HM Treasury

IFRS 16 Leases

Application guidance

January 2023

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19 December 2018	-	Original version published.
27 January 2021	-	Updated version published.
18 Janaury 2023	17.14 and previously 17.15 (now deleted)	Updated version published. The previous version was updated as follows: • Changed the effective date of the PPP accounting guidance from 2022-23 to 2023-24. • Clarified that the requirement relates to PPP liabilities (added the word liabilities to one sentence, removed the word lease from another). • Updated guidance, which previously required remeasurement when cash flows are affected, to instead require an initial remeasurement at 1 April and then a subsequent remeasurement when further changes affect cash flows. This aligns with FRAB's decision in June 2022 (Please refer to FRAB147 (18) and FRAB 148 (01), Item 18). • Removed the paragraph which stated no changes were expected in 2020-21 or 2021-22.

HM Treasury

IFRS 16

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IFRS 16 Leases

IFRS 16 Leases is being applied by HM Treasury in the Government Financial Reporting Manual (FReM) from 1 April 2022 (with limited options for early adoption from 1 April 2019 and 1 April 2021).

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and replaces the previous Standards IAS 17 *Leases* and related IFRIC and SIC Interpretations. The IASB published IFRS 16 because it was aware that the previous lease accounting model was criticised for failing to provide a faithful representation of leasing transactions. In particular, the previous accounting model made a distinction between finance and operating leases, and did not require lessees to recognise assets and liabilities arising from operating leases.

IFRS 16 introduces a single lessee accounting model that results in more faithful representation of a lessee's assets and liabilities and, together with enhanced disclosures, will provide greater transparency of a lessee's financial leverage and capital employed.

IFRS 16 requires a lessee to recognise assets and liabilities for leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. As a consequence, a lessee also recognises depreciation of the right-of-use asset and interest on the lease liability, and classifies cash repayments of the lease liability into a principal portion and an interest portion and presents them in the statement of cash flows applying IAS 7 *Statement of Cash Flows*.

IFRS 16 also contains disclosure requirements for lessees. Lessees will need to apply judgement in deciding upon the information to disclose in order to meet the objective of providing a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of the lessee. Entities are reminded to use the principles of materiality that flow through all accounting standards to ensure they provide relevant and reliable information about leases in the financial statements.

IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. However, there are changes to the classification guidance for subleases, and enhanced disclosure requirements that will improve information disclosed about a lessor's risk exposure, particularly to residual value risk.

FReM interpretations and adaptations

The FReM interprets and adapts IFRS 16 for the public sector context in several ways. IFRS 16, as adapted and interpreted by the FReM, will be effective from 1 April 2022, with two exceptions.

Early adoption from 1 April 2019 is available for entities when the following criteria are met:

- the entity has at least one subsidiary that, under the Companies Act, is required to follow EU-adopted IFRS and the total assets of the subsidiary comprise at least 10% of the total assets at the group level
- the subsidiary (or subsidiaries) described above have operating lease commitments that comprise at least 10% of the operating lease commitments at the group level, and
- approval to early adopt has been received from HM Treasury.

Early adoption from 1 April 2021 is available for entities where approval has been received from the relevant authority.

The FReM interprets IFRS 16 for the public sector in the following ways, as set out in FReM Chapter 8:

- The option to apply the election in IFRS 16(5(a)) has been withdrawn. All entities must apply the recognition and measurement exemption for short-term leases in accordance with IFRS 16 paragraphs (6-8).
- Where entities cannot readily determine the interest rate implicit in the lease, they are instead required to use the HM Treasury discount rate promulgated in PES papers as their incremental borrowing rate. However, if an entity can demonstrate that another discount rate would more accurately represent their incremental borrowing rate (for example, if they undertake external borrowing independently of the Exchequer), they shall use that discount rate as their incremental borrowing rate.
- The subsequent measurement basis for all right-of-use assets shall be consistent with the principles for subsequent measurement of property, plant and equipment set out in the adaptations to IAS 16.
- The option to reassess whether a contract is, or contains, a lease at the date of initial application has been withdrawn. All entities shall use the practical expedient detailed in IFRS 16(C3) (for peppercorn leases, see separate transition adaptations).[1]
- Upon transition, the accounting policy choice to apply IFRS 16 retrospectively to each prior period presented in accordance with IAS 8 has been withdrawn. All entities applying the FReM shall recognise the cumulative effects of initially applying IFRS 16 recognised at the date of

[1] This presumes that entities have been applying the guidance in IAS 17 and IFRIC 4 appropriately in the past. Any known misapplication of the definition of a lease guidance should be corrected as a prior period error in accordance with IAS 8 unless an entity has explicit approval from the relevant authority to do otherwise.

initial application as an adjustment to the opening balances of taxpayers' equity (or other component of equity, as appropriate) per IFRS 16(C5(b)).

- Upon transition, entities shall measure the right-of-use asset under leases previously classified as operating leases per IFRS 16(C8(b(ii))): at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.
- Upon transition, all entities applying the FReM shall apply the following options for leases previously classified as operating leases:
    - no adjustment for leases for which the underlying asset is of low value that will be accounted for applying IFRS 16(6). [IFRS 16(C9(a)]
    - no adjustment for leases for which the lease term ends within 12 months of the date of initial application (with a requirement to include the cost associated with those leases in the short-term lease expense disclosure). [C10(c)]
    - use hindsight in determining the lease term if the contract contains options to extend or terminate the lease. [C10(e)]

The FReM adapts IFRS 16 for the public sector context in the following ways, as set out in FReM Chapter 8:

- The definition of a contract is expanded to include intra-UK government agreements where non-performance may not be enforceable by law.
- Peppercorn leases are defined as leases for which the consideration paid is nil or nominal (that is, significantly below market value). Peppercorn leases are in the scope of IFRS 16 if they meet the definition of a lease in all aspects apart from containing consideration. All lessees shall account for peppercorn leases as follows:
    - recognise a right-of-use asset and initially measure it at current value in existing use or fair value, as set out in paragraphs 10.1.4-10.1.6 of the FReM. However, if the right-of-use asset meets the definition of a heritage asset, it should be initially measured in accordance with paragraphs 10.1.34-10.1.39.
    - recognise a lease liability measured in accordance with IFRS 16.
    - recognise the difference between the carrying amount of the right-of-use asset and the lease liability as income, as required by IAS 20 as interpreted in the FReM.
    - subsequently measure the right-of-use asset following the principles of IFRS 16 as adapted and interpreted in the FReM.

