Financial Reporting Advisory Board Paper

Code of Practice on Local Authority Accounting

Issue:	Update on CIPFA/LASAAC development of the *Code of Practice on Local Authority Accounting in the United Kingdom* (the Code)
Impact on guidance:	This report sets out the current position with regard to the Update to the 2020/21 Code (for Transport for London (TfL) only) and the outcomes of the 2021/22 Code consultation. FRAB Members are also requested to consider FRAB reports FRAB 134 (04) and 138 (07) and the previous decisions made by the Board.
IAS/IFRS adaptation?	A) IFRS 16 *Leases* – The Update to the 2020/21 Code includes the adaptations as agreed with FRAB. B) 2021/22 Code – no new adaptations anticipated. C) Adoption of IFRS 16 Leases – the CIPFA LASAAC housing sub group proposes changing the adaptation scoping housing tenancies out of IFRS 16 accounting to an interpretation that indicates that housing tenancies are operating leases and with the exception of the reporting of housing tenancy income the disclosure requirements for operating leases for lessors do not apply as they are not relevant.
Impact on WGA?	The Update of the 2020/21 Code may require adjustments for TfL for WGA purposes.
IPSAS compliant?	A) IFRS 16: The adoption of IFRS 16 will create a misalignment with IPSAS which is based IAS 17 *Leases*. The IPSASB is currently developing an Exposure Draft based on IFRS 16. B) Development of 2021/22 Code: The Code has included reference to IPSAS 29 *Financial Instruments: Recognition and Measurement* this will now be replaced with IPSAS 41 *Financial Instruments* with regard to accounting for loans at discretionary rates. There are no changes though to the recognition and measurement requirements for financial instruments. The Code does not yet adopt IPSAS 42 *Social Benefits* though there are unlikely to be substantial differences in accounting treatment.
Impact on budgetary regime?	None – local authorities only.
Alignment with National Accounts	The Update of the 2019/20 Code may require adjustments for TfL for National Accounts purposes.
Impact on Estimates?	None – local authorities only.

Recommendation:	This report requests: 1. approval of the Statement on the Update to the 2021/22 Code which applies only to TfL. 2. that FRAB provide comments on the Single-Issue Consultation – Housing Revenue Account Tenancies and Leasing Standards 3. approval of the 2021/22 Code.
Timing:	2020/21: IFRS 16 *Leases* early adoption considerations affect 2020/21 2021/22 2022/23

DETAIL

Background

1. CIPFA LASAAC met on 3 November 2020 to consider the outcomes of its annual consultation. FRAB Members will be aware that CIPFA LASAAC had delayed publication of the 2020/21 Code to remove the provisions of the delayed adoption IFRS 16 *Leases.* This also led to delay in the annual timetable for the development of the Code. In order to catch-up with normal Code production timescales the consultation on the 2021/22 Code was issued on 3 September 2020 for a reduced period of six weeks. The normal timescales are eight weeks.

2. The number of respondents to the Code consultation was, as expected, substantially reduced from the normal numbers at 25 respondents (last year's consultation response rate was 42). It is considered that the reduction in response rate was due to the highly technical nature of the consultation and the reduced resources in finance teams as a result of the COVID - 19 Pandemic.

3. The consultation papers included final implementation issues relating to IFRS 16 and normal standards updates. It also included a question on the Redmond Review and a number of questions relating to CIPFA LASAAC's Strategic Plan. Note that one of the responses was a late response and that the statistics included in this report are based on 24 respondents.

4. A copy of the Draft of the 2021/22 Code [has been provided to FRAB][1] and a record of the amendments is included at Annex 1.1. It should be noted that the decisions outlined in this report are early decisions and they await the final approval of CIPFA LASAAC.

IFRS 16 Leases Implementation

5. At its meeting on 9 November 2020 CIPFA LASAAC Members considered the implementation date for the adoption of IFRS 16 and the impact of the pandemic. The issue was raised by a small number of respondents to the consultation with one, a large authority,

[1] replaced "attached to this report at Annex 1" with [text]. The Code itself was not included as an Annex due to its significant length

indicated that it would not be able to implement the standard for the 2021/22 financial year. The Board considered the impact of the pandemic in depth with members raising the issue of the additional workload, for example, the implementation and administration of grants to businesses. This was on top of the issue of staff redeployment to other tasks. Additionally, the impact of the delay of the accounts and audit timetables in local government meant that this had a knock-on effect to the annual timetables and the work of finance teams in local government.

6. CIPFA LASAAC also considered polls undertaken by CIPFA's Finance Advisory Network indicating that only 8% (March 2020) and 11% (September 2020) considered themselves reasonably well prepared. CIPFA LASAAC decided to delay the implementation of the standard in government until 2022/23 financial year. CIPFA LASAAC agreed to consider the debate and advice from FRAB at its 19 November 2020 meeting and the impact of any decisions taken on Whole of Government Accounts. CIPFA LASAAC will meet to consider these issues at its 20 November 2020 meeting.

Update to the 2020/21 Code (Transport for London Only)

7. Transport for London (TfL) adopted IFRS 16 in their 2019/20 financial statements, in line with an Update to the 2019/20 Code which included a revised Section 4.2 setting out the Code treatment under IFRS 16, and consequential amendments to other parts of the 2019/20 Code. The principles and Code's provisions included in the 2019/20 Code have to be extended to the 2020/21 and possibly the 2021/22 Codes. TfL will be able to follow the Update to the 2019/20 Code to produce fully updated reporting requirements applicable to TfL in 2020/21.

8. Rather than reproducing a full 2020/21 Code Update CIPFA LASAAC propose issuing a statement indicating that the Update to the 2019/20 Code will also apply to the 2020/21 year except for a number of minor amendments. The Statement is therefore accompanied by a list of a small number of differences arising from minor changes to the 2020/21 Code. The Statement from CIPFA LASAAC subject to FRAB's agreement would not require a statement from the Chair of FRAB. A draft of the Statement for the FRAB's consideration is attached at Annex 2.

