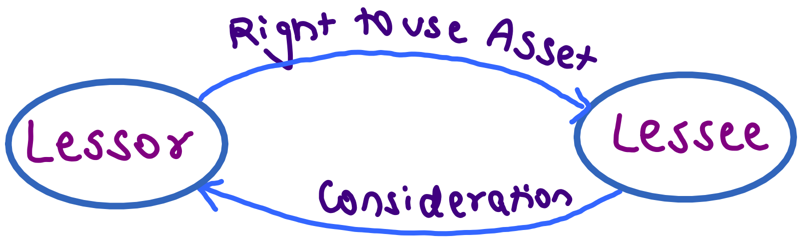
LEASES (AS-19)

Lease means transfer of right to use asset for specified period against consideration / series of consideration.



Lease can be of 2 types:

1) Finance Lease 2) Operating Lease

Conditions of Finance Lease:

a) Transfer of ownership at end of Lease term
b) Lessee has purchase option at reduced rate & lessee is certain to opt.
c) Lease period substantially covers economic life of asset.
d) Present value of Minimum Lease payments substantially covers fair value of asset.
e) Asset is of specialised nature

FINANCE LEASE [Books of Lessee]

Journal Entries:

1) Asset on Lease A/c - Dr
   To Lessor A/c

Amount = Lower of

* Present value of Minimum Lease Payments from Stand point of Lessee (MLP_{Lessee})

$\boxed{OR}$

* Fair Value of Asset

MLP_{Lessee} => Lease Payments / Rentals
+
Guaranteed Residual value by Lessee or on his Behalf

2) Lessor A/c -Dr

Finance charges A/c -Dr

To Bank A/c

3) Depreciation A/c -Dr

To Asset on Lease

Period

1) If Asset will be retained at the end : Useful life

2) If Asset will be returned : useful life or Lease period w.e. is shorter

4) P&L A/c -Dr

To Finance charges A/c

To Depreciation A/c

Note:

* Rate of Interest would be incremental Rate of Return (IRR) (Interest rate Implicit on Lease)
* Whenever IRR is given, follow given IRR
* If Fair value of Asset < Present value of MLP Lessee, IRR would be recomputed
* If Interest rate implicit on Lease cannot be computed, use lessee's incremental borrowing rate of interest.

FINANCE LEASE [Books of Lessor]

Journal Entries:

1) Lease Receivable / Lessee A/c - Dr
To Sale / Asset A/c

Amount = Net Investment

Net Investment = Present value of Gross Investment

$$\text{Gross Investment} = \underbrace{\overbrace{\text{Lease Rentals} + \text{Guaranteed Residual value}_{\text{Lessor}}}^{\text{MLP Lessor}} + \text{Unguaranteed Residual value}}_{}$$

Residual value

GRV_{Lessor} = Higher of

GRV_{Lessee}

or

$GRV_{3rd\ Party}$

2) Bank A/c - Dr

To Lease Receivable / Lessee A/c

To Finance Income A/c

3) Finance Income A/c - Dr

To P&L A/c

$\boxed{\text{Unearned Finance Income} = \text{Gross Investment} - \text{Net Investment}}$

OPERATING LEASE

Lessor

Rental Income

Lessee

Rental Expense

To be recognised in the Statement of P&L in the ratio of benefit derived.

If not available, then SLM is used.

SALE & LEASE BACK

$$\begin{tikzcd} A \arrow[r, bend left, "\text{Sale}"] & B \arrow[l, bend left, "\text{Lease}"] \end{tikzcd}$$

Sale & Finance Lease Back:

Any Profit / loss is to be deferred in the ratio of depreciation over lease period.

Sale & Operating Lease Back:

Step 1: Calculate Impairment Loss : Carrying Amount − Fair value

To be recognised Immediately

Step 2: Calculate Deferred Income : Sale Price − Fair value

To be recognised over Lease period

Step 3: Calculate Difference : +ve or −ve

To be recognised immediately

Exception: If Loss is compensated by future lease payments then it should be amortised over the period.

LEASES (AS-19)

(Transfer of Right to use asset for specified period against consideration)

Normal Lease

Finance Lease

Lessee

Record Asset at

Lower of

P.V. of MLP_{Lessee}

or

Fair value of Asset

MLP_{Lessee} ⇒ Lease Rentals + GRV_{Lessee}

Lessor

Record Sale at

Net Inv. = P.V. of Gross Inv.

Gross Inv. =

MLP_{Lessor} { Lease Rentals + GRV_{Lessor} } + UGRV → R.V.

Operating Lease

Rental Income/Expense in Ratio of Benefit derived.

If not, then SLM

Sale & Lease Back

Sale & Finance Lease Back

Profit/Loss in ratio of dep. over Lease

Sale & Operating Lease Back

- Impairment Loss: Recognised Immediately
- Deferred Income: Over Lease Period
- Difference: Recognised Immediately