- upon transition, any peppercorn leases that were not previously classified as finance leases under IAS 17 shall be recognised as follows[2]:
    - the right-of-use asset shall be measured at current value in existing use or fair value, as set out in paragraphs 10.1.4-10.1.6 of the FReM, as at the date of initial application. However, if the right-of-use asset meets the definition of a heritage asset, it should be initially measured in accordance with paragraphs 10.1.34-10.1.39 of the FReM.
    - the lease liability shall be measured at the present value of lease payments, discounted using the lessee's incremental borrowing rate (as promulgated in PES papers) at the date of initial application.
    - the difference between the carrying amount of the right-of-use asset and lease liability shall be included as part of the adjustment to the opening balances of taxpayers' equity (or other component of equity, as appropriate) per IFRS 16 (C5(b)).

Note on this application guidance

This guidance focusses on the public sector application of IFRS 16, and not the application of the Standard itself, and sets out the basis for the public sector adaptations and interpretations. It does not seek to duplicate the extensive guidance and illustrative examples already included in IFRS 16, nor take away the judgements each entity will be required to make when applying IFRS 16.

[2] This includes any peppercorn leases that were previously classified as operating leases under IAS 17, or were argued to be outside the scope of IAS 17 because they did not include a payment, or series of payments.

Chapter 1
Recognition exemptions

1.1 IFRS 16 provides two optional recognition and measurement exemptions:

- for short-term leases
- for leases for which the underlying asset is of low value.

Short-term leases

1.2 Short-term leases are defined in IFRS 16 as having a lease term of 12 months or less, after the assessment of any options. Any lease with a purchase option cannot qualify as a short-term lease. The recognition and measurement exemption for short-term leases in IFRS 16 is made by class of underlying asset.

1.3 Examples of short-term leases currently within central government include some property leases, software licences, specialised equipment and hire cars. These leases generally meet a short-term need, where longer leases or purchasing the asset would not constitute value for money.

1.4 The determination of the lease term (discussed in paragraphs 18-21 and B34-B41 of IFRS 16) is essential in assessing whether a lease qualifies for the short-term exemption. It is critical for a lessee to consider the substance of an arrangement to determine the lease term and, therefore, whether the recognition exemption is applicable. When assessing leases with an initial non-cancellable term of less than 12 months, paragraph B39 of IFRS 16 may be relevant, which notes that the shorter the non-cancellable period of a lease, the more likely it is that the lessee will exercise an option to extend.

1.5 To reduce the costs of applying IFRS 16 and ease the burden on preparers, FReM mandates the recognition and measurement exemption for short-term leases. Disclosures are still required for short-term leases, if material.

1.6 Public sector interpretation: The option to apply the election in IFRS 16 (5(a)) has been withdrawn. All entities must apply the recognition and measurement exemption for short-term leases in accordance with IFRS 16 paragraphs 6-8.

Leases of low-value assets

1.7 In addition to the recognition and measurement exemption for short-term leases, IFRS 16 also provides a recognition exemption for leases of low-value *underlying assets.* IFRS 16 provides some guidance as to how to assess whether an underlying asset is of low value. The low value assessment is performed on the underlying asset, not the right-of-use asset. It is based on the value of that underlying asset when new, regardless of the age of the asset being leased.

1.8 Importantly, this assessment should be performed on an absolute basis and is separate from materiality. This means different public sector entities, regardless of size, should reach similar conclusions about whether different underlying assets qualify as low value. For example, a large ministerial department and a small arms-length body should come to the same conclusions regarding which assets qualify as low-value assets, because the size of the entity is irrelevant in this consideration.

1.9 Whilst IFRS 16 does *not* provide a numerical threshold as to what constitutes a low value, it does provide some examples of low-value underlying assets. The examples provided in IFRS 16 are:

- tablet and personal computers
- small items of office furniture
- telephones.

Leases of these types of assets will likely be prevalent in some areas of the public sector, including leases of water coolers, franking machines and photocopiers. IFRS 16 also explicitly states that a car would not qualify as a lease of a low-value asset.

1.10 Again, the low-value underlying asset recognition exemption is separate from the materiality considerations that apply to every standard. For example, a public sector entity might have a large volume of low-value asset leases that are material in the aggregate. These leases would still qualify for the recognition and measurement exemption, regardless of their materiality.

1.11 However, it is likely that for at least some public sector entities, leases of low-value underlying assets will be immaterial, even in the aggregate. In this case, the general principles of materiality should apply, and an entity should not make the disclosures regarding leases of low-value underlying assets that are required in IFRS 16.

1.12 Moreover, a public sector entity will likely have leases of underlying assets which do not qualify as low value, but are immaterial to that entity. Following the requirements of IAS 1 *Presentation of Financial Statements*, the entity is not required to apply IFRS 16 to those immaterial leases (regardless of those leases failing to qualify as leases of low-value underlying assets).

1.13 It is important to note that there are no public sector adaptations made for the low-value asset lease exemption; therefore, this exemption is optional and undertaken on a lease-by-lease basis (unlike the short-term lease exemption, as adapted by the FReM). The only exception to this is on transition; the FReM mandates that there should be no adjustments made for leases of low-value asset leases on transition to IFRS 16. This discrepancy (mandating treatment on transition, as compared to leaving optional treatment after transition) is to allow for consistency on transition and ease of application.

Chapter 2

Definition of a lease

2.1 IFRS 16 defines a lease as a contract that 'conveys the right to control the use of an identified asset for a period of time in exchange for consideration.' This definition applies both to lessees and lessors.

2.2 IFRS 16 retains the definition of a lease that was previously in IAS 17 but changes the application guidance around how to apply that definition. The most substantive change in the application guidance is around the concept of *control* used within the definition of a lease.

2.3 IFRS 16 requires entities to use the definition of a lease guidance in IFRS 16 to assess all contracts entered into after the date of initial application. However, on transition, the FReM requires entities to carry forward the assessments that were made in accordance with the requirements in IAS 17 and IFRIC 4 regarding whether contracts are, or contain, leases (see Chapter 7)[1]. Therefore, the guidance in IFRS 16 on the definition of a lease is only relevant for contracts that are entered into, or amended, after the date of initial application.

2.4 There are two aspects of the definition of a lease for which IFRS 16 provides guidance:

- whether a contract depends on the use of an *identified asset*
- whether a customer has the right to *control the use* of that identified asset.

Identified asset

2.5 In order to contain a lease, a contract must involve the use of an identified asset. Typically, an asset in a lease is identified by being explicitly specified (e.g. being named in a contract). However, an asset can also be identified by being implicitly specified.

