seek EFRAG FR TEG-CFSS members' additional views on the questions the IASB will raise at the forthcoming September ASAF meeting (see agenda paper 07-03) and input in addition (or in contrast) to the preliminary one collected so far and summarised from paragraph 9 to 13 below;
  - (b) assess the prevalence and the relevance of the application issues identified and summarised from paragraphs 14 to 15 below (and listed in the Appendices 2 and 3) in the EFRAG FR TEG-CFSS members' jurisdictions – and, for those jurisdictions where assessment is still in progress, to understand the expected timeline; and
  - (c) explore whether EFRAG CFSS members are aware of or organising any future outreach or technical discussions in their jurisdiction related to the PIR of IFRS 16 in response to the IASB PIR of IFRS 16 (the EFRAG Secretariat preparatory work is exhibited here as a source of information for such an outreach/discussion).

#### Structure of the session and the related agenda papers

- 2 From paragraph 4 to 7, an overview of the IASB project and of the EFRAG Secretariat's preparatory work in anticipation of the IASB Post-Implementation Review of IFRS 16 Leases ("PIR of IFRS 16") is provided.
- 3 Further, in preparation of the ASAF questions in 07-03, the EFRAG Secretariat provided for this session, and for background purposes only, the following papers:
  - (a) **Agenda paper 07-02**, which aims to provide an overview of the general messages and the preliminary issues identified during the EFRAG Secretariat's preparatory work.
  - (b) **Agenda paper 07-04**, which summarises the results from the EFRAG Preparers' Survey on IFRS 16 Leases presented at the EFRAG FR TEG-User Panel joint meeting on 24 May 2024

- (c) **Agenda paper 07-05**, which summarises the results from the EFRAG Users' Survey on IFRS 16 Leases presented at the EFRAG FR TEG-User Panel joint meeting on 24 May 2024;

These papers formed the basis for the EFRAG Secretariat initial assessment of the ASAF questions summarised from paragraph 9 to 15.

### Background of the IASB project

- 4 In June 2024 the IASB started the PIR of IFRS 16 and is planning to conduct outreach with consultative groups and other stakeholders to inform a request for information, whose publication of the Request for Information ("RFI") is expected in the first half of 2025.
- 5 For further information about the project please refer to the ASAF paper contained in 07-03.

### Overview of EFRAG Preparatory work

- 6 As further detailed in slide 5 of the agenda paper 07-02, EFRAG's preparatory work started in February 2024 and is expected to continue until the issuance of the IASB RFI (H1 2025). It aims at developing a preliminary list of application challenges and proposed recommendations that will be further discussed, categorised and prioritised by EFRAG FR TEG and EFRAG FRB in preparation of EFRAG comment letter in response to the IASB RFI.
- 7 Further information about the overall messages received from stakeholders and a list of the preliminary application challenges raised during the outreach is provided in the agenda paper 07-02.

### EFRAG Secretariat initial assessment of the ASAF questions

- 8 The following paragraphs reflect the feedback collected so far through the EFRAG's online surveys, at previous EFRAG FR TEG, CFSS and EFRAG Working Groups meetings and other outreaches held with preparers, auditors and users as listed in the Appendix 1.

#### *ASAF Question 1 - Overall assessment of IFRS 16*

- 9 The feedback collected so far indicated that IFRS 16 has mainly achieved its objective - to ensure that lessees and lessors provide relevant information in a manner that faithfully represents leases – although some requirements are still challenging to apply and stakeholders provided mixed feedback based on their background, industry and relevance of lease contracts. In particular:
- (a) Preparers operating in the most impacted industries (e.g., retail and real estate) expressed some concerns about the outcome arising from the application of IFRS 16 (e.g. the fact that relevant amounts of variable lease payments are not included in the lease liability calculation) and the high level of judgment, which might impair comparability among entities (e.g. discount rates, lease term). Further, some preparers highlighted that IFRS 16 increased deviation between internal and external reporting.
- (b) Users of financial statements said that IFRS 16 is working well, it improves information comparability, it provides useful information and a more faithful

presentation of lease transactions in the financial statements. However, some users (e.g., valuation specialists) still prefer using pre-IFRS 16 figures for their analysis.

- (c) Auditors highlighted that the implementation phase required a lot of effort from the entities to develop new internal procedures to collect data and to understand the requirements. Further, they noted that some application issues exist, but they could go beyond the scope of this PIR.
- 10 To date many implementation issues raised at first time application have been addressed – e.g. through IFRS Interpretation Committee’s agenda decisions and well-established practice developed over the last years. Therefore, stakeholders expressed mainly limited appetite for fundamental changes and highlighted that addressing the remaining issues might go beyond the scope of this PIR.
- 11 Finally, differences between IFRS and US GAAP still remain. However, enhanced disclosures could help users in dealing with the lack of comparability.

