

AS 19 - Leases

(4-6 marks)

7 Definition of Lease

A lease is an agreement whereby the lessor (legal owner) conveys to the lessee the right to use an asset for a period of time in return for a payment or series of payments.

eg: BB Sis gives studio on rent to AK Sis for 5 years @ \$ 5,00,000 per annum.

↓ ↓

lessor (owner) lessee (tenant)

- lease rentals/
- lease payment
- Minimum lease payment

Chapter Overview

↓
Two types of lease 
Operating lease
Finance lease

⑥ Operating lease (It is like a rent agreement) → Jisne rent pe diya hai uske liye income hai
jisne asset rent pe liya hai uske liye exp.

Journal entries

<u>Yr leud</u> Lease Payable A/c Dr TO Int Inc (PII)	<u>Yr leud</u> Int Exp A/c Dr TO lease Payable
<u>Yr leud</u> ClB A/c Dr TO lease Payable	<u>Yr leud</u> Lease Payable A/c Dr TO ClB.

Yr lend Asset is now in AK's
Books in case of Fin lease

Depn Alc D₂
TO PPE Alc.

2] Scope

This standard applies to all leases other than:

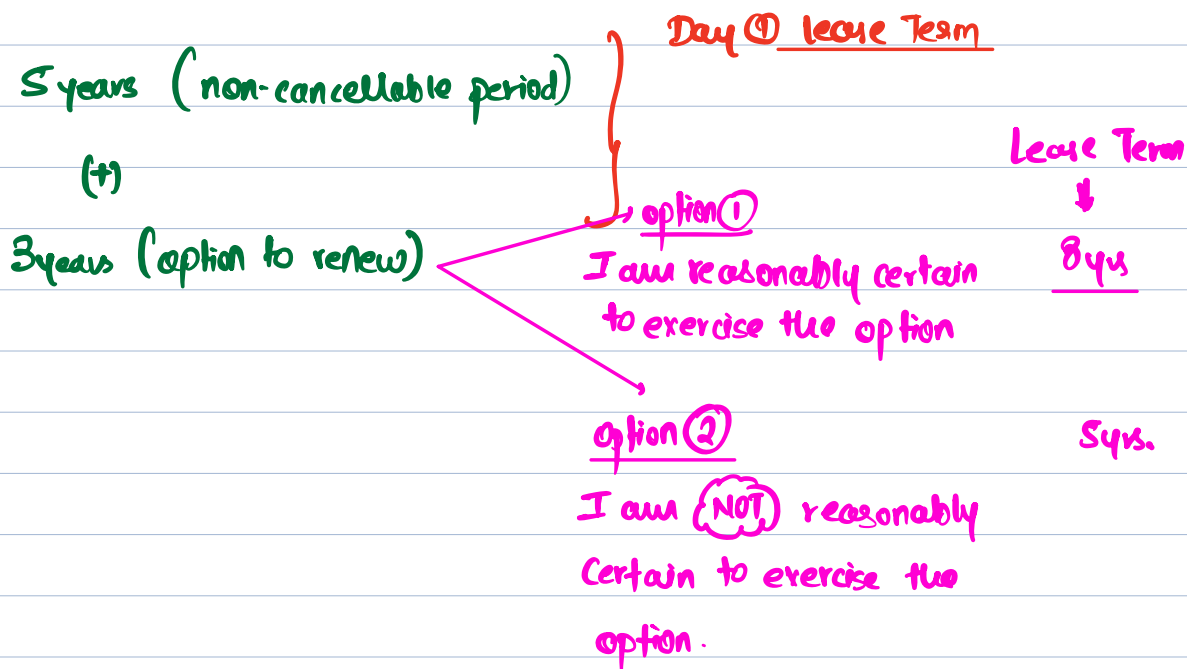
- ⑥ lease agreement to explore or use of natural gas/resources eg: oil, gas, minerals etc.
- ⑥ licensing agreement for items such as motion picture films, video recordings, plays, manuscripts, patents & copyrights.
- ⑥ lease agreement to use Lands.

3] Important terms

⑥ leave team

It includes non-cancellable period (+) Renewal period (if reasonably certain to exercise)

eg: BB Sia _____, AK Sia
(lessor) (lessee)



⑥ Lease Payments / Lease Rentals / Minimum lease Payments

lessor	lessee
1] <u>Fixed lease Rentals</u> ^{Eg ①}	1] <u>Fixed lease Rentals</u>
2] <u>Guaranteed Residual Value (GRV)</u> ↳ GRV given by lessee - Eg ② ↳ GRV given by independent 3rd party ↳ Eg ③	2] <u>Guaranteed Residual Value (GRV)</u> ↳ GRV given by lessee
3] <u>Renewal option / Purchase option payment</u> Eg ④ Eg ⑤	3] <u>Renewal option / Purchase option payment</u>

Eg ① Fixed Lease Payments

BB sis gave studio on lease to Ak sis for 3yrs. Rentals every year were as follows:

yr	Lease Rent
1	10L
2	11L
3	13L

→ Fixed lease Rentals → Iska Amount Day ① se pata hota hai.

Eg ② GRV

Ak sis gives Ferrari (car) on lease to Mow Ltd for 30L p.a. for 3 years.
(lessor) (lessee)

Guaranteed Residual value → 15L @ the end of 3rd year.
(To ensure proper usage)

Lease Rent	yr	L.R
	1	30L
	2	30L
	3	30L + 15L ↓ GRV.