IFRS 16 and Housing Tenancies

9. FRAB will be aware that CIPFA LASAAC has established a sub-group to consider the impact of the standard on housing tenancies but also to consider the potential impacts of IAS 17 *Leases*. The sub-group first met in July 2020 and has met four times in total. Its membership includes three CIPFA LASAAC Members, FRC representation and the CIPFA LASAAC Secretariat. CIPFA LASAAC is very grateful to the sub-group for all its work.

10. CIPFA LASAAC recognised that it would be difficult to complete the work in time for any changes identified as necessary to be included in the 2021/22 Code but agreed that the sub-group would make its best efforts to do this. This sub-group has manged to complete its analysis – produced in a Technical Appendix and a consultation paper attached as Annexes 3 and 4 to this report, with the Exposure Draft at Annex 5. Due to the short timescales the

draft consultation papers have been sent to CIPFA LASAAC at the same time as they are being sent to FRAB in order that FRAB can consider progress to date and make any relevant comments. CIPFA LASAAC has agreed to this on the basis that otherwise FRAB would have to be sent an out of meeting paper.

11. In relation to IFRS 16 the sub-group considered three questions in the consultation paper covering three sections:

    - Is the secure tenancy for tenants within local housing authorities a lease for accounting purposes (section B)?

    - If the secure tenancy meets the definition of a lease, is it a finance or an operating lease (section C)?

    - Dependent on the classification decided on in section C, what reporting requirements will be needed by the users of local authority financial information relating to housing tenancies and the related assets (section D)?

12. The sub-group focussed its analysis on secure tenancies because government statistics confirm that these comprise 94 % of the tenancies held by local authorities in England. The tests have of necessity and due to the lack of information in some areas been provided on an average, estimated or countrywide basis and some information was provided on a sample basis (though this sample was statistically relevant).

13. The sub-group has concluded that under IAS 17 secure tenancies are not leases because the period of time has to be agreed. As there are no end dates agreed in secure tenancies then they do not meet the definition of a lease.

14. The sub-group undertook the full analysis required by IFRS 16 to consider whether a contract is or contains a lease. The sub-group concluded that the majority of the evidence available meant that housing tenancies are leases:

    - the secure tenancy agreement is a contract which identifies the asset as the council dwelling in question

    - the tenant consumes substantially all of the economic benefits from the use of the asset throughout the period of use and, specifically, the tenant can direct the use of the asset

    - the authority benefits from the service potential in the asset but this is used at the point the tenancy is granted.

    The sub-group is of the view that these arguments are likely to apply to other forms of tenancy though this is subject to consultation.

15. The sub-group also concluded that housing secure tenancies are operating leases as substantially all the risks and rewards of ownership had not transferred from local authorities. This is principally because the authority will retain the rewards of ownership in the form of the rights to the appreciation in sale value and the receipt of rental income from the tenant. The

sub group considered the other lease tests in IFRS 16 and considered them on both a ‘reasonably certain’ basis (the level of judgement required by the standard) but also on the lower level of probable assessment to ensure that the tests in IFRS 16 (examples of situations) were met. All of the example situations in the first set of indicators, particularly the ones based on the lease term being the major part of the economic life of the asset and the present value of the rental streams being a substantially all of the fair value of the asset did not lead to the conclusion that the risks and rewards of ownership had transferred from local authorities. The second set of indicators (in as much as they applied to housing tenancies) also did not lead to the conclusion that the risks and rewards had transferred from local authorities. Therefore, the sub-group concluded that secure housing tenancies were operating leases.

16. The sub-group was also of the view that any other forms of tenancy were less likely to transfer the risks and rewards of ownership of the council dwellings from local authorities and therefore the sub-group has proposed that on the adoption of IFRS 16 an interpretation is included in the Code that housing tenancies are operating leases.

17. The sub-group has also considered the disclosures for operating leases under IFRS 16. It concluded that the disclosure relating to lease income was already met as housing rental income is included on the face of the Housing Revenue Account Income and Expenditure Statement. It considered that the requirement to report how the lessor manages the risk associated with any rights it retains in underlying assets (which principally relates to the management or residual values) is not relevant to local authorities as local authorities are not able to realise residual values. When a dwelling becomes vacant, they have to re-let them as soon as possible. The final disclosure on the maturity of lease payments is also not relevant as these can only be ensured for the notice period.

18. As the disclosure information is either satisfied by other reporting requirements or is not relevant the sub-group proposes adding to the interpretation to confirm this position. This has been included in the Exposure Draft.

Service Concession Arrangements – Measurement of the Liability

19. CIPFA LASAAC consulted for the third year on the measurement of the service concession arrangement liability. It considered two options – option 1 – measurement of the service concession arrangement as the lease liability where the liability may change if the cash flows are modified and option 2 – measurement of the liability under the actuarial measurements allowed by IAS 17 and where the liability is fixed at the commencement. The largest number of respondents (50%) supported option 1 while 29% supported option 2. The positive response to option 1 has substantially reduced since it was considered last year at (81%). The respondents supporting option 1 considered the difficulties of continuing to use the measurement provisions in a standard which was no longer extant, the symmetry of application to IFRS 16 and the ability to use the modifications provisions in IFRS 16. The respondents supporting option 2 were principally concerned with workload issues related to the change of measurement (which might need to be replicated on an annual basis). One respondent commented that the nature of service concessions is that they are a combination of the purchase of an asset and the delivery of services. Therefore, the element of the unitary charge which repays the liability is akin to borrowing to finance the purchase of an asset.

20. This response would indicate that remeasurement should impact wholly on the delivery of service. However, another respondent (an audit firm) indicated that the proportion of indexed unitary charge in PFI operator financial models is there solely to optimise the overall funding solution and the indexed element rarely if ever derives either directly or indirectly from assumptions for lifecycle and facilities management costs. These two opposing conceptual views need to be considered so that any change in measurement is appropriate to the fact pattern that arises in the contracts. CIPFA LASAAC has therefore agreed to establish a working group to consider the issue and the approach to measuring the liability under IFRS 16. Until this group has resolved the issue CIPFA LASAAC does not propose to change the measurement provisions for service concession arrangements. It is anticipated that the working group will complete its work in 2021.