*ASAF Question 2 - Cost-benefit analysis and transition to IFRS 16*

- 12 Overall, costs and benefits associated with the implementation and application of IFRS 16 are mainly aligned with those expected by the IASB when IFRS 16 was issued. In particular:
- (a) From preparers’ side, limited benefits were perceived, and they were mainly related to the internal control system (e.g., improved internal controls and monitoring of leases, better understanding of lease contracts portfolio, improved transparency and data quality on leases). Further, they noted that IFRS 16 implementation was too costly and complex (e.g., data collection, IT tools and staff training) and that on-going costs are still relevant (e.g., IT tools and data collection continuous updating, additional challenges in case of business acquisition, IT integration needs within the group).
  - (b) From users’ side, reduced costs for obtaining useful information on leases were noted and, overall, IFRS 16 increased, albeit to varying degrees among different entities and industries, the relevance and the transparency of the information and improved users’ ability to estimate future cash flows as well as information on the entity’s profitability. Further, overall users noted an improvement in terms of information comparability, both between entities and between leased and purchased asset.
- 13 Commenting on transition to IFRS 16, stakeholders welcomed the options provided under the transition requirements (e.g., modified retrospective approach) and some simplifications (e.g., in determining discount rates) which helped them in reducing workload and complexity that would be otherwise needed under the full retrospective initial application. Feedback was different depending on the industry. Indeed, the majority of respondents to our survey applied the modified retrospective method, including practical expedients, mainly because it was less costly and complex to apply.

*ASAF Question 3 - Application issues and interactions with other IFRS Accounting Standards*

- 14 The main sources of concern raised by stakeholders include:
- (a) *The high level of judgment which may lead to diversity in practice*, for example with reference to the determination of the lease term and of the discount rate;

- (b) *Too complex and burdensome accounting requirements*, mainly in relation to the contract modifications and the low-value asset contract disclosure;
  - (c) *Lack or limited guidance in IFRS 16*, for example in relation to sale and leaseback transactions and to the distinction between variable and in-substance fixed payments;
  - (d) *Substance of the transaction not properly reflected in the financial statements*, for example with reference to the presentation of the lease payments in the statement of cash flows and the determination of the appropriate ROU asset depreciation period for those leases that combine fixed and variable lease payments; and
  - (e) *The interaction with other IFRS Accounting Standards*, including those critical interactions already highlighted by EFRAG in previous recent PIRs (e.g. PIR of IFRS 15 and IFRS 9)
- 15 Appendices 2 and 3 of this cover note include a table who summarises, respectively, the application issues and the interactions with other IFRS Accounting Standards raised by the stakeholders for EFRAG FR TEG and CFSS members further consideration in terms of:
- (a) Their relevance (i.e., the issue materially affects users of financial statements' ability to analyse trends and compare entities) and prevalence (i.e., widespread diversity in practice exists) in your jurisdiction;
  - (b) Their pervasiveness in your jurisdiction (e.g. it affects transactions that occur frequently in various industries); and
  - (c) How the IASB should address the issue (e.g. narrow standard-setting activity, submission to the IFRS Interpretation Committee, educational material, additional guidance).

For further details about the preliminary issues identified, please refer to the agenda paper 07-02.

### Questions for EFRAG FR TEG and CFSS

#### EFRAG Secretariat specific questions

- 16 Do EFRAG FR TEG-CFSS members agree with the EFRAG Secretariat analysis summarised from paragraph 9 to 13 above? Do you have additional input in relation to the overall assessment of IFRS 16 and the cost-benefit analysis that the EFRAG Secretariat should consider in its preparatory work?
- 17 Among those detailed in the agenda paper 07-02 and listed in the Appendices 2 and 3:
- (a) which are the application issues and interactions with other IFRS Accounting Standards that are particularly prevalent and relevant in your jurisdiction?
  - (b) In your view, how the IASB should address them?
- Please refer to paragraph 15 above. For those jurisdictions starting or planning to work on this PIR project (where assessment is still in progress) could you please envisage the timeline for the assessment.
- 18 Are there other relevant application issues and interactions with other IFRS Accounting Standards besides those detailed in the agenda paper 07-02 and listed in the Appendices 2 and 3? If yes, how the IASB should address them?
- 19 Are EFRAG FR TEG-CFSS members aware of any initiative or outreach in their local jurisdictions in preparation of the IASB's RFI and that might inform the EFRAG Secretariat's preparatory work?

The IASB ASAF questions are contained in full in the agenda paper 07-03.

#### Next steps

- 20 The EFRAG Secretariat will continue to monitor the IASB project and to collect feedback from various stakeholders to assess to which extent the identified issues are widespread and relevant to the EU stakeholders.