Eg ③ Iphone purchased by Ak from Flipkart → Day ① BuyBack offer from Flipkart

Ak gave iphone on lease to kushal
(lessor) (lessee).

No GRV promised by kushal.

↓
(After 3 years Flipkart will BuyBack iphone @ ₹18k).

yr	L.R (Given)
1	30k
2	30k
3	30k

Lessor		Lessee	
yr	L.R	yr	L.R
1	30k	1	30k
2	30k	2	30k
3	30k + 18k	3	30k

GRV 3rd party

Ex 4 BB sis gave his studio on lease to AK sis for 5 years @ £5L p.a.
 BB sis also gave an option to renew for another 3 years @ £4L p.a.
 for the renewal period. It is reasonably certain that renewal option
 will be exercised. Calculate L.R for each year.

yr	L.R
1	5L
2	5L
3	5L
4	5L
5	5L
6	4L
7	4L
8	4L

} It is a part of lease Rentals only if it is reasonably certain to renew for 3 years.

Eg ⑤ BB Sia gave studio on lease to AK Sia for 5yrs @ ₹5L p.a.

BB Sia also gave an option to purchase the studio @ the end of 5 years @ ₹18L

AK Sia is reasonably certain to exercise the purchase option

Yr	L.R
1	5L
2	5L
3	5L
4	5L
5	5L + 18L

AK Sia is NOT reasonably certain to exercise the purchase option

Yr	L.R
1	5L
2	5L
3	5L
4	5L
5	5L + 18L

4] Types of leases

Operating lease

→ Does not trf risks & rewards of the asset
It is like a normal serv agreement

Finance lease

↳ Trf of Risk & rewards

• It is like a purchase/sale of asset on loan/EMI Basis.

⑤ Indicators of Finance lease

(These are 5 conditions, if any 1 is met, then it is a Finance lease)

① Ownership

If lessor transfers the ownership of the asset to the lessee @ the end of lease term.

(eg: BB Sia gave classroom on rent for 5 yrs & at the end of 5 yrs ownership of asset will be transferred to AK Sia)

② Purchase option

If lessee has an option to purchase the asset at a price which is expected to be lower than fair value & it is reasonably certain that the option will be exercised. (Sasta purch option (+) certainty that it will be exercised)

Eg: BB Sia gave studio on lease for 5 yrs @ ₹5L and at the end of 5th yr AK Sia has option to purchase the ^{P.A.} asset @ ₹1L (Mkt value 50L). It is reasonably certain that purchase option will be exercised.

③ Lease term

(75% or more) / 60% ^{in icai ques}

If lease term is for major part of economic life of the asset.

Eg: AK Sia gave Ferrari on lease to BB Sia for 8 yrs (Total life = 10 yrs)
Lease term covers 80% of life $\left(\frac{8 \text{ yrs}}{10 \text{ yrs}} \times 100 \right) \rightarrow$ It is fin lease.

Eg: Same as above except lease term is 4 yrs.

Lease term covers 40% of life $\left(\frac{400}{1000} \times 100\right) \rightarrow$ It is Not a Fin lease

*** Present value

(D) PV of Minimum lease Payments (90% or more)

At inception of the lease, if present value of MLP Substantially covers the fair value of asset, then it is Fin. lease.

Eg: Ak sis gave Ferrari on lease to BB sis for ₹ 40L p.a for 3 years.
(lessor owner)

Fair value of asset on Day 0 = 1 cr.

D.F @ 10%.

Yr end	L.R (MLP)	D.F @ 10%	PV
1	40L	0.909	36.36L
2	40L	0.826	33.04L
3	40L	0.751	30.04L
PV of MLP			<u>99.44L approx</u>

Fair Value 1 cr (Given)

% of PV of MLP = $\frac{99.44L}{100L} \times 100 = 99.44\%$ $\therefore$ It is a Fin lease.

Eg ② Ak Ferrari, Max 1H (F.V = 1cr)
3 years.

L.R = 30L p.a. GRV = 25L D.F @ 10%.

Calculate PV of MLP to check whether FL or Not.

<u>Solⁿ:</u>	yr	L.R	D.F@10%	PV
	1	30L	0.909	
	2	30L	0.826	
	3	30L + 25L	0.751	

93.35L approx.

$$\% \text{ of PV of MLP} = \frac{93.35}{100} \times 100 = 93.35\% \text{ approx}$$

↙
Fair
value

↓
It is a F.L.

⑤ Specialised Nature

The leased asset is of a specialised nature such that only lessee can use it without major modifications being made.

eg: BB sis studio Ak sis

↓
Modifications

- king size bed
- Swimming Pool
- Water proof fishes
- multiplex for movies
- Rangan light

Because asset is of
specialised nature
(only useful for lessee)
∴ It is a Fin. lease.

Note: If **none** of the above 5 indicators are met, then it is an operating lease.

⑥ Accounting for finance lease

→ Lessee Books
→ Lessor Books.

① Lessee Books

Journal entries

Day ①

① Asset	Atc	Dr	xx	} lower of: PV of MLP or Fair Value
	To lease Payable / lease Liability		xx	

② Yrend

Int Exp Atc Dr
To lease Liability

lease Liability Atc Dr
To ClB Atc.