Aspects of the Public Sector Interpretation for Leases at Nil Consideration, a Nominal Amount, or at a Peppercorn

21. Following the issues raised on implementation by Transport for London of the interpretation for leases at nil consideration, nominal amount or at a peppercorn which require such leases for lessees to be treated as donated assets where the lease was a commercial transaction (reported to FRAB at its June meeting), CIPFA LASAAC sought to find out whether there were any local authorities encountering similar transactions. No substantial evidence was generated by the consultation responses. However, the responses did indicate that it would be important to be clear in the Code what type of transactions the interpretation was meant to cover. CIPFA LASAAC has therefore included the clarification in the Code Draft (included in Appendix F of the Code which includes the agreed provisions relating to the Code's adoption of IFRS 16) such that the interpretation only relates to transactions where the substance of the transaction is that the lessor donates the asset to the lessee (see Appendix F Code paragraphs 4.2.1.5, 4.2.2.48, 4.2.2.51 and 2.3.2.17).

COVID-19-Related Rent Concessions: Amendments to IFRS 16

22. CIPFA LASAAC proposed to include cross reference to COVID-19 Related Rent Concessions: Amendments to IFRS 16 in the 2021/22 Code. This was agreed to by 62% of the respondents to the consultation with 17% disagreeing. CIPFA LASAAC agreed that it would proceed with these amendments if it continued with implementation of IFRS 16 in 2021/22. The amendments would not apply as they are time limited to 30 June 2021 if CIPFA LASAAC proceeds with its deferral to 2022/2023.

23. The issue of whether the Code should provide guidance on COVID-19 related rent concessions was raised at CIPFA LASAAC's meeting at the 3 November 2020. Accounting for COVID-19-related rent concessions has been included as an amendment to FRS 102 *The Financial Reporting Standard Applicable in the UK and Republic of Ireland* in October 2020. The FRC included the amendments because there were differences of opinion over how the requirements of FRS 102 should be applied to COVID-19-related rent concessions, specifically those arising from forgiven payments in operating lease agreements. There was not much evidence that this was an issue in the consultation on the 2021/22 Code. However, the Secretariat considers that there might be an opportunity to add this to the consultation on

HRA on HRA tenancies and IFRS 16 and will seek CIPFA LASAAC's views on whether it should be included in the single issue consultation (though it is recognised that this would no longer be a single issued consultation).

Annual Standards Updating

24. The following amendments to Standards will apply without adaptation or interpretation:

- Definition of a Business: Amendments to IFRS 3 *Business Combinations*
- Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS 7 (Phase 1)
- Interest Rate Benchmark Reform - Phase 2: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16– note that this is subject to UK endorsement by 1 January 2021. Note also that 2021/22 Code would also not include the amendment relating to IFRS 16 due to the deferral decision.

Dedicated Schools' Grant

25. At FRAB 141 CIPFA LASAAC reported on the accounting treatment of the Dedicated School's Grant emanating from deficit's generated on these grant accounts. The Ministry of Housing, Communities and Local Government has issued an amendment to the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. The amendments to the Regulations[1] insert a new regulation which provides that where a local authority has a deficit on its school budget, the authority must not charge any such deficit to its revenue account. Instead, the amendments provide that local authorities must charge any such deficit to a separate account, established and usable only for that purpose. The 2021/22 Code includes an amendment to recognise the introduction of the new legislative requirements.

Other Changes

26. The 2021/22 Code also includes other mostly minor changes including:

- reference the UK endorsement process
- augmentation to its provisions on estimation uncertainty at paragraph 3.4.2.91 in accordance with the provisions of IAS 1 *Presentation of Financial Statements*
- updating of references relating to IPSAS 29 *Financial Instruments: Recognition and Measurement* to IPSAS 41 *Financial Instruments* including the confirmation that this has not changed the recognition and measurement requirements for financial instruments
- supplementary confirmation of the adaptation which has been in place since the inception of the IFRS -based Code in relation to standards issued but not yet adopted under IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, and

[1] The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2020

- clarification of the calculation process for the Capital Financing Requirement which is based on the requirements of CIPFA's *Prudential Code for Capital Finance in Local Authorities*.

Redmond Review

27. The Code consultation also included questions on the impact of the Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting led by Sir Tony Redmond (the Redmond Review). CIPFA LASAAC did not included a structured consultation question because the Redmond Review recommendations were issued three days before the planned issue of the Code consultation. The views provided were therefore not necessarily representative of those that would have been received if specific questions were asked. CIPFA LASAAC's consideration of the responses focussed on the areas directly relevant to its work ie the commentaries related to the proposal for a Standardised Statement on Service Information and the impact of the recommendations on the development of the Code. CIPFA LASAAC will use this feedback when it is clear what the future direction of the recommendations.

Strategic Plan – Questions

28. The consultation questions also included a number of questions on various elements of its Strategic Plan which CIPFA LASAAC will consider at its meeting on 20 November 2020. This will enable it to revisit and reprioritise its plans of work across its workstreams and themes. CIPFA LASAAC will report to FRAB on its updated Strategic Plan at the Board's March 2021 meeting.