2.6 Even if an asset is specified, a customer would not have the right to use an identified asset if the supplier has a substantive right to substitute the asset throughout the period of use. A supplier's right to substitute the asset is substantive if the supplier has the practical ability to substitute alternative assets throughout the period of use, and the supplier would benefit economically from exercise of its substitution right. IFRS 16 provides more detailed guidance about the assessment of whether a contract depends on the use of an identified asset.

[1] This presumes that entities have been applying the guidance in IAS 17 and IFRIC 4 appropriately in the past. Any known misapplication of the definition of a lease guidance should be corrected as a prior period error in accordance with IAS 8 unless an entity has explicit approval from the relevant authority to do otherwise.

Controlling the use of an identified asset

2.7 In order to contain a lease, a contract must also provide the customer with the right to control the use of an identified asset. A customer controls the use of an identified asset if they have the right to obtain substantially all of the economic benefits from use of the asset, and the right to direct the use of that asset.

2.8 IFRS 16 provides extensive guidance regarding the determination of whether the customer has the right to direct the use of an asset. At a high level, a customer has the right to direct the use if it:

- has the right to direct how and for what purpose the asset is used, or
- the relevant decisions about how and for what purpose the asset is used are predetermined, and the customer has the right to operate the asset, or designed the asset in a way that determines how and for what purpose the asset will be used.

Intra-UK government agreements

2.9 The FReM makes two adaptations to the definition of a lease in IFRS 16 for the public sector. The first concerns intra-UK government agreements, and the second concerns nil-consideration agreements.

2.10 **Public sector adaptation: The definition of a contract (and therefore, of a lease) is expanded to include intra-UK government agreements that are not legally enforceable.**

2.11 This adaptation is intended to capture lease-like arrangements between Crown bodies, or other governmental bodies, that are not legally enforceable but are in substance akin to an enforceable contract. Although this adaptation broadens the definition of a lease, it does not mean that all lease-like intra-UK governmental agreements will meet this definition. Any such agreements made after the date of implementation should be carefully analysed to determine whether they meet the definition of a lease (apart from the public sector adaptation). Additionally, when applying paragraph B34 of IFRS 16 to lease-like arrangements between Crown Bodies, an entity should consider whether the lessee and lessor each has the right to terminate the lease without permission from the other party with no more than an insignificant penalty, notwithstanding the fact that the agreement is not legally enforceable.

2.12 Box 2.A below provides an illustrative example of how the IFRS 16 guidance on the definition of a lease applies to intra-UK government agreements. There are multiple illustrative examples on the definition of a lease included in IFRS 16.

Box 2.A: Illustrative Examples – Definition of a Lease

<u>Example 1A:</u> Government Department A enters into an agreement with Government Department B. The agreement allows Government Department B to use office space in a building owned by Government Department A for two years.

The agreement gives Government Department B the right to use space equivalent to 1,000 square metres—Government Department B will use this space as office space for civil servants in the region. The entire building comprises 30,000 square metres of space, of which 60% is currently occupied.

Whilst the agreement guarantees Government Department B 1,000 square metres of space, it does not specify where in the building that space will be. Government Department A has the right, following a one-week notice period, to change the space that Government Department B is using within the building.

Government Department A would benefit economically from switching the space set aside for Government B to use. The flexibility could benefit Government Department A as it completes an expected restructuring, or allow it to offer different configurations of office space to other government departments, or private customers, over time.

Example 1A analysis: The contract does not contain a lease. Government Department A has the substantive right to substitute the 1,000 square feet of office space offered to Government Department B. Government Department A has the practical ability to substitute the space that Government Department B is using, and it would benefit economically from exercise of that right.

Since Government Department A has a substantive right to substitute the asset, Government Department B does not have the right to use an identified asset.

Example 1B: Government Department A enters into an agreement with Government Department B. The agreement allows Government Department B to exclusively use two specified floors (the second and third floors) in a building owned by Government Department A for five years.

Government Department B has the right to use the specified floors throughout the period covered by the agreement, and Government Department A cannot evict or otherwise move Government Department B from those floors except in exceptional circumstances.

Government Department A provides cleaning and security services as part of the contract.

Example 1B analysis: The agreement contains a lease. Government Department B has the right to use two floors of a building for five years.

The two floors of a building are an identified asset. They are explicitly specified in the agreement, and Government Department A does not have the right to substitute the asset.

Although the two floors represent only a portion of the entire building, they are physically distinct and so can be identified.

Government Department B has the right to control the use of the two floors of the building because it has the right to obtain substantially all of the economic benefit from use of the floors (it has exclusive use), and it has the right to direct the use of those floors (it can make decisions about how and for what purpose the floors are used).

Lease-like agreements with nil consideration

2.13 The definition of a lease in IFRS 16 contains a requirement that the right to use an asset be conveyed in exchange for consideration. However, in the public sector there are arrangements in which the right to use an asset is conveyed freely (that is, there is no consideration given).

2.14 The adaptations around peppercorn leases mean that arrangements with nil consideration can qualify as leases if they meet the definition of a lease in every other aspect. These types of arrangements exist in the public sector and are very similar to donated assets, or other types of peppercorn leases. Again, these arrangements would only be included in the scope of IFRS 16 if they meet the definition of a lease in every other respect. See Chapter 4 for more details of the peppercorn lease adaptations.

Separating lease and service components

2.15 It is common in the public sector for contracts to contain both the right to use an asset or assets (lease components) and services (service components).

2.16 If a contract contains both lease and service components, IFRS 16 provides guidance on how to separate those components. If a lessee separates lease and service components, it should only capitalise amounts related to the lease components.

2.17 However, IFRS 16 also provides an option for lessees to combine lease and service components and account for them as a single lease. This should provide relief for cases in which it is costly to separate lease and service components.

Chapter 3

Lessee accounting

3.1 IFRS 16 introduces a single lessee accounting model that requires a lessee to recognise assets and liabilities for all leases (apart from the exemptions discussed in Chapter 1 above). This replaces the dual lessee accounting model in IAS 17.

3.2 At a high level, the IFRS 16 lessee accounting model treats leases in a similar way to finance leases under IAS 17. For any lease not captured by the exemptions discussed in Chapter 1, a lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments.

Initial measurement

Lease term

3.3 When initially measuring right-of-use assets and lease liabilities, an entity will need to determine the lease term. IFRS 16 defines the lease term as the non-cancellable period for which a lessee has the right to use an underlying asset, together with both i) periods covered by an option to extend the lease if the lessee is reasonably certain to exercise that option; and ii) periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option.