③ Deprn

Deprn Atc Dr
To Asset/PPE

→ If ownership trf to lessee after lease term → Depreciate over full useful life of asset
→ If ownership NOT trf after lease term → Depreciate over lease term or useful life (whichever is lower)

Extra Entry

PLC Atc Dr
To Int Exp
To Deprn.

Note: Initial Direct Cost → Add to cost of Asset taken on lease → PPE xx
(incurred by lessee) To ClB xx

lessee

lessor

Ex ① Aditya Ltd took an asset on lease from Harsh Ltd for 5 years.

Asset Fair value = ₹10,00,000

lease Rentals are ₹250,000 p.a. (payable @ the end of each year).

GRV @ the end of lease term promised by lessee is ₹50,000.

D.F @ 10%.

Calculate lease Liability in the Books of Aditya Ltd & also calculate Interest charges for each year end (Assume Fin lease)

Solⁿ: In the Books of Aditya (lessee)

Yr 1

<u>Day ①</u>	Asset A/c Dr	978550	} WN ①
	To lease Liability A/c	978550	

<u>Yr end</u>	Int Exp A/c Dr	97855	} WN ②
	To lease Liability	97855	
	lease Liability	250000	
	To CB	250000	

Deprn	195710
To PPE	195710
(978550/5yr)	

Extra

P/L	293565
To Deprn	195710
To Int	97855

WN① Calculation of lease liability

lower of: Fair value = 10,00,000

or

PV of MLP : 978550

Yr end	L.R.	DF @ 10%	PV
1	250000	0.909	227250
2	250000	0.826	206500
3	250000	0.751	187750
4	250000	0.683	170750
5	250000 + 50000 ↓ GRV	0.621	186300
		PV	<u>978550 approx</u>

WN② Calculation of Interest & repayment.

Yr end	Opening lease Liab	Int/Finance charges @ 10% ↓ Disc. Factor	Repayment/ Instalment/ lease Rep payment	closing of lease Liab.
1	978550	97855	(250000)	826405
2	826405	82641	(250000)	659046
3	659046	65905	(250000)	474951
4	474951	47495	(250000)	272446
5	272446	27245 (309) → approx adj	(250000) (50000)	NIL

Assumed that GRV will also paid.

4r2

4r2nd Int Exp Alc Dr 82641
 To lease Liability 82641

lease Liability 250000
 To clB 250000

Deprn 195710
 To PPE 195710
(978550/5yrs)

Ex19a PIL 278351
 To Deprn 195710
 To Int 82641

Q1 → H.W

Q2 → In the books of lessee (S. Square)

i) Calculation of lease Liability

4r end	L.R	D.F @ 15%	PV
1	625000	0.8696	543500
2	625000	0.7561	472563
3	625000	0.6575	410937
4	625000 + 125000 ↓ GRV	0.5718	428850
			<u>18,55,850 approx</u>

Journal entry

Day ① Asset Acc Dr 1855850
 TO lease Liab 1855850

Int Exp Acc Dr 278378
 TO lease Liability 278378

lease Liability 625000
 TO CLB 625000

Deprn 463963 $\left(\frac{1855850}{4yrs} \right)$
 TO PPE 463963

PIL 742341
 TO Deprn 463963
 TO Int Exp 278378

wn 2 Calculation of Interest Expense & Repayment for each year.

Yr end	Opening lease Liab	Int/Finance charge @ 15% ↓ Disc. Factor	Repayment/ Instalment/ lease Rent payment	Closing of lease Liab.
1	1855850	278378	(625000)	1509228
2	1509228	226384	(625000)	11,10,612
3	11,10,612	166592	(625000)	652204
4	652204	97831 (35) approx adj	(625000) (125000)	NIL

Assumed that GRN was also paid.

Ques 4 (LDR)

i) Calculation of Lease Liability

4r end	Lease Rentals	D.F@ 10%	PV
1	350000	0.909	
2	350000	0.826	
3	350000	0.751	
4	350000 + 70000 GRV	0.683	
			PV 11,56,960 approx

Journal entry

Day ①

Asset (Maulino) A/c Dr	1150000
To lease liability	1150000

(lower of: Fair value = 11,50,000
or
PV of MLP 1156960

⑧ Lessor Accounting

Hint: Its calculation is different from lessee. So don't mix it up.

Journal Entries (Lessor Books, Finance lease)

Day ① Lease Receivable A/c Dr } @ Net Investment
To PPE A/c

Yr end Lease Receivable
To Int Income

Yr end CIB A/c Dr
To Lease Receivable A/c.

Yr end : Deprn (Nali aayego)

Extra J-E

Int Income A/c Dr
To P/L

Important terms

① Gross Investment = Minimum lease Payments (+) UGRV (Unguaranteed Res. value)
lease + GRV
Rent
P.V = 100, GRV = 60
UGRV = 40 (Bif)

$$\textcircled{2} \text{ Net Investment} = \text{PV of Gross Investment} \\ = \text{PV of MLP's} + \text{PV of UGRV}$$

$$\textcircled{3} \text{ Unearned Finance Income} = \text{Gross Investment} (-) \text{Net Investment}$$

Eg Shlok took an asset on lease from Daksh Ltd



lessee



lessor

Lease Rentals = 10L p.a. (excluding GRV)

Residual value = 1,00,000, GRV = 80,000, UGRV = 20,000

Lease Term = 5 yrs, DF@ 10%

Pass J-E on Day ① & Y end in the Books of Daksh Ltd (lessor)
(Assume Fin lease). Also calculate unearned finance income.