Summary and recommendation for the Code of Practice on Local Authority Accounting in the United Kingdom

29. This report requests approval of the Statement on the Update to the 2021/22 Code which applies only to TfL.

30. It also requests comments on the Single-Issue Consultation – Housing Revenue Account Tenancies and Leasing Standards

31. The report requests approval of the 2021/22 Code.

CIPFA/LASAAC
November 2020

Record of Amendments to the 2021/22 Code

Paragraph Number	Reason for Amendment
Paragraph 1.2.7	Confirmation of the move to the UK Endorsement Process.
Paragraph 1.3.1	Confirmation of the application date for the 2021/22 Code.
Paragraph 1.3.12	Change of date for the deferral of IFRS 16 Leases to the 2022/23 Code and confirmation of the change from date in the Code.
Paragraph 1.6.2	Confirmation of the move to the UK Endorsement Process and changes in date for the endorsement process and IFRS 16 deferral.
Paragraph 2.3.3.13	Confirmation of accounting treatment for the changes brought about as a result of the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2020.
Paragraph 3.3.1.3	Confirmation of the adaptation which has been included in the IFRS based Code since its inception of standards issued but not yet adopted under the Code's adoption of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.*
Paragraph 3.3.4.3	Annual date changes for the confirmation of the adaptation to IAS 8.
Paragraph 3.3.6.1	Normal confirmation of the changes to the section of the Code with the additional confirmation that this change is not a new reporting requirement but has been included in the Code since its inception.
Paragraph 3.4.2.91	Augmentation of the Code's provisions on estimation uncertainty.
Paragraph 4.1.4.3 5)	Confirmation that the Capital Financing Requirement is calculated based on the provisions in the Prudential Code.
Paragraph 7.1.1.1	Replacement of IPSAS 29 *Financial Instruments: Recognition* and Measurement with IPSAS 41 *Financial Instruments.*
Paragraph 7.1.12.1	Normal confirmation of the changes to the section of the Code with the additional

Paragraph Number	Reason for Amendment
	confirmation that there have been no changes to the recognition and measurement requirements for financial instruments.
Paragraph 7.2.4.4	Confirmation by cross-reference that the Interest Rate Benchmark Reform - Phase 2: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 (IBOR Phase 2) amendments apply to local authorities.
Paragraph 7.2.4.5 to 7.2.4.6	Confirmation by cross reference of the transitional reporting requirements of IBOR Phase 2.
Paragraph 7.3.2.16	Confirmation by cross-reference of the additional reporting requirements arising from IBOR Phase 2.
Paragraphs 7.3.2.17 to 7.3.2.21	Paragraph renumbering as a result of inserted paragraph 7.3.2.16.
Chapters 2 to 9 and Appendix A	The end of each section/chapter confirms any changes that have been made to that section/chapter or confirms that no changes have been made.
Appendix C: Changes in accounting policies: disclosures in the 2020/21 and 2021/22 financial statements	Changes to reflect the standards which have been updated in the 2021/22 Code and the transitional reporting requirements.
Appendix D: New or amended standards introduced to the 2021/22 Code	New standards are listed.
Appendix F: Accounting provisions on the adoption of IFRS 16 Leases from 1 April 2022	All dates have been changed to reflect the deferral of IFRS 16.
Appendix F: Paragraph 4.2.1.5	Clarification of the treatment of leases with nil or nominal consideration or at a peppercorn.
Appendix F: Paragraph 4.2.2.48	Clarification of the treatment of leases with nil or nominal consideration or at a peppercorn and removal of internal inconsistency for the measurement of donated assets.
Appendix F: Paragraph 4.2.2.51	Clarification of the treatment of leases with nil or nominal consideration or at a peppercorn.
Appendix F: Paragraph 2.3.2.17	

STATEMENT BY THE CIPFA LASAAC LOCAL AUTHORITY ACCOUNTING CODE BOARD ON THE UPDATE TO THE 2020/21 CODE OF PRACTICE ON LOCAL AUTHORITY ACCOUNTING IN THE UNITED KINGDOM

Introduction

This statement provides the basis for the application of the 2020/21 *Code of Practice on Local Authority Accounting in the United Kingdom* (the Code) to Transport for London.

The Update to the 2019/20 *Code* applied only to Transport for London, in order to allow for the early adoption of IFRS 16 *Leases.*

That Update shall also apply as the Update to the 2020/21 Code in order to allow the continuing use of IFRS 16 *Leases* by Transport for London.

All other provisions in the 2020/21 Code apply as published.

Basis for application of the update

The Update to the 2019/20 Code took the form of:

- a revised Section 4.2 (Leases (Transport for London Only)) setting out the Code treatment under IFRS 16, and
- consequential amendments to other parts of the 2019/20 Code.

The Update of the 2019/20 Code included transitional reporting requirements in section 4.2. These are no longer relevant as Transport for London has adopted the IFRS 16 reporting requirements in its financial statements. The Update of the 2019/20 Code also included material describing differences from the 2018/19 Code which are also no longer relevant.

Transport for London shall therefore apply the remaining provisions of the Update to the 2019/20 Code as the Update to 2020/21 Code for IFRS 16. The Annex to this Statement explains how provisions are to be applied to paragraphs of the 2020/21 Code which have been renumbered.

CIPFA LASAAC LOCAL AUTHORITY ACCOUNTING BOARD
DECEMBER 2020

ANNEX TO THE CIPFA LASAAC STATEMENT

The requirements of the 2020/21 Code shall apply except where modified by the Update to the 2019/20 Code to allow the continuing use of IFRS 16, *Leases* by Transport for London.

The provisions in the Update which remain applicable mostly relate to paragraphs, sections and chapters which are identically numbered in the 2020/21 Code. However, two of the amendments in the table on page 35 of the Update relate to paragraphs which have been renumbered, as follows:

Update to the 2019/20 Code	Update to the 2020/21 Code	Wording Change
Paragraph 3.4.2.71 Financing Activities c)	Paragraph 3.4.2.72 Financing Activities c)	'Finance lease' should be read as 'lease'
Paragraph 3.4.2.75 Financing Activities c)	Paragraph 3.4.2.76 Financing Activities c)	'Finance lease' should be read as 'lease'.

The 2021/22 Code of Practice on Local Authority Accounting in the United Kingdom – Single Issue Consultation – Housing Revenue Account Tenancies and Leasing Standards

Invitation to Comment

the people
in public finance

code 2021/212itc

Invitation to Comment

Introduction

1. Local authorities in the United Kingdom are required to keep their accounts in accordance with 'proper practices'. This includes, for the purposes of local government legislation, compliance with the terms of the *Code of Practice on Local Authority Accounting in the United Kingdom* (the Code), prepared by the CIPFA LASAAC Local Authority Accounting Code Board (CIPFA LASAAC). The Code is reviewed continuously and is issued annually.