3.4 Whilst these requirements are very similar to IAS 17, IFRS 16 provides significantly more guidance on how to make these assessments (refer to paragraphs B34-B41).

Lease payments

3.5 IFRS 16 requires the right-of-use asset, and the lease liability, to be initially measured at the present value of unavoidable future lease payments. The following payments are included in the initial measurement of the right-of-use asset and lease liability:

- fixed payments (including in-substance fixed payments)
- variable lease payments that depend on an index or a rate (for example, payments linked to a consumer price index or market rental rates)
- amounts expected to be payable by the lessee under residual value guarantees
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option
- payments of penalties for terminating the lease, if the lease term reflects the lessee exercising a termination option.

The right-of-use asset may require further adjustment for initial direct costs, prepayments or incentives, and costs related to restoration at the end of a lease (refer to IFRS 16 paragraph 24).

Irrecoverable VAT payable on lease payments should not be included in the initial measurement of the right-of-use asset and lease liability; rather, it should be treated as an expense at the tax point in accordance with IFRIC 21 *Levies*.

Discount rate

3.6 IFRS 16 requires the lease liability to be discounted using the rate implicit in the lease, or where this is not readily determined, the lessee's incremental rate of borrowing. The incremental rate of borrowing is defined as the rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.

3.7 Within central government, entities are funded by Supply from the Exchequer (either directly (departments) or via grant in aid (agencies and ALBs) from their parent department). Whilst the Exchequer borrows externally as necessary to meet public sector finance requirements, there are only a very limited number of circumstances where central government entities would borrow externally themselves.

3.8 To address this issue, the FReM interprets IFRS 16 to introduce a presumption that, when entities cannot readily determine the rate implicit in the lease, they instead use an HM Treasury discount rate promulgated in PES papers as their incremental borrowing rate. The rate issued will be a single discount rate, independent of the type of underlying asset, to reflect the nature of the borrowing by the Exchequer. To reflect the fact that there are circumstances where a central government entity can borrow externally, if an entity can demonstrate that another discount rate would more accurately represent their incremental borrowing rate, they shall use that rate as their incremental borrowing rate.

3.9 Refer to appendix 1 in this guidance for further detail on how to discount lease liabilities, using HM Treasury rates.

3.10 **Public sector interpretation: Where entities cannot readily determine the interest rate implicit in the lease, they are instead required to use the HM Treasury discount rate promulgated in PES papers as their incremental borrowing rate. However, if an entity can demonstrate that another discount rate would more accurately represent their incremental borrowing rate (for example, if they undertake external borrowing independently of the Exchequer), they shall use that discount rate as their incremental borrowing rate.**

Subsequent measurement

Lease liability

3.11 After the commencement date (the date that the lessor makes the underlying asset available for use by the lessee), a lessee shall measure the liability by:

- increasing the carrying amount to reflect interest

- reducing the carrying amount to reflect lease payments made
- remeasuring the carrying amount to reflect any reassessment or lease modifications, or to reflect revised in substance fixed lease payments.

3.12 IFRS 16 contains detailed guidance around reassessment of the lease liability, and the treatment of lease modifications. At a high level, the lease liability shall be remeasured if there is a change in the lease term; assessment of purchase option; amounts expected to be payable under a residual value guarantee; or change in future payments resulting from changes in an index or rate. The treatment of lease modifications depends on whether a modification increases the scope of the lease and the consideration for the lease increases commensurately. Paragraphs 39-46 of IFRS 16 contain more guidance on reassessment and lease modifications.

Right-of-use asset

3.13 A public-sector interpretation has been introduced for the subsequent measurement of right-of-use assets.

3.14 **Public sector interpretation: The subsequent measurement basis of all right-of-use assets shall be consistent with the principles for subsequent measurement of owned property, plant and equipment set out in the adaptations to IAS 16.**

3.15 Accordingly, right-of-use assets should be measured at either fair value or current value in existing use (i.e. the revaluation model should be used, rather than the cost model).

3.16 This will ensure that the measurement of right-of-use assets will be consistent with the measurement of owned assets in the public sector, and that the benefits of using a current value measurement be maintained for right-of-use assets.

3.17 However, in practice, in most cases, the cost measurement model in IFRS 16 will be an appropriate proxy for current value in existing use or fair value. This is because leases will often have terms that require lease payments to be updated for market conditions, which will be captured in the IFRS 16 cost measurement provisions. Moreover, right-of-use assets generally have shorter useful lives and values than their respective underlying assets, and the FReM sets out, in the guidance on IAS 16, that cost can be used as a proxy for assets with shorter economic lives or lower values.

3.18 However, for some right-of-use assets, the cost model in IFRS 16 will not be an appropriate proxy for current value in existing use or fair value. This is likely to be the case when both of the following conditions are met:

- A longer-term lease has no terms that require lease payments to be updated for market conditions (such as rent reviews), or if there is a significant period of time between those updates; and
- The fair value or current value in existing use of the underlying asset is likely to fluctuate significantly due to changes in market prices. This is more likely to be the case with property assets.

An example of the case described above would be a 30-year lease of property with one rent review at the end of year 15, where the market for the property was active and volatile.

3.19 The assessment of whether cost is an appropriate proxy for current value in existing use or fair value should be performed on an asset-by-asset basis.

3.20 To measure the current value in existing use of a right-of-use asset, a valuer should calculate the full replacement cost of the right-of-use asset. This should be done by identifying the current market rental value that could be achieved for existing use of the right-of-use asset and capitalising it for the full remaining lease term from the valuation date. This valuation should reflect the terms and conditions of the lease giving rise to the right-of-use asset, and should reflect an assumption that the entity requires the use the entire right-of-use asset. The Royal Institution of Chartered Surveyors (RICS) has published guidance for valuers consistent with the above here.

3.21 If the cost model in IFRS 16 is used as a proxy for current value in existing use or fair value then this fact should be disclosed, including the classes of right-of-use assets within which it has been used (where appropriate) and the reasons why.

3.22 Finally, entities should bear materiality in mind when applying this guidance, just as in other areas of financial reporting. Part of the reason that, in most cases, the cost model in IFRS 16 is an appropriate proxy for current value is that there is not a material difference between the valuation produced by the cost model or the valuation produced by the revaluation model.

Chapter 4

Peppercorn leases

4.1 Within the public sector, there are a number of leases which are provided on a peppercorn basis. That is, leases are provided to public sector lessees for nil[1] or nominal consideration in return. At present, such leases are generally treated as finance leases in IAS 17 by both the lessee and the lessor. This results in the lessor de-recognising the asset and the lessee treating the asset as if it were owner occupied.