Solⁿ: In the Books of lessor

$$\text{i) Gross Investment} = \text{MLP} + \text{UGRV} \\ = 51,00,000$$

$$\text{ii) Net Invest} = \text{PV of G.I} \\ = 38,52,879$$

$$\text{iii) Unearned Finance Income} = \text{G.I} (-) \text{N.I} \\ = 51,00,000 (-) 38,52,879 \\ = 12,47,121$$

Not Booked on Day 1. This is computed for disclosure purpose.

<u>WNI</u>	<u>Yr end</u>	<u>Lease Rentals</u>	<u>D.F@ 10%</u>	<u>PV</u>
	1	10,00,000	0.909	
	2	10,00,000	0.826	
	3	10,00,000	0.751	
	4	10,00,000	0.683	
	5	10,00,000 + 80000 + 20000	0.621	
		<u>80000</u> GRV <u>20000</u> UGRV		
		<u>51,00,000</u> ↓ Gross Invest		PV = 3852100 approx or 3852879 approx ↓ Net Investment

JE.

Day ① Lease Releable A/c Dr 3852879
TO PPE A/c 3852879 } Net Inst

4r leud	Lease Reable	385288	Exro
	TO Int Income	385288	Int Inc 385288
			TO PU 385288
4r leud	CIB Alc Dr	10,00,000	
	TO Lease Reable	10,00,000	No Depm

wn 2 Calculation of Interest Income & Instalments

Year end	Opn Bal of lease Payable	Int Income @ 10%	Repayment (lease Rent received)	Clb. Bal.
1	3852879	385288	(10,00,000)	3238167
2	3238167	323817	(10,00,000)	25,61,984
3	2561984	256198	(10,00,000)	18,18,182
4	18,18,182	181818	(10,00,000)	10,00,000
5	10,00,000	1,00,000	(10,00,000)	NIL
		<u>1247121</u>	(200000)	
		/	(200000)	
		Unearned Fin Income	Assumed GRV & UGRV is rec'd	

Ques 5 (lessor) → Fin lease (Unearned Fin. Income was asked)

∴ It is a hint that Accounting in the Books of lessor is asked under Finance Lease.

(₹ in lakhs)

$$1] \text{ Gross Investment} = \text{Minimum lease Payments (+) UGRV (without PV)}$$

$$= 43 \text{ lakhs}$$

$$2] \text{ Net Investment} = \text{PV of Gross Investment}$$

$$= 28.31 \text{ lakhs}$$

$$3] \text{ Unearned Finance Income} = \text{Gross Invest (-) Net Invest}$$

$$= 14.69 \text{ lakhs}$$

WN ①

Yr end	Lease Rent	D.F @ 15%	PV
1	8	0.8696	6.96
2	8	0.7561	6.05
3	8	0.6575	5.26
4	8	0.5719	4.57
5	8 + 1.6 + 1.4	0.4972	5.47
	↓ GRV UGRV		28.31 approx ↓ Net Invest
	43 ↓ Gross Invest		

7. Special Cases in lessor Accounting (Fin lease)

a) Annual Lease Rent is missing?

Whenever annual lease rent is missing we assume that cost of equipment will be recovered through PV of L.P & PV of UGRV

i.e. Cost of equipment = PV of lease Payments + PV of UGRV

$$\text{Annual L-R} = \frac{\text{PV of L-P}}{\text{Annuity factor of lease Term}}$$

Q6 (LOR)

Annual lease payments → Missing

Cost of equipment = PV of lease Payments + PV of UGRV

$$16,99,999.50 = \text{PV of L-P} + 100,300$$

(133500 × D.F of 3rd yr @ 10%)

$$16,99,999.50 - 100300 = \text{PV of L-P}$$

$$= 15,99,699.50$$

$$\text{i) Annual lease Rent} = \frac{15,99,699.50}{\cancel{3\text{yr}} 2.486}$$

$$\text{Annual lease Rent} = \frac{\text{PV of L-R}}{\text{Annuity factor of 3yrs}}$$

<u>Extra Post</u>	<u>yr</u>	<u>L-R</u>	<u>(x) D.F @ 10% =</u>	<u>PV</u>
	1		0.909	
	2		0.826	
	3		0.751	
			2.486	15,99,699.50
			Annuity factor.	

$$L.R \times \underline{D.F} = PV$$

$$L.R \times 2486 = 15,99,699.50$$

$$L.R = \frac{1599699.50}{2486}$$

$$= 643483.$$

$$ii) \text{ Unearned Finance Income} = GI (-) N.I$$

$$= 2063949 (-) 16,99,999.50$$

$$= 363949.5$$

<u>Yr</u>	<u>L.R</u>	<u>D.F @ 10%</u>	<u>PV</u>
1	643483	0.909	
2	643483	0.826	
3	643483 + 133500	0.751	
	<u>UGPV</u>		
	2063,949		16,99,999.50
	GI.		

Hint:

Q7 (LOR) i) Annual L.R ii) Indicator's check iii) UFI.

i) Annual Lease Rent

Cost / FV of equipment = PV of Lease Payments + PV of UGRV

$$10,00,000 = \text{PV of L-P} + 75130$$

$$\text{PV of L-P} = 924870 \quad (1L \times 0.7513)$$

$$\text{Annual L.R} = \frac{\text{PV of L-P}}{\text{Annuity factor of 3yrs}}$$

~~3yrs~~
Annuity factor of 3yrs

$$= \frac{924870}{2.4868}$$

$$= 371912$$

ii) Check whether finance lease or Not (5 conditions, Any 1 to be met)

a) Ownership Not getting trf @ the end of lease term

b) There is NO purchase option @ the end of lease term

c) lease term should cover major part of life = $\frac{\text{lease term}}{\text{life}} \times 100$ as per IAS its major
 $= \frac{3\text{yrs}}{5\text{yrs}} \times 100 = 60\%$
90% ↓ Not major.

d) PV of MLP should cover substantially the fair value of asset.

$$\frac{\text{PV of MLP}}{\text{Fair value}} \times 100 = \frac{924870}{1000000} \times 100 = 92.49\% \text{ approx} \rightarrow \text{It is a finance lease.}$$

e) Asset is not of specialised nature.

Since 4th condition is met $\therefore$ it is a finance lease.

$$\begin{aligned}
 \text{iii) } \underline{\text{Unearned Finance Income}} &= \text{Gross Invt} - \text{Net Invt} \\
 &= 1215736 - 10,00,000 \\
 &= 215736
 \end{aligned}$$

<u>WY</u>	<u>Yr</u>	<u>L.R</u>	<u>DF@ 10%</u>	<u>PV</u>
	1	371912	0.909	
	2	371912	0.826	
	3	371912 + 1000000 ↓ UGRV	0.751	
		<u>12,15,736</u> ↓ GI.		<u>10,00,000 approx</u> ↓ NI

(Interest Rate)

⑧ Discounting factor is missing

In this case we find IRR (Internal rate of return). It is a rate where Day 1 Fair Value = PV of future lease rentals & PV of UGRV. (includes GRV)
Here, we do trial & error to find the rate & also follow interpolation technique.

→ Internal Rate of Return
Eg: (Find Interest rate / IRR)

Annual Lease Rent = 1,00,000 @ the end of the year

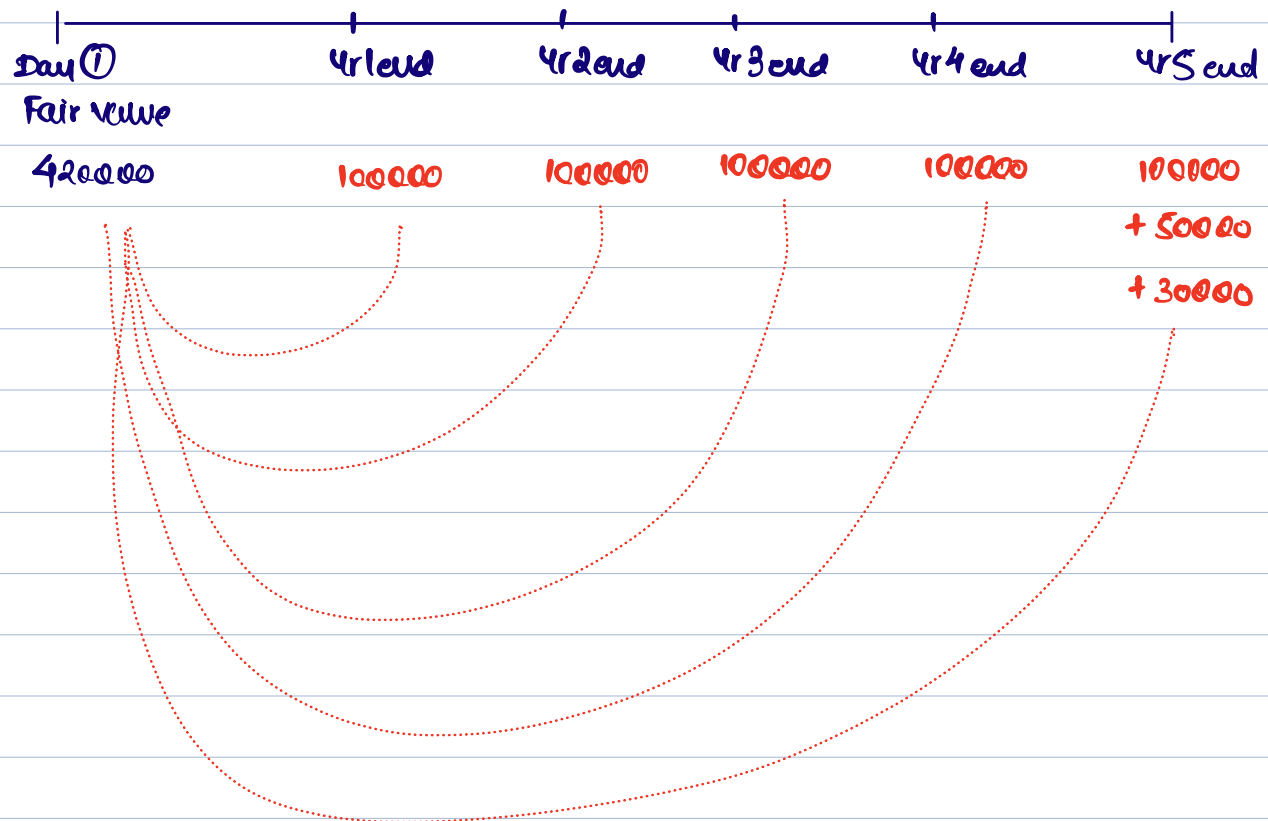
Lease term = 5 yrs

GRV = 50,000

UGRV = 30,000

Fair Value @ the Beg = 4,20,000

Find Interest Rate / IRR



Discount the cash flows of 5 years @ such rate that PV should be equal Day 0 FV i.e. 420,000



Now we will start trial & error

Assume D.F @ 10%

yr	L.R	D.F @ 10%	PV
1	100,000	0.909	90,900
2	100,000	0.826	82,600
3	100,000	0.751	75,100
4	100,000	0.683	68,300
5	100,000 + 50,000 + 30,000	0.621	111,780

428,680 😞

Assume DF@12%.

yr	L.R	DF@12%	PV
1	100000	0.893	
2	100000	0.797	
3	100000	0.712	
4	100000	0.636	
5	100000 + 50000 + 30000	0.567	

405872 approx. 😞

10% → PV 428680
12% → PV 405872 } inke beech mein hai 420000

By using interpolation = $10\% + \frac{428680 - 420000}{428680 - 405872} \times (12\% - 10\%)$

BODMAS

Bracket open Divide Multiply Add Subs.

$= 10\% + \frac{8680}{22808} \times 2\%$ } 1st Divide

$= 10\% + 0.38 \times 2\%$ } 2nd Multiply

$= 10\% + 0.76$ } 3rd Add.

$= \boxed{10.76\%} \rightarrow \text{Disc factor / IRR / Int Rate.}$

Q.10 (Wk)

Discount lease Rent, GRV, UGRV @ such rate that present value should come to £2,00,000 (Fair value)

Assume 10%.

yr	L.R	D.F @ 10%	PV
1	50k		
2	50k		
3	50k		
4	50k		
5	50k + 25k + 15k		

214376 approx 😞

Assume 12%.

yr	L.R	D.F @ 12%	PV
1	50k		
2	50k		
3	50k		
4	50k		
5	50k + 25k + 15k		

202936 approx

Assume 14%.

yr	L.R	D.F @ 12%	PV
1	50k		
2	50k		
3	50k		
4	50k		
5	50k + 25k + 15k		

192429 approx.

10% → 214376 X

12% → 202936

14% → 192426

} → inke Beech mein hai 200000

By using interpolation, $12\% + \frac{202936 - 200000}{202936 - 192426} \times (14\% - 12\%)$

$$= 12\% + \frac{2936}{10510} \times 2\%$$

$$= 12\% + 0.28 \times 2\%$$

$$= 12\% + 0.56$$

$$= \boxed{12.56\%} \text{ approx}$$

8. Accounting for operating lease

→ lessee Books

→ lessor Books

lessee

Day ① No entry

Yr end Lease Rent Exp Alc Dr

To ClB

lessor

Day ① No entry

Yr end ClB Alc Dr

Lease Equilisation Dr (BIF)

To Lease Rent income

To Lease Equi (BIF)

[As 19 suggests to Book lease rent income/exp on SLM Basis unless any other method is more appropriate]

↓
Straight Line method.

4r end Deprn
 To PPE } useful life.
 cost

(lessee)

(lessor)

Eg: AK sis took studio on lease from BB sis for 5 years. It is an operating lease

Lease Rent	yr	L.R.
	1	100000
	2	110000
	3	120000
	4	130000
	5	140000
		<u>600000</u>

Soln: In the Books of BB sis (lessor)

Avg Rent p.a = $\frac{600000}{5 \text{ years}}$ = 120000 p.a.
 (Sim Basis)

Journal entries

4r end ClB Alc Dr 1,00,000

← Lease Equilisation Alc Dr. 20000

BB
current
asset

To lease Rent income (PIU) 120000

4r 2nd ClB Alc Dr 110000

Lease Equilisation Alc 10000

To lease Rent income (PIU) 120000

Yr 3 end ClB Ac Dr 120000

 To lease Rent income (PIU) 120000

Yr 4 end ClB Ac Dr 130000

 To lease Rent income (PIU) 120000

 To lease Equilisation Ac. 10000

Yr 5 end ClB Ac Dr 140000

 To lease Rent income (PIU) 120000

 To lease Equilisation Ac. 20000

Lessee Books (In the Books of Ak sis)

Yr 1 end lease Rent Exp 120000

 To ClB 100000

 To lease Equilisation 20000

→ Bls Current Liab

Yr 2 end lease Rent Exp 120000

 To ClB 110000

 To lease Equilisation 10000

Yr 3 end lease Rent Exp 120000

 To ClB 120000

Total Rent = 120000

	Yr1	Yr2	Yr3
output	10000 units	20000 units	30000 units

Lease Rent 20000 40000 60000

to be Booked

In P/L $\left(\frac{120000 \times 10000}{60000} \right)$ $\left(\frac{120000 \times 20000}{60000} \right)$ $\left(\frac{120000 \times 30000}{60000} \right)$

Yr1 end (Lessee Book)

Lease Rent Exp Ac Dr 20000

Lease Equilisation Ac Dr 20000

To CIB Ac 40000

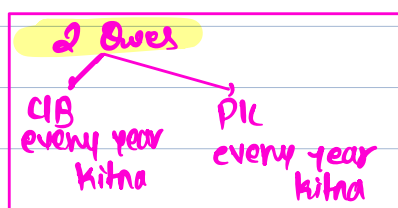
Yr2 end Lease Rent Exp Ac Dr 40000

To CIB Ac 40000

Yr3 end Lease Rent Exp Ac Dr 60000

To CIB Ac 40000

To Lease Equilisation Ac 20000



Q11 (10K)

Op lease (3 years) life of Asset (5 yrs)

⑥ Calculation of Annual Lease Rent

Cost of Machine	150000
(+) Profit Margin (30%)	45000
	<u>195000</u>

The life of asset is 5 years but we are giving on lease only for 3 yrs.
∴ Proportionate rent will be recovered in the ratio of output &
not in the ratio of years.

~~195000 → 5 yrs
? 3 yrs~~

Yr output

1 40000

2 50000

3 60000

4 80000

5 70000

3,00,000 units

Total
Lease Period output = 150000 units.

Total lease Rent for 3 years = $195000 \times \frac{\text{output of 3 yrs}}{\text{Total output}}$
= $195000 \times \frac{150000 \text{ units}}{300000 \text{ units}}$

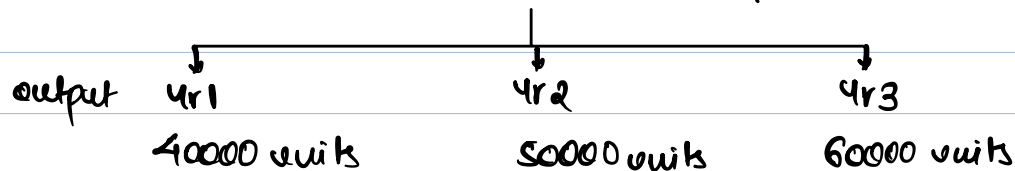
$$= 97500$$

$$\text{Annual lease Rent} = \frac{97500}{3\text{year}}$$

$$= 32500 \rightarrow \text{Yeh CIB ka amount hai every year.}$$

⑥ Lease Rent income to be booked each year

$$\text{Total Rent} = 97500 \text{ (for 3yrs)}$$



lease Rent income to be booked in PIL	26000	32500	39000
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<u>Extra</u>	<u>yr1</u>	CIB	32500
		TO lease income	26000
		TO lease Eq.	6500

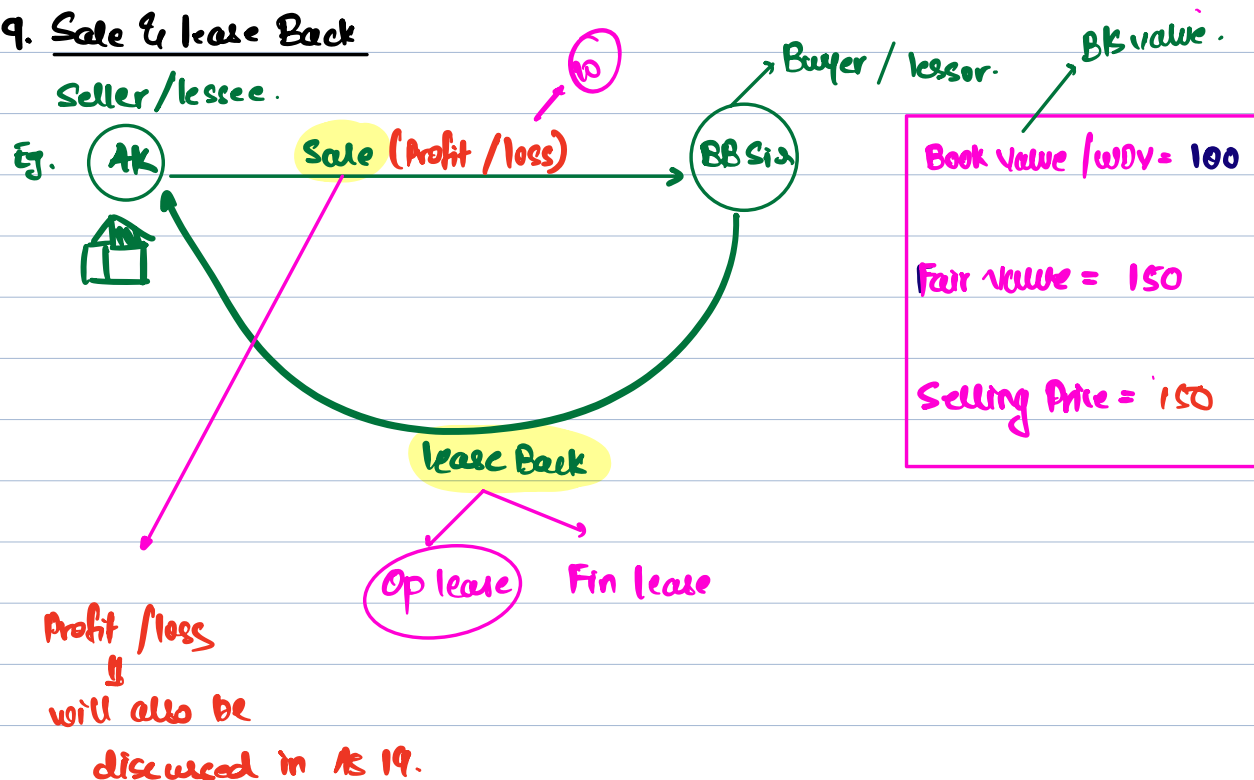
⑦ Depreciation for 3years

Deprn is always charged on the cost of machine (i.e. ₹ 150000) over useful life of asset is 5 yrs. & not 3yrs.

In ques deprn method is suggested in ratio of output.

Yr	Deprn	
1	20000	$(150000 \times \frac{40000}{200000})$
2	25000	$(150000 \times \frac{50000}{200000})$
3	30000	
4	40000	
5	35000	
	<u>150000</u>	

9. Sale & lease Back



A] Sale Done & lease back results in Finance lease

Profit/loss on sale is to be amortised & booked over the lease term in the proportion of deprn.

B] Sale Done & leaseback results in Operating lease



We will discuss how to treat profit/loss on sale

Case ① Sale Price = Fair value	Case ② Sale Price is less than Fair value	Case ③ Sale Price is more than Fair value
Profit/loss on sale can be recognised immediately	⑥ If there is profit, Book immediately. ⑦ If there is loss & such loss is compensated by future lease payments @ Below market rate, Then such loss should be deferred & Booked in proportion of future lease payment. (If loss But no compensation of less rentals, then Book loss immediately)	• Profit/loss upto Fair value can be booked immediately. • Excess profit (i.e. Selling price over Fair value) should be deferred & Booked over the period for which asset is expected to be used
In case 1 & 2, Compare S.P & w.D.V to calculate profit		<u>Hint:</u> • $F.V(-) w.D.V / B.V = \text{xx}$ Profit/loss Book immediately. • $S.P(-) F.V = \text{Profit}$ Defer.

Eg: Asset WDV / BV = 100

i) S.P. = 120, FV = 120

→ Case ① $FV = S.P$

→ Profit = 20 → Book immediately

ii) S.P. = 120, FV = 130

→ Case ② S.P less than F.V

Profit = 20 → Book immediately

(S.P-way)

iii) S.P. = 90, FV = 110

→ Case ② SP less than FV

loss = 10
(S.P-way)

→ If loss compensated by future lease payments at below mkt rate, then defer loss

→ otherwise trf loss immediately to P/L.

iv) S.P. = 150, FV = 130

Case 3

→ 30
↳ FV - WDV → Book immediately
(130 - 100)

↳ S.P. - FV = 20 → Defer
150 - 130

v) S.P. = 140, FV = 90

→ Case ③

i) (10 loss) → Book immediately

(FV - WDV)

90 100

ii) SO Profit → Defer

(SP - FV)

140 - 90

Ques 12 (W.R)

Hint:

Case kounsa hai uske liye compare S.P & FV
Profit / loss ke liye compare (S.P & WDV)

① Case ① : Profit (S.P - WDV) = 50 Lakh - 40 L
(SP = FV) = 10 Lakh (Book immediately)

② Case ② a) → Profit (S.P - WDV) = 50 L - 40 L
(Selling price less than Fair value) = 10 L Profit (Book immediately)

③ Case 2 b) → loss (S.P - WDV) = 38 L - 40 L
= (2 L) loss

(If loss compensated by future lease payment at below mkt rate, then defer, otherwise book immediately in P/L)

④ Case 3 :
(Selling price more than FV) → Profit (FV - WDV) = 40 (-) 40 = 10 → Book immediately
Profit (S.P - FV) = 50 - 40 = 10 Profit (Defer)

e) Case ③
(Selling price more than FV) → Profit (FV - WDV) = 46L - 40 = **6** → Book immediately

Profit (S.P - FV) = 50L - 46L = **4** → Profit Defer

f) Case ③
(Selling price more than FV) → **loss** (FV - WDV) = 35L - 40L = **5** (loss) → Book immediately

Profit (S.P - FV) = 39L - 35L = **4** profit (Defer)

10. Other Misc Points

a) Contingent Rent

If lease rent is based on future sales/future profits etc, then such rentals will be booked in P/L as & when received/paid.

b) Initial Direct Cost

Cost which are incurred for entering into lease. (eg: Brokerage, legal fees, etc.)

Accounting treatment

→ If incurred by lessee (under Fin lease) → Add to cost of Asset taken on lease.

→ All other cases → Trf to P/L

e) Normally lease Rentals are paid @ the end of the year
(eg: L.R = 1L, L.T = 3yrs, D.F @ 10%)

Yr	Lease Rent	D.F @ 10%	PV
1	1L	0.909	
2	1L	0.826	

→ If rentals are paid @ the **Begin** of the year.

Yr	Begin	L.R	D.F @ 10%
1		1L	0.909 1
2		1L	0.909
3		1L	0.826

3 1L 0757