2. Under the oversight of the Financial Reporting Advisory Board (FRAB), CIPFA LASAAC is able to issue mid-year updates to the Code. However, this will only be done in exceptional circumstances.

3. The edition of the Code that is applicable for a financial year is normally based on accounting standards in effect on 1 January prior to the start of the financial year. For the 2021/22 Code, this means the UK endorsed accounting standards with an effective date of 1 January 2021 or earlier will need to be taken into account[1].

4. An overview (Part 1) summarises the areas being consulted on for the proposals to developing the new edition of the Code (the 2021/22 Code) as it relates to the accounting for housing tenancies under the leasing standards. Part 2 of the Invitation to Comment (ITC) sets out CIPFALASAAC's, comments in more detail and will consider the changes which will apply to accounting periods commencing on or after 1 April 2021. CIPFA LASAAC has also provided a Technical Appendix which includes the detailed considerations provided by its Housing Sub-Group consisting of CIPFA LASAAC Members and Observer nominees. CIPFA LASAAC would like to thank the sub group members for their work on producing this consultation paper.

The Consultation Process

5. Where CIPFA LASAAC is interested in specific issues, consultation questions have been included in the ITC. However, CIPFA LASAAC also welcomes responses to individual questions or areas if these are of specific interest to a stakeholder. In order to assess comments properly, CIPFA LASAAC would prefer respondents to support comments with clear evidence, reasons and, where applicable, preferred alternatives.

6. Responses to this ITC will be regarded as on the public record and may be published on the CIPFA website unless confidentiality is specifically requested. Copies of all correspondence and an analysis of responses may be provided to the Financial Reporting Advisory Board.

7. A copy of the Exposure Drafts of the 2021/22 Code in PDF format can be downloaded from the CIPFA website.

8. To assist interested parties in responding to the consultation, a response form (in Word format) is attached. We would be grateful if respondents to the consultation could use this form as this will speed up the analysis.

[1] The 2021/22 Code now applies standards adopted for UK application under the terms of The International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 (SI 2019/685).

9. Responses are required by **date** and may be sent, preferably e-mailed, to:

Email: cipfalasaac@cipfa.org

Or by post to:

The Secretary

CIPFA LASAAC Local Authority Accounting Code Board

c/o Policy and Technical Directorate

CIPFA

77 Mansell Street

London

E1 8AN

(For ease of handling, emailed responses using the Word document form provided are preferred.)

PART 1 – SUMMARY

10. The following tables provide an overview of the areas where stakeholder feedback would be particularly appreciated:

PART 2: HOUSING REVENUE ACCOUNT TENANCIES AND LEASING STANDARDS

PART 2: HOUSING TENANCIES AND LEASING STANDARDS

Section A: Introduction

11. The Housing Revenue Account (HRA) plays an important role in local authority financial reporting. It is a financial statement that reflects a statutory obligation to maintain a revenue account for local authority housing provision in accordance with Part 6 of the Local Government and Housing Act 1989 (England and Wales) or the Housing (Scotland) Act 1987. In England and Wales, Schedule 4 of the 1989 Act specifies the debits and the credits to the account.

12. Income from housing tenancies have generally been treated in the Code as rental payments with these payments being an integral part of the statement. Income is recognised on an accruals basis in accordance with the revenue accounting standard's basis ie in accordance with the Code's adoption of IFRS 15 *Revenue from Contracts with Customers*. Rental income is recognised on the face of the HRA Statement.

13. Across the three countries of the UK where Housing Revenue Accounts exist the Code requires separate reporting of rent arrears (Code, paragraph 3.5.4.2). Disclosures are also required for number and types of dwelling for each housing authority.

14. English authorities are required by The Housing Revenue Account (Accounting Practices) Directions 2016 to provide detailed disclosures on Housing Revenue Account housing stock including current value, vacant possession values, sources of financing etc. These disclosure requirements are included in the Code at paragraph 3.5.5.1 for ease of reference and to ensure consistency of the Code with statutory provisions.

15. Arguably the current approach in the Code generally means that a treatment similar to operating lease accounting treatment is applied to HRA tenancies, since the assets are retained on the authority's balance sheet and income is generally treated on a consistent basis with no material indirect costs or discounts requiring changes in the income recognition profile and the transparency of the separate disclosure of rental income on the face of HRA income and expenditure statement.

16. It is also arguable that due to the statutory nature of the Housing Revenue Account enough information was specified under the current arrangements for the users of Housing Revenue Account financial statements and therefore no further information was required. CIPFA LASAAC therefore decided to exclude housing tenancies from the scope of IFRS 16 *Leases*.

17. However, CIPFA LASAAC has agreed following challenge and commentary from FRAB that it would provide a further analysis on whether this accounting treatment was the most useful for users of local authority financial statements.

18. Generally, it is understood that for local authorities most tenancies are secure tenancies (see paragraph 27). It was therefore decided that CIPFA LASAAC would consider the lease accounting tests under IFRS 16 *Leases* for secure tenancies as a primary consideration. This option was chosen because except for the definition of a lease and the provisions for considering a lease term, the tests for classification of leases are the same for IAS 17 *Leases* and the supporting interpretations as they are for IFRS 16 and therefore the outcomes will be the same.

19. In order to consider the lease accounting treatment CIPFA LASAAC is of the view that the following three questions apply in accordance with the provisions of IFRS 16:

- Section B: Is the secure tenancy for tenants within local housing authorities a lease for accounting purposes?
- Section C: If the secure tenancy meets the definition of a lease, is it a finance or an operating lease?
- Section D: Dependent on the classification decided on in Section C, what disclosure requirements will be needed by the users of local authority financial information relating to housing tenancies and the related assets?

Section B: Is the secure tenancy for tenants within local housing authorities a lease for accounting purposes?

21. The Technical Appendix considers the guidance provided in IFRS 16 on whether an agreement is or contains a lease. It uses as its basis the definition of a lease, which is analysed in the application guidance in Appendix B of IFRS 16. Also considered are the questions contained in the flow chart at paragraph B31 of IFRS 16 which is included in the Annex to the Technical Appendix.

22. Secure tenancies are not legally leases. Leases are defined in the Code and IFRS 16 as '*A contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration'.*

23. In order to assess whether a contract is a lease throughout the period of use local authorities need to assess whether the tenant has the right to obtain substantially all of the economic benefits and from use of the asset and can direct its use. The Code adds service potential ie the capacity to provide services that contribute to achieving the local authority's service objectives to the assessment.

24. The assessment in the Technical Appendix considers that as:

- the secure tenancy agreement is a contract which identifies the asset as the council dwelling in question
- as the tenant consumes substantially all of the economic benefits from the use of the asset throughout the period of use and, specifically, the tenant can direct the use of the asset
- the authority benefits from the service potential in the asset but this is used at the point the tenancy is granted.

then it is likely that the tenancy agreement represents a lease.

25. There may be arguments around the issue that as there is no end date to a secure tenancy that there is no specified period of time and therefore the tenancy does not meet the definition of a lease and is outside the scope of the standard. Alternatively, it could be argued that the lease term is defined to be the length of the lease to date and the end period. It is also useful to consider that the *Housing SORP: 2018 Update, Statement of Recommended Practice for Registered Social Housing Providers* (the Housing SORP) considers rental agreements for tenanted social housing properties to be operating leases.

26. CIPFA LASAAC's assessment therefore is that the balance of factors is such that secure tenancies are in substance leases.

27. The Ministry of Housing, Communities and Local Government Statistical Release Social Housing Lettings: April 2018 to March 2019, England 2018/19 sets out that almost 94% of local authority new lettings in 2018/19 were lifetime or secure tenancies. Just 4 percent are fixed term. Therefore, CIPFA LASAAC is of the view that the assessment of whether a lease exists is likely to cover all but a small minority of social housing tenancies.

28. CIPFA LASAAC has not repeated the assessment in detail for these other forms of tenancy but they:

- are subject of a contract
- have an identified asset
- are likely to also provide tenants with the right (though only throughout the period of use) to transfer substantially all of the economic benefits from the use of the asset to the tenant, and
- allow the tenants to direct its use

in a similar way to secure tenancies. CIPFA LASAAC is of the view that these tenancies are also likely to be leases. CIPFA LASAAC would be interested to hear the views of stakeholders on this assessment.

Definition of a Lease under IAS 17 Leases

29. CIPFA LASAAC has considered the definition of a lease for secure tenancies under IAS 17 (see the Technical Appendix, Annex A) and is of the view that as they are not for an agreed period of time, they do not meet the definition of a lease. The key difference with the conclusion in paragraph 26 above is that IFRS 16 does not require the agreement to the period of time and it is therefore possible that the period of time can be indeterminate. As secure tenancies do not meet the definition of a lease there is no need to consider changing the current provisions in the 2020/21 Code for secure tenancies. This interpretation would only apply to leases without an agreed term and may not apply to flexible (fixed term) tenancies. However, as only 4 per cent of tenancies are fixed term (and 94 per cent are secure tenancies) CIPFA LASAAC is of the view that there is no need to specify any accounting treatment in the 2020/21 Code for these transactions.

Is the secure tenancy for tenants within local housing authorities a lease for accounting purposes?

Q1 Do you agree with CIPFA LASAAC's conclusions that a secure tenancy for housing tenants in substance represents a lease? If not, why not? Please provide a reason for your response.

Q2 Do you agree with CIPFA LASAAC's conclusions that a secure tenancy for housing tenants transfers substantially all the economic benefits from the use of the asset to the housing tenant? If not, why not? Please provide a reason for your response.

Q3	Do you agree that other forms of housing tenancies also in substance represents a lease? If not, why not? Please provide a reason for your response.
Q4	Do you agree that secure housing tenancies do not meet the definition of a lease under IAS 17 Leases and that there is no further need to specify an accounting treatment in the Code for any other forms of tenancy? If not, why not? Please provide a reason for your response.

Section C: If the secure tenancy meets the definition of a lease, is it a finance or an operating lease?

30. Both the Code and IFRS 16 require a lease to be classified as a finance lease when the substantially all the risks and rewards incidental to ownership of an underlying asset are transferred to the lessee (the tenant). Again, as local authorities do not hold assets solely for economic benefits consideration needs to be made of the impact of service potential when considering the transfer of risks and rewards.

31. CIPFA LASAAC is of the view that by providing the council dwelling to the tenant that the authority is maximising the service potential in the asset, but the service potential is applied when a tenancy is granted. The authority will retain the rewards of ownership in the form of the rights to the appreciation in sale value and the receipt of rental income from the tenant. It also retains the risks relating to repairs and maintenance to maintain the value of the asset. This is the standard position for all leases. The tenant while occupying also received the benefit of consumption of the value inherent in the property through occupation. CIPFA LASAAC is of the view though that the balance of the risks and rewards lie with the local authority and the lease is in substance and operating lease.

32. When considering the examples of circumstances prescribed by IFRS 16 which individually or in combination would lead to a lease being classified as a finance lease. CIPFA LASAAC considered the following:

- The lease does not transfer the ownership of the lease to the tenant.
- Although there is an opportunity for tenants to buy the asset under the right-to-buy provisions of section 118 of the Housing Act 1985 the economic circumstances are such at the inception of the lease (tenancy agreement) that tenants cannot afford to purchase council housing and that it is not reasonably certain that they will take up this option. It should also be noted that right-to-buy provisions are not included in the contract and therefore are not part of the lease but arise as a result of statutory provisions.
- Taking into account estimates of the average life of a secure tenancy based on national stock turnover (ie of 15 years) and the estimated average economic life of local authority housing stock of 53 years, the estimated length of the tenancy (the lease term) is not for the major part of the economic life of the council dwelling.

- Based on the average weekly rent of local authority council dwellings across England the net present value does not amount to substantially all of the fair value of the assets (on a sample basis).

- Council dwellings are not typically so specialised that they cannot be used without major modifications.