4.2 The application of the IFRS 16 cost model for initial measurement of these leases would not result in an appropriate valuation for the right-of-use asset, as the lease liability would be substantially low or nil value for peppercorn leases.

4.3 To address this issue, the FReM makes a number of adaptations for peppercorn leases for the public sector:

4.4 Public sector adaptation: Peppercorn leases are defined in the FReM as leases for which the consideration paid is nominal (that is, significantly below market value). Peppercorn leases are in the scope of IFRS 16 if they meet the definition of a lease in all aspects apart from containing consideration. All lessees shall account for peppercorn leases as follows:

- recognise a right-of-use asset and initially measure it at current value in existing use or fair value, depending on whether the right-of-use asset will be held for its service potential. However, if the right-of-use asset meets the definition of a heritage asset, it should be initially measured in accordance with the FReM guidance on heritage assets.
- recognise a lease liability measured in accordance with IFRS 16.
- recognise any difference between the carrying amount of the right-of-use asset and the lease liability as income as required by IAS 20 as interpreted in the FReM.
- subsequently measure the right-of-use asset following the principles of IFRS 16 as adapted and interpreted in the FReM.
- upon transition, any peppercorn leases that were not previously classified as finance leases under IAS 17 shall be recognised as follows[2]:
    - the right-of-use asset shall be measured at current value in existing use or fair value, as set out in paragraphs 10.1.4-10.1.6 of the FReM, as at

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[1] See discussion of adaptation for nil-consideration arrangements in Chapter 2.

[2] This includes any peppercorn leases that were previously classified as operating leases under IAS 17, or were argued to be outside of the scope of IAS 17 because they did not include a payment, or a series of payments.

the date of initial application. However, if the right-of-use asset meets the definition of a heritage asset, it should be initially measured in accordance with paragraphs 10.1.34-10.1.29 of the FReM.

- the lease liability shall be measured at the present value of lease payments, discounted using the lessee's incremental borrowing rate (as promulgated in PES papers) at the date of initial application.
- the difference between the carrying amount of the right-of-use asset and lease liability shall be included as part of the adjustment to the opening balances of taxpayers' equity (or other component of equity, as appropriate) per IFRS 16 (C5(b)).

4.5 These adaptations should ensure that the right-of-use asset in a peppercorn lease is measured at an amount that reflects its value, while at the same time avoiding the costs associated with revaluation (similar to right-of-use assets under other leases).

4.6 These adaptations should also ensure that the right-of-use asset in a peppercorn lease is accounted for similarly to a donated owned asset, particularly the difference between the right-of-use asset (initially measured at fair value), and the lease liability (initially measured at cost, so an amount close to nil value). This difference will be recognised in accordance with IAS 20, just as it would for donated assets. This is appropriate, as a peppercorn lease is similar in substance to a donated right-of-use asset. Moreover, right-of-use assets in a peppercorn lease will also be subsequently measured similarly to owned assets. Cost will not be an appropriate proxy for current value in existing use or fair value for peppercorn leases, and so the revaluation model should be applied.

4.7 Similarly, the FReM has been amended to clarify that right-of-use assets can meet the definition of a heritage asset.

4.8 These adaptations should be broadly consistent with the treatment of peppercorn leases under IAS 17. Peppercorn leases were generally treated as finance leases by the lessee, so the lessee treated the asset as if it were owner-occupied. HM Treasury expects any entities not currently accounting for their peppercorn leases as finance leases to consider whether a prior period error exists and an adjustment needs to be made.

4.9 Finally, these adaptations will not mean that every contract involving the use of an asset where there is nil or nominal consideration will be in the scope of IFRS 16. These arrangements should only be accounted for as leases under IFRS 16 where they meet the definition of a lease in IFRS 16 in every respect apart from containing consideration.

Chapter 5

Lessee disclosures

5.1 IFRS 16 includes an overarching disclosure objective for lessees that requires lessees to disclose information that, together with the amounts in the financial statements, enables a user to understand the effect that leases have on the financial position, financial performance and cash flows of the lessee.

5.2 IAS 17 did not specify a disclosure objective, but instead provided a list of required qualitative and quantitative disclosures. While there are still some required quantitative disclosures, entities will need to use judgement in determining how to meet the disclosure objective, rather than approaching disclosures as simply meeting a checklist of requirements.

5.3 Specific disclosures are not required under IFRS if the information resulting from that disclosure is not material. As with all disclosures, care should be taken to not reduce the understandability of the financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures and functions. The materiality concept should be applied on a disclosure-by-disclosure basis.

5.4 IFRS 16 requires that lessee disclosures should be made in a single note or separate section in its financial statements. However, it also states that an entity need not duplicate information that is already presented elsewhere in the financial statements (provided that there is a cross-reference in the leases note or section). Similarly, under the Simplifying and Streamlining project, information does not need to be duplicated across the three sections of the annual report and accounts. For example, if sufficient information is provided for leases in the financial statements, these need not be duplicated in the accountability report. Appropriate cross-referencing should be included to ensure that the financial statements and notes are understandable.

5.5 The following paragraphs summarise the specific disclosure guidance and requirements in IFRS 16 and contain some illustrative examples about how the disclosure requirements could be fulfilled. The summaries are not exhaustive, and the illustrations are not templates; entities are reminded to review the disclosure requirements in the context of their own activities and financial statements.

Changes in accounting policies (IAS 8)

5.6 As part of the adoption of IFRS 16, entities will need to reassess their leases accounting policy disclosures. Entities are also reminded that in the year of initial application of IFRS 16, the disclosure requirements of IAS 8 (28) come into force which require entities to disclose details about changes in accounting policies. These disclosures might include details about elections or practical expedients in IFRS 16 employed and an overview of the new lessee accounting model. However, due to the transition approach adopted for IFRS 16, the requirements of IAS 8 (28(f)) are not required as they are substituted by the additional disclosures on transition (see paragraph 7.12).

Quantitative disclosures related to the right-of-use asset

5.7 IFRS 16 requires the following quantitative disclosures regarding the right-of-use asset:

- additions to right-of-use assets
- the carrying amount of right-of-use assets at the end of the reporting period by class of underlying assets.

5.8 Additionally, IFRS 16 requires right-of-use assets to be presented separately from other assets in the statement of financial position, or disclosed in the notes to the statement of financial position with a statement of which line item includes right-of-use assets.

Box 5.A: Illustration: Right-of-use asset disclosure

	Property	Equipment	Vehicles	Total
Balance at 1 April	X	X	X	X
Depreciation expense	(X)	(X)	(X)	(X)
Balance at 31 March	X	X	X	X

Additions to right-of-use assets during 20XX totalled X.

Quantitative disclosures related to the lease liability

5.9 IFRS 16 requires an entity to disclose a maturity analysis of lease liabilities applying paragraphs 39 and B11 of IFRS 7. This requires an entity to use judgement in determining which time bands should be disclosed in order to provide the most useful information to users of the financial statements. An entity should consider the specific features of its lease portfolio, especially typical lease terms, when making this judgement, along with its existing IFRS 7 disclosures. Entities will also be subject to WGA requirements for this disclosure but will retain the ability to use judgement when determining time bands for their own accounts.

Quantitative disclosures related to elements recognised in the SoCNE

5.10 IFRS 16 also requires the following quantitative disclosures for those elements not captured in the measurement of the right-of-use asset or lease liability, but instead recognised in the Statement of Comprehensive Net Expenditure:

- depreciation charge for right-of-use assets by class of underlying asset
- interest expense on lease liabilities
- the expense related to short-term leases (excluding leases with a lease term of one month or less)
- the amount of lease commitments for short-term leases, if the portfolio of short-term leases an entity is committed to at the end of the reporting period is dissimilar to the portfolio of leases for which the short-term lease expense disclosure described above is made
- the expense related to leases of low-value assets for which the recognition and measurement exemption is applied (excluding short-term leases of low-value assets)
- the expense related to variable lease payments not included in the measurement of lease liabilities
- income from subleasing right-of-use assets
- gains or losses arising from sale and leaseback transactions.

5.11 Entities are reminded that, just as in all disclosure requirements, these items should only be disclosed if material.

Quantitative disclosures related to cash

5.12 IFRS 16 also requires the total cash outflow for leases to be disclosed.

Additional information to meet the disclosure objective: qualitative and quantitative disclosures

5.13 In addition to the quantitative disclosure requirements described above, IFRS 16 discusses the need for additional information to be disclosed to meet the disclosure objective. Entities will need to use judgement to determine what, if any, additional information is required to meet the disclosure objective, and it is likely that the additional information provided will differ between entities.

5.14 IFRS 16 provides examples of additional information that could be provided to satisfy the disclosure objective:

- the nature of the lessee's leasing activities
- information about significant extension or termination options, variable lease payments, residual value guarantees, or leases committed to but not yet commenced that will help users assess future cash outflows to which the lessee is exposed that are not reflected in the lease liability
- restrictions or covenants imposed by leases

- sale and leaseback transactions.

Box 5.A: Examples of additional information

The following provides examples of additional information that may be needed to meet the disclosure objective in the public-sector context:

- the nature of leasing activities, including the reasons for entering into leases, the flexibility provided by leases, restrictions imposed by leases or deviations from normal public-sector leasing practices.
- information relating to extension or termination options, including the reasons for using those options, the prevalence of those options, and the magnitude of optional lease payments to lease payments included in the measurement of the lease liability.
- information relating to peppercorn leases, including the reasons for entering into peppercorn leases, the prevalence of those leases, the underlying assets in those leases, and a comparison of peppercorn leases to non-peppercorn leases.
- provision of the above, or other additional information about leases disaggregated by class of underlying asset, or by operating segment categories.

Chapter 6

Lessor accounting: subleases

6.1 IFRS 16 leaves the lessor accounting requirements largely unchanged from IAS 17; lessors will continue to classify leases as either operating or finance leases and account for them accordingly. However, IFRS 16 makes some changes to lessor accounting: it expands the lessor disclosure requirements; changes sale and leaseback requirements; and changes the guidance on subleases.

6.2 The change regarding subleases may be most relevant for the public-sector context. Whilst many public sector entities do not frequently act as a lessor, they are most likely to act as a lessor by subleasing a leased asset (often within the public sector).

6.3 Therefore, it is critical the entities are aware of the change in accounting for subleases introduced by IFRS 16. This change regards the classification of a sublease as either a finance or an operating lease. Previously under IAS 17, a sublease was classified as either a finance or operating lease with reference to the risks and rewards incidental to ownership of the underlying asset in the head lease.

6.4 Entities will now classify subleases under IFRS 16 as follows:

- If the head lease is a short-term lease, the sublease is classified as an operating lease.
- Otherwise, the sublease is classified with reference to the right-of-use asset arising from the head lease, rather than with reference to the underlying asset.

6.5 The impact of this change is that there may be more finance subleases under IFRS 16 as compared to IAS 17, as it is more likely that a sublease would transfer substantially all of the risks and rewards incidental to ownership of the right-of-use asset in a head lease, as compared to the underlying asset. However, the Basis for Conclusions to IFRS 16 notes that this change is appropriate, as it reflects real economic differences. For example, if a sublease is for all of the remaining term of the head lease, the intermediate lessor has in effect transferred its right-of-use asset to another party and finance lease accounting is appropriate.

Chapter 7

Transition arrangements

7.1 There are several considerations to evaluate as part of the transition from IAS 17 (and its related interpretations) to IFRS 16. These include the transition arrangements around retrospective application (and the associated reliefs) and disclosure considerations.

7.2 The date of initial application is the date when an entity first applies the transition requirements of IFRS 16 and must be the beginning of a reporting period after the Standard is issued. For the public sector this will usually be 1 April 2022, unless the entity is early adopting at 1 April 2019 or 1 April 2021, as described in the executive summary. Entities must have made certain key assessments by this date including:

- identifying and locating all lease contracts[1], along with implementing a process for entering those leases into their accounting system
- determining methodologies for separating lease and service components, if necessary
- determining how to communicate and educate all relevant stakeholders as to the impact of IFRS 16, including commercial, legal and finance teams
- considering which disclosure requirements are material, and where the necessary information is held to provide sufficient disclosures to meet the disclosure requirements.

7.3 Many of the judgements and much of the information required by IFRS 16, including the determination of whether a contract contains a lease and the determination of the lease term, have already been required by IAS 17. Entities are not expected to duplicate or recreate these judgements, assuming that they have been performed appropriately under IAS 17.

Definition of a lease

7.4 As a practical expedient, IFRS 16 does not require an entity to reassess whether a contract is, or contains, a lease at the date of initial application. Instead, the entity is permitted:

- to apply the Standard to contracts that were previously identified as leases applying IAS 17 and IFRIC 4

[1] Entities will not need to re-examine previous judgements made about whether contracts are leases or services; refer to paragraph 7.3.