#### Agenda Papers

- 21 In addition to this cover note, agenda papers for this session are:
- (a) Agenda paper 07-02 – PIR IFRS 16 - Issues paper – List of the preliminary issues;
  - (b) Agenda paper 07-03 – PIR IFRS 16 - IASB ASAF paper;
  - (c) Agenda paper 07-04 – Summary of responses - EFRAG Preparer's Survey on IFRS 16 Leases - EFRAG FR TEG-User Panel joint meeting 24-05-14.pdf (for background purpose only); and
  - (d) Agenda paper 07-05 – Summary of responses - EFRAG Users' Survey on IFRS 16 Leases - EFRAG FR TEG-User Panel joint meeting 24-05-14.pdf (for background purpose only);

## **Appendix 1 – Detailed list of outreach activities**

- 1 Since January 2024, the EFRAG Secretariat conducted several outreaches that can be summarised as follows:
  - (a) French preparers operating in the retail industry (January 2024)
  - (b) Meeting with EFRAG FR TEG-CFSS (March 2024)
  - (c) Italian preparers operating in the retail industry (July 2024)
  - (d) German preparers operating in the automotive industry (April and May 2024)
  - (e) Members of the International Valuation Standards Council (March 2024)
  - (f) Meeting with representatives of large audit firms (March-April 2024)
  - (g) Meeting with the European Public Real Estate Association (EPRA) (July 2024)
  - (h) Meeting with Leaseurope (April 2024)
  - (i) Meeting with National Standard Setters (NSS) (April-May 2024)
  - (j) Meeting with EFRAG FR TEG and User Panel (May 2024)
  - (k) Meeting with EFRAG FIWG, EFRAG Academic Panel and EFRAG IAWG (May 2024)
  - (l) Meeting with Italian National Standard Setter (OIC)' working groups (June – July 2024)
  - (m) Meeting with French National Standard Setter (ANC)' working groups (June – July 2024)
  - (n) Meeting with EFRAG RRAWG (July 2024)
- 2 Furthermore, EFRAG got input during the April 2024 International Forum of Standard-setters (IFASS) meeting (see meeting report [here](#) - Item 15 from page 61).

**Appendix 2 – Summary of the application issues further explained in the agenda paper 07-02**

#	Description of the issue	Impacted Industries	Source of concern
<i>Application difficulties and lack of consistent application</i>			
1	Determining the discount rate	Across industries	Survey, IFASS (All panellists), Outreaches
2	Determining the lease term	Across industries	Survey, IFASS (All panellists), Outreaches
3	Identifying lease contracts	Across industries	Survey, IFASS (All panellists), Outreaches
4	Separating lease and non-lease components	Across industries	Survey
<i>Lack of guidance is leading to diversity in practice</i>			
5	Sale and leaseback transaction	Across industries	Survey, IFASS (All panellists), Outreaches (auditors)
6	Determining the lease payments	Retail industry	Survey, Outreaches (preparers and auditors)
7	Non-monetary consideration	Real estate	Survey, IFASS (China, France), Outreaches (auditors)
8	Distinction between lease and in-substance purchase of assets:	Across industries	Survey, IFASS (France)
9	Accounting for expenditures incurred before the leased assets became operational	Across industries	Survey, IFASS (China)
10	Accounting for leases with non-consecutive lease periods	Retail industry	IFASS (China)
<i>Too complex and burdensome accounting requirements</i>			
11	Contract modification	Retail industry	Survey, IFASS (China, France), Outreaches (preparers and auditors)
12	Low-value asset lease exemption	Across industries	Survey, IFASS (France), Outreaches (mainly preparers)
<i>Substance of the transaction not properly reflected in the FS</i>			
13	Determination of the appropriate ROU asset depreciation period	Retail industry	IFASS (China), Outreaches (preparers)
14	Presentation requirement in the CF statement	Across industries	Survey, Outreaches (users)

**Appendix 3 – Summary of the interactions with other IFRS Accounting Standards further explained in the agenda paper 07-02**

Standard	Short description of the issue	Type of issue	Impacted Industries	Already reported in previous PIR or project
IFRS 9	Distinction between a lease modification (IFRS 16) and extinguishment of a lease liability (IFRS 9) arising from a rent concession	Lack of guidance in the standard	Across industries	Yes
	Application of the ECLs model under IFRS 9 to lease liabilities from the lessor's perspective	Lack of guidance in the standard	Across industries	Yes
IFRS 15	Sale and leaseback transaction	Application difficulties and lack of consistent application	Real estate and retail industry	Yes
	Identifying components in lease contracts and scope	Application difficulties and lack of consistent application	Real estate and retail industry	Yes
IAS 16	Different level of certainty in assessing optional periods to define the depreciation period	Inconsistency across standards	Across industries	
	Definition of initial direct costs	Inconsistency across standards	Across industries	
IAS 36	Application of the impairment test requirements	Lack of consistent application	Across industries	
IFRS 3	Accounting for lease contracts in the context of a business combination	Lack of consistent application	Across industries	Yes
IFRS 10	Sale and leaseback of a single asset entity through corporate wrapper	Lack of consistent application	Across industries	Yes
IAS 37	Accounting for onerous lease contracts	Lack of guidance in the standard	Across industries	
IFRS 11	Accounting for leases in context of joint operations	Lack of consistent application	Oil&Gas	