33. The example situations specified in the Code and IFRS 16 do not provide evidence that housing tenancies are finance leases. The Code and IFRS 16 provide three secondary indicators of situations that could lead to a lease being classified as a lease. CIPFA LASAAC is of the view that tenants do not bear the costs of lease cancellation. Neither of the other two indicators clearly apply to local authorities.

34. CIPFA LASAAC is of the view that on examination of both primary and secondary indicators that secure housing tenancies are operating leases. It has therefore included this as an interpretation in section 4.2 of the Code to ensure certainty in treatment for accounts preparers.

35. CIPFA LASAAC has not assessed in detail the other tenancy types (these include but may not be limited to introductory or flexible tenancies (including flexible tenancies with fixed terms) or licence arrangements) but is of the view that these tenancies are typically much shorter than secure tenancies and that the Right-to-Buy scheme does not apply. It is likely that in both an examination of the risks and rewards of ownership and the examples of circumstances or situations where leases could be classified as finances leases would result in the classification as operating leases. It has confirmed this position in the Code in the interpretation. CIPFA LASAAC would welcome views on its conclusions and the interpretation

If the secure housing tenancy meets the definition of a lease, is it a finance or an operating lease?

Q5 Do you agree with CIPFA LASAAC's conclusion that for secure housing tenancy agreements the lease is an operating lease? If not, why not? Please provide a reason for your response.

Q6 Do you agree with the proposed interpretation relating to housing tenancies as leases? If not, why not? Please provide a reason for your response.

Q7 Do you agree with CIPFA LASAAC's conclusion that all other forms of tenancies are also likely to be operating leases? If not, why not? Please provide a reason for your response.

Section D: Dependent on the classification decided on in section C, what disclosure requirements will be needed by the users of local authority financial information relating to housing tenancies and the related assets?

36. As set out in section A, the HRA includes substantial disclosure and reporting requirements for housing income, including rent arrears and on the value (and the movements in that value) of a housing authority's housing stock. The classification of housing tenancies as operating leases would then need to

consider the usefulness of the disclosures for operating leases. The disclosures relating to operating leases for lessors are considered in the table below.

Table 1: IFRS 16 Operating Lease Disclosures for lessors and their usefulness to the users of local authority financial statements

Disclosure	Usefulness of the disclosures to local authority financial statements
Lease income, separately disclosing income relating to variable lease payments that do not depend on an index or a rate.	Information relating to income from housing tenants and related services is shown on the face of the HRA Income and Expenditure Statement. It is unlikely that any further information is required.
How the lessor manages the risk associated with any rights it retains in underlying assets. A lessor is required to disclose its risk management strategy for the rights it retains in underlying assets, including any means by which the lessor reduces that risk.	The nature of local authorities' activities relating to the rental of social housing is explained in the narrative statement which precedes the HRA Income and Expenditure Statement. In England local authorities are required by The Housing Revenue Account (Accounting Practices) Directions 2016 to provide detailed disclosures on Housing Revenue Account housing stock. These disclosures are not directly related to the risks associated with the rights it retains in the council dwellings (e.g. freehold ownership), but they allow for monitoring movements in the housing stock and consideration of the state of these assets. Consideration might need to be given as to whether further information is provided in Scotland and Wales. The examples in IFRS 16 and the Code of what may be provided by this disclosure refers to residual value guarantees. As local authorities will seek to continue letting council dwellings rather than realising the residual value of these assets, this disclosure is not considered useful to the users of local authority financial statements. The Right-to-Buy provisions may represent a risk to the authority's right that it retains in these assets. However, given the low incidence of Right-to-Buy sales, this risk is deemed not to be significant. Therefore, this disclosure is also not considered to be

	useful to the users of local authority financial statements.
A maturity analysis of lease payments.	For most tenancy agreements payments can only be ensured for following four-week period and, possibly for some tenancies which are coming to an end, less than this. The objective of the IFRS 16 disclosures on leases is to enable users to more accurately forecast future lease cash flows and estimate liquidity risk) was not considered particularly relevant in the context of housing tenancies, and not relevant enough to justify introducing an additional disclosure (given the current information included in the notes to the HRA account). Consequently, this information is not useful to the users of local authority financial statements

37. The disclosures for operating leases for lessors under the current Code's adoption of IAS 17 include the requirement to report a description of a local authority's lessor arrangements (which is covered by the narrative description which precedes the Housing Revenue Account Income and Expenditure Statement) and a maturity analysis of lease payments under non-cancellable lease payments and for this latter disclosure the same reasoning set out in the above table applies.

38. CIPFA LASAAC is of the view therefore that the disclosures for operating leases for lessors as they apply to local authority housing tenancies are either already covered by the existing disclosures, or not relevant and not useful to users of local authority financial statements. Their inclusion risk obscuring information which is relevant in local authority accounts. It therefore proposes to include this in the interpretation in section 4.2 of the Code.

Dependent on the classification decided on in section C, what reporting requirements will be needed by the users of local authority financial information relating to housing tenancies and the related assets?

Q8 Do you agree with CIPFA LASAAC's conclusion for the reporting requirements in relation to the information requirements for the reporting of housing tenancies? If not, why not? Please provide a reason for your response.

Q9 What are your views on the usefulness of the IFRS 16 Leases disclosures for operating leases (included in the Annex to the Technical Appendix) when applied to housing tenancies?

Transitional Arrangements for IFRS 16 Leases

39. As set out earlier CIPFA LASAC is of the view that secure tenancies do not meet the definition of a lease under IAS 17 but meet the definition of a lease under

IFRS 16. Paragraph 4.2.2.93 includes a practical expedient which requires authorities not to apply IFRS 16 to contracts that were not previously identified as being leases or containing leases under IAS 17 and IFRIC 4. This does not have a practical impact as local authority reporting requirements do not change. However, should the consultation lead to any other conclusions the impact of this practical expedient may need to be considered.

Section E: General Application of the Leasing Standard in England

40. CIPFA LASAAC would note that the treatment of other leased assets used by the Housing Revenue Account should follow the general requirements of IFRS 16 and therefore depreciation related to the right of use asset would be charged to the HRA. This would be reversed by statutory provisions in Scotland and Wales but is not reversed under the self-financing regime in England.

Section F: Further Guidance

41. CIPFA LASAAC would also wish to remind stakeholders that comments or suggestions regarding the Code can be submitted to cipfalasaac@cipfa.org at any time. Please note that this is not an advice or enquiries service.

Further Guidance	
Q10	Are there any areas within the Code where additional guidance or improvements to the Code would be helpful? Please support your answer by giving details of the amendments you would suggest.

Technical Appendix – Accounting for Housing Tenancies under IFRS 16 *Leases*

Section A: Introduction - Technical Accounting Issues to be Considered in Relation to Housing Tenancies Under IFRS 16 and IAS 17

1. This Technical Appendix will consider the key issues relating to housing tenancies and leasing standards focussing on the new standard IFRS 16 *Leases*. The technical assessment will consider only secure tenancies entered into by housing tenants across Great Britain. It is considered that similar approaches and considerations will then be able to be applied to other tenancy agreements. This is particularly the case because secure tenancies are understood to be by far the largest type of tenancy held with local housing authorities (see paragraph 27 of the main Information to Comment ITC) document.

2. This Technical Appendix will consider the following three questions:

    - Section B: Is the secure tenancy for tenants within local housing authorities a lease for accounting purposes?

    - Section C: If the secure tenancy meets the definition of a lease, is it a finance or an operating lease?

    - Section D: Dependent on the classification decided on in Section C, what reporting requirements will be needed by the users of local authority financial information relating to housing tenancies and the related assets?

3. **This Technical Appendix will of necessity consider the secure tenancy from a general basis making common assumptions. This is the case as it is trying to make an overall assessment. Transactions will differ on an individual basis for each local authority for accounting purposes and certainly for individual tenancies. The descriptions and analysis have been undertaken to assess the relevant accounting treatment. They offer no commentary on the security of these tenancies for any other purpose.**

4. In order to undertake the assessments, it has been necessary to use average or estimated information as the relevant information is not collected or available. To assist with this a sample of 40 local authorities in England was used to ascertain the useful life of council dwellings and to gain an estimate of fair or market value.

5. The adoption of IFRS 16 has been delayed to 2022/23 financial year. However, Appendix F of the 2020/21 Code of Practice includes CIPFA/LASAAC's agreed provisions to date. References to the Code below are therefore to the agreed provisions in Appendix F of the 2020/21 Code.

6. Annex A to this Technical Appendix considers whether the secure housing tenancies meet the definition of a lease under IAS 17 *Leases* and IFRIC 4 *Determining whether an Arrangement Contains a Lease*. This assessment has been made to ensure that the accounting position is correct for current editions of the Code and to ensure that the starting position for the transition to IFRS 16 is clear.

Section B: Is the secure tenancy for tenants within local housing authorities a lease for accounting purposes?

7. Secure tenancies are not legally leases. However, IFRS 16 has a clear process for identifying whether an arrangement is or contains a lease for accounting purposes irrespective of its legal status. A lease is defined in IFRS 16 as:

‘*A contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration*.’

8. Local authorities use assets not just for the economic benefits that may be obtained from their use but also for their ability to support services so paragraph 4.2.2.36 of Appendix F adds the concept of ‘service potential’ to the IFRS 16 decision making process for the identification of a lease. Service potential is described in the IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (IPSASB 2014) as the capacity to provide services that contribute to achieving the entity’s objectives.

9. Therefore, to assess whether a contract conveys the right to control the use of an identified asset for a period of time, a local authority is required to assess whether, throughout the period of use, the customer has both of the following:

- the right to obtain substantially all of the economic benefits and/or *service potential* from use of the identified asset; and

- the right to direct the use of the identified asset.

10. IFRS 16 sets out steps to assess whether a contract is or contains a lease (summarised in the flow chart at paragraph B31). The relevant questions from this flow chart as they would apply to secure housing tenancies are considered in the table below. The flow chart is included in the Annex B to the Technical Appendix.

Table 1: Questions to Consider for the IFRS 16 Identification of the Lease

Questions	Considerations/Response
Is there a contract? (See paragraph B13 of IFRS 16)	**Yes**, the secure tenancy is agreed and a contract for the tenancy exists between the authority as landlord and the tenant as customer.
Is there an identified asset? (See paragraph B13 of IFRS 16)	**Yes**, the agreement specifies the property (the council dwelling) in which the tenant will live and therefore identifies the asset in question.
Will the customer have the right (throughout the period of use) to obtain substantially all of the economic benefits and/or service potential from use of the asset? (See paragraph B21 to B23 of IFRS 16)	**There is a transfer of economic benefits to the customer.** The customer (tenant) uses the property and therefore consumes the value (economic benefits) inherent in the building during the contract period.

Questions	**Considerations/Response**
	There is not complete freedom of use: • tenants are not free from eviction as certain conditions exist such as paying rent and service costs on time • social behaviour is considered and must be maintained for the tenant to continue to live in the property. *(These conditions are more likely to be protective rights for the authority to maintain the value of the property, rather than restrictions over the customer's consumption of its value).* Tenancies are unusual when being considered as leasing arrangements in that the tenant's objective is solely to occupy the property, not to make returns from the use of property unlike that of a business that would use an asset to make returns from the production or supply of goods and services. The authority is the only party receiving cash flows. Section 93 of the Housing Act 1985 allows tenants some functions of subletting ie tenants are able to take lodgers but section 93 2) does not allow tenants to sublet the whole of the dwelling house (where this is the case this is no longer a secure tenancy. (*This provides an indication that the tenant during the period of can make gains and therefore obtains some economic benefits in the asset*). However, economic benefits are being consumed during the tenancy as is evidenced by depreciation of the property. The gains from consumption fall wholly to the tenant. During the period of use the authority is the only user of the service potential in the asset (to house local authority housing tenants). But this service potