AS-19 - SUMMARY CHART

L34

Lease :- Lessor conveys to the lessee :-

→ the right to use the asset
→ in exchange :- a payment / series of payments.

Leases can be of two types :-

Operating lease	Finance lease
Only right to use is transferred by lessor to lessee.	→ Right to use is transferred & → Substantially all risks & rewards incidental to ownership are transferred.

Indicators of Finance Lease

1) Lessor transfer the ownership to lessee at the end of lease term.
2) Lessor gives the lessee the right to purchase the asset at the end of lease term at a price which is substantially lower than the fair market value, such that at the inception of lease it becomes reasonably certain that the lessee will exercise the option.
3) Lease Term is for the major part of economic life of asset.
4) PV of MLP is approximately equal to fair value at the inception.
5) The asset is of such specialised nature that only the lessee can use it without major modifications being made.
6) If on cancellation of lease, the losses accruing to lessor are borne by lessee.
7) Fluctuations to Residual Value → Gain/Loss → accruing to lessee.
8) Lease rent for secondary term is substantially lower.

Accounting for Finance Lease

Lessee Books

Assets :- Leased Asset + Initial Direct cost
Expense :- Depreciation, Interest (finance ch.)
Liability :- Lease Rental payable

Lessor Books

Asset :- Lease Rent receivable.
Income :- Interest Income
Initial Direct cost will be charged to P&L.

Lessee will record the asset in his books at lower of :-
1) Present Value of MLP
2) Fair Value.

Important Terminologies for practical questions

Minimum Lease Payment

Lessee POV

→ Lease Rentals
→ Guaranteed residual value
: by lessee
: on behalf of lessee

Lessor POV

→ Lease Rentals
→ Guaranteed residual value
: by lessee
: on behalf of lessee
: by independent third party.

* contingent rent is not included in MLP.

+ Unguaranteed Residual Value

= Gross Investment in Lease (MLP + UGRV)

-Interest
Unearned finance Income

= Net Investment in Lease (PV of MLP + PV of UGRV)

Accounting for operating lease

Lessee Books

Asset :- x
Expense :- Lease Rentals + Initial Direct cost
Liability :- Lease Rental pay.

Lessor Books

Asset :- Leased Asset + IDC
Expense :- Depreciation
Income :- Lease Rental

Sale & Leaseback Transactions

Finance Lease

→ Profit/Loss on sale will be deferred and amortised over the lease term.

Operating Lease
↓
THUMB RULE

→ Compare CA with FV.
→ Compare RCA with SP.

Sale & Leaseback : Operating Lease

(imp-points)

1) If CA > FV : recognise loss immediately & bring down CA to FV.
If CA < FV : no treatment required.
We will arrive at RCA.

2) RCA < SP : **Profit**
- SP > FV → Profit will be deferred & amortised over lease term.
- SP = FV → Profit will be recognised immediately.

RCA > SP : **Loss**
- SP < FV
  - Loss is compensated by future lower lease rentals → Defer and amortise over lease term.
  - Loss doesnot have an impact on future lease rentals. → Recognise loss immediately.
- SP = FV → Recognise loss immediately.

Question 5) b) **CASE I :-**

CA = 40L FV = 45 SP = 38

1) Compare CA with FV.

CA : 40L FV = 45L

Loss : 0

RCA = 40L

2) Compare RCA with SP.

RCA = 40L SP = 38L

(FV = 45L)

Loss = 2L

Loss of 2L will be charged to P&L a/c if such loss is not compensated by future lower lease rentals.

However, if such loss is compensated by future lower lease rentals then such loss will be deferred & amortised over the lease term.

CASE II :-

CA : 40L FV : 40L SP = 50L

1) Compare CA with FV.

CA = 40L FV = 40L

No Loss

RCA = 40L

2) Compare RCA with SP.

RCA = 40L SP = 50L (FV = 40L)

Profit = 10L

Since the SP exceeds the FV the profit of ₹ 10 lakhs will be deferred and amortised over the lease term.

CASE III :-

CA = 40L FV = 46L SP = 50L

1) Compare CA with FV.

CA = 40L FV = 46L

Loss = 0

RCA = 40L

2) Compare RCA with SP.

RCA = 40L SP = 50L

(FV = 46L)

P = 10L

P= GL

↓

Credited to P&L.

P= AL

↓

Defer & amortise over lease term.

Question 17:-

CASE I :-

CA = 50L   FV = 60L   SP = 60L

1) Compare Carrying Amt. with fair Value

CA = 50L   FV = 60L

No loss.
RCA : 50L

2) Compare RCA with Selling Price

RCA = 50L   SP = 60L
P = 10L   (FV = 60L)
↓
Credit to P&L

CASE II :-

CA = 50L   FV = 50L   SP = 45L

1) Compare CA = 50L with FV = 50L

CA = 50L   FV = 50L
L = 0
RCA = 50L

2) Compare RCA = 50L with SP = 45L

RCA = 50L   SP = 45L
L = 5L   (FV = 50L)

If such loss is compensated by future lower lease rentals then defer and amortise the loss over the lease term.

If such loss is not compensated by future lower lease rentals then immediately charge it to P&L a/c.

CASE III :-

CA = 50L   FV = 55L   SP = 62L

1) Compare CA with FV.

CA : 50L   FV = 55L

L = 0
RCA = 50L

2) Compare RCA with SP.

RCA = 50L   SP = 62L
P = 12L   (FV = 55L)

P = 5 ↓ Credit to P&L

P = 7 ↓ Defer & amortise over lease term.

CASE IV :- CA = 50L   FV = 45L   SP = 48L

1) Compare CA with FV

CA = 50L   FV = 45L
L = 5L → immediately Dr. to P&L.
RCA = 45L

2) Compare RCA with SP

RCA = 45L   SP = 48L
P = 3L   (FV = 45L)
↓
Defer & amortise over lease term