- not to apply the Standard to contracts that were not previously identified as containing a lease applying IAS 17 and IFRIC 4.

7.5 To improve consistency across the public sector and to ease implementation for entities, the Standard has been interpreted to mandate this practical expedient.

7.6 Public sector interpretation: Upon transition, the option to reassess whether a contract is, or contains, a lease at the date of initial application has been withdrawn. All entities should use the practical expedient detailed in IFRS 16 (C3) (for peppercorn leases, see separate transition adaptations).[2]

Lessee transition approach

7.7 IFRS 16 allows two approaches for transition:

- retrospective application with full restatement in accordance with IAS 8 (subject to practical expedients) or
- retrospective application with the cumulative effect recognised as an adjustment to opening balances.

7.8 To improve consistency across the public sector and consolidation of entities within the Whole of Government Accounts (WGA), and to ease implementation for entities, the Standard has been interpreted to mandate the second transition approach, and also mandate certain transitional reliefs available.

7.9 Public sector interpretation: Upon transition, the accounting policy choice to apply IFRS 16 retrospectively to each prior period presented in accordance with IAS 8 has been withdrawn.

All entities applying the FReM shall recognise the cumulative effect of initially applying the Standard at the date of initial application as an adjustment to the opening balance of taxpayers' equity (or other component of equity, as appropriate) per IFRS 16 (C5(b)).

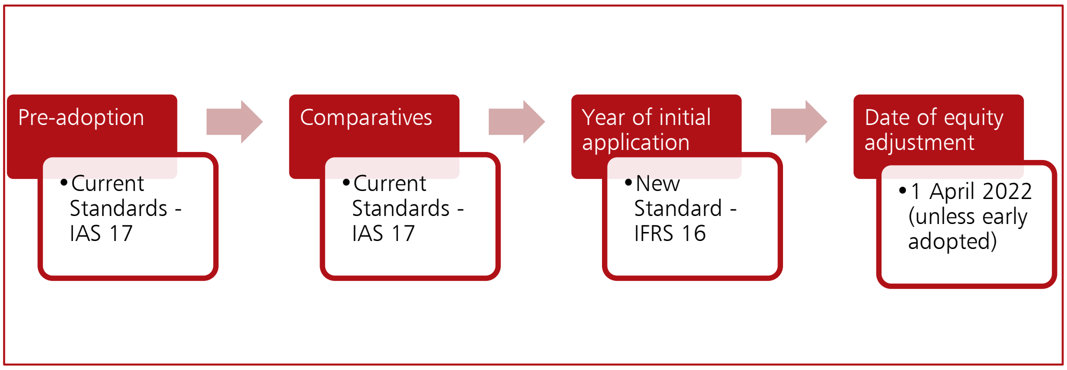
In using this transition approach, all entities applying the FReM shall apply the following options for leases previously classified as operating leases:

- Measure the right-of-use asset at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application. No adjustments for leases for which the underlying asset is of low value that will be accounted for applying IFRS 16 (6). (IFRS 16 C9 (a)).
- No adjustments for leases for which the lease term ends within 12 months of the date of initial application (with a requirement to include the cost associated with these leases in the short-term lease expense disclosure) (C10 (c)).
- Use hindsight in determining the lease term if the contract contains options to extend or terminate the lease (C10 (e)).

2 This presumes that entities have been applying the guidance in IAS 17 and IFRIC 4 appropriately in the past. Any known misapplication of the definition of a lease guidance should be corrected as a prior period error in accordance with IAS 8 unless an entity has explicit approval from the relevant authority to do otherwise.

7.10 The following diagram provides a summary of the impact of this transition approach on the financial statements:

Box 7.A: Impact of transition approach on the financial statements



Lessee optional practical expedients

7.11 Although the FReM interprets IFRS 16 to mandate some practical expedients for transition, there are other practical expedients that are optional. These practical expedients include expedients like the option to rely on its assessment of whether leases are onerous applying IAS 37 rather than applying IAS 36 at the date of initial application. Refer to paragraph C10 of IFRS 16 for a full list of practical expedients.

Lessee disclosures on transition

7.12 The transition approach adopted does require additional disclosures to enable users to understand the effects of implementing IFRS 16. In accordance with IFRS 16 Appendix C, entities will need to disclose:

- the weighted average lessee's incremental borrowing rate applied to lease liabilities recognised at the date of initial application
- an explanation of any differences between operating commitments disclosed applying IAS 17, discounted using the incremental borrowing rate described above, and lease liabilities recognised at the date of initial application
- the use of any optional practical expedients in paragraph C10.

Public-private partnerships (PPPs)

7.13 The FReM provides guidance regarding public-private partnerships (PPPs), which utilises the principles of IFRIC 12 from the grantor's perspective. PPPs that previously met the definition of a lease and were directly accounted for under IAS 17 should be accounted for under IFRS 16 and are subject to the transition provisions above.

7.14 PPP accounting guidance will be updated in the 2023-24 FReM. The area of the guidance which will change relates to PPP liabilities containing future payments linked to a price index. Entities who follow the FReM will be required to remeasure the liability at 1 April 2023 for indexation changes which have taken effect in the cash flows until that date, and thereafter when a change in indices causes a change in future lease payments and that change has taken effect in the cash flow. Previous accounting for index linked PPP payments had in practice been linked to IAS 17, with amounts relating to changes in indices expensed as incurred. The change in guidance will align with IFRS 16 requirements.

Lessor transition approach

7.15 Lessors generally are not required to make adjustments on transition to IFRS 16. However, one exception is for subleases. Lessors are required to reassess the subleases previously classified as operating leases under IAS 17, to see if the classification is still appropriate following the provisions of IFRS 16. Any operating leases under IAS 17 that should be classified as finance leases under IFRS 16 should be accounted for as a new finance lease entered into at the date of initial application.

Chapter 8

Whole of Government Accounts

8.1 Implementation of IFRS 16 presents some challenges to WGA. The asymmetry between lessee and lessor accounting will make eliminations more complex for intra-governmental leases. Similarly, the change to the classifications of subleases may make eliminations more complex for intra-governmental leases. The data collection and accounts preparation process will require changes to address this issue. See Box 8.A for a simplified example of how intra-governmental eliminations will work under IFRS 16.

8.2 IFRS 16 data collection will be built into the WGA data collection process, and entities will need to understand which leases they hold with other bodies within the WGA boundary (from both the lessor and lessee perspective). This data will be collected and stored in separate account codes, allowing for intra-governmental transactions to be identified and eliminated.

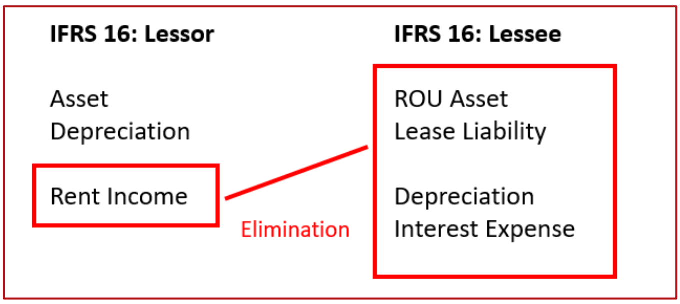
8.3 Disclosures in WGA will also require more detail in the transition year to allow users of the financial statements to understand the impact of IFRS 16 implementation. Post-implementation disclosures will require more judgement, and potentially more information, to meet the disclosure objective in IFRS 16.

8.4 Supplementary data may need to be collected as part of the transition process, particularly to support adjustments to opening balances, and to demonstrate that IFRS 16 has been implemented in a materially consistent fashion across WGA.

8.5 Finally, in fiscal years 2019-2020, 2020-21, and 2021-22, some entities within the WGA boundary will apply IFRS 16, and others will apply IAS 17. WGA data collection is expected to be carried out based on IAS 17, and therefore departments applying IFRS 16 will need to be able to unwind their transition adjustments for WGA purposes.

8.6 Entities with intra-group leases will likely need to consider similar issues for their group financial statements, particularly with respect to eliminations.

Box 8.A: Illustration of WGA eliminations under IFRS 16



Chapter 9
Budgets and Estimates

Budgets

9.1 Budgeting for leases should follow the principles in IFRS 16. Detailed budgeting guidance on IFRS 16 is available here.

Estimates

9.2 Where there is a change in accounting standards there is no net impact on budgets and the Supply sought at the time was correct. Parliament is therefore content not to see a Prior Period Adjustment (PPA) on the voted part of the Estimate (i.e. Part I, Part II).

9.3 However, Parliament does require departments to identify the change due to adopting a new accounting standard and the impact on prior years in the 'Note F to an Estimate-Accounting Policy changes.' Further details can be found in paragraphs 3.39-3.40 of the Supply Estimates guidance manual.

Appendix 1
Discounting lease liabilities

1. Under IFRS 16, as adapted and interpreted by the Financial Reporting Manual, there is a presumption that where entities cannot readily determine the interest rate implicit in the lease, they are instead required to use the HM Treasury discount rate promulgated in PES papers as their incremental borrowing rate. However, if an entity can demonstrate that another discount rate would more accurately represent their incremental borrowing rate (for example, if they undertake external borrowing independently of the Exchequer), they shall use that discount rate as their incremental borrowing rate. This is outlined in 3.6 to 3.10 above.

2. Where entities use the discount rate promulgated in PES papers, HM Treasury will issue a single nominal discount rate to apply to leases (real rates will not be applied). This rate is derived from the yield curves on government gilts, as a measure of the cost of government borrowing, and so is an appropriate proxy for the lessee's incremental borrowing rate. The PES papers are issued annually in December.

3. To measure the lease liability, variable lease payments tied to an inflation index by contract terms can be inflated using HM Treasury CPI inflation rates (also promulgated in PES papers), or another inflation rate if entities demonstrate the alternative inflation rate is more applicable to the underlying cash flows.

4. Entities should be careful to ensure they do not overstate lease payments where the payment/rent review sets cash flows for a set period (i.e. 5 years), by subsequently updating cumulative inflation for each new year in the set period. Example B below clarifies this and provides an example of how cash flows can be inflated.

5. Departments should be familiar with IFRS 16: 39-43, which outlines the circumstances in which lease liabilities are remeasured and when the discount rate should be revised.

6. The below provides two examples of how to discount lease payments on initial measurement of a lease liability, showing both a lease with no rent reviews, and a lease with a rent review based on an inflation index. The below uses 1.81% as an example nominal discount rate and inflation rates as issued in PES 2018 (12) (where the inflation rate applied on cash flows from after 2 years from the date of SOFP is 2%).

7. Entities should bear materiality in mind when applying this guidance, just as in other areas of financial reporting.

A: Example of 10 year lease with cash flows each year of £1m and no rent reviews

Year	Lease cashflow	Nominal rate (%)	Present Value*
1	£1,000,000	1.81%	£982,222
2	£1,000,000	1.81%	£964,760
3	£1,000,000	1.81%	£947,608
4	£1,000,000	1.81%	£930,761
5	£1,000,000	1.81%	£914,214
6	£1,000,000	1.81%	£897,961
7	£1,000,000	1.81%	£881,997
8	£1,000,000	1.81%	£866,316
9	£1,000,000	1.81%	£850,915
10	£1,000,000	1.81%	£835,787
			£9,072,540

B: Example of a 13 year lease with cash flows each year of £1m and a rent review in year 8. The rent review takes CPI at year 8 close vs lease commencement and inflates cash flows for year 8 onwards

Year	Lease cashflow	Inflation rate (%)		Cumulative inflation rate	Inflated cashflows	Nominal rate (%)	Present Value*
1	£1,000,000	0			£1,000,000	1.81%	£982,222
2	£1,000,000	0			£1,000,000	1.81%	£964,760
3	£1,000,000	0			£1,000,000	1.81%	£947,608
4	£1,000,000	0			£1,000,000	1.81%	£930,761
5	£1,000,000	0			£1,000,000	1.81%	£914,214
6	£1,000,000	0			£1,000,000	1.81%	£897,961
7	£1,000,000	0			£1,000,000	1.81%	£881,997
8	£1,000,000	2%	Inflation fixed**	17%	£1,171,659	1.81%	£1,015,028
9	£1,000,000	2%		17%	£1,171,659	1.81%	£996,982
10	£1,000,000	2%		17%	£1,171,659	1.81%	£979,258
11	£1,000,000	2%		17%	£1,171,659	1.81%	£961,848
12	£1,000,000	2%		17%	£1,171,659	1.81%	£944,748
13	£1,000,000	2%		17%	£1,171,659	1.81%	£927,952
					£14,029,956		£12,345,338

*The present value formula is = lease cashflow/(1+nominal rate)^year

** Note the rent review occurs only once and fixes cashflows for years 8 onwards. Therefore the cumulative level of inflation to apply on cashflows from year 8 onwards is also fixed at the cumulative inflation rate derived for the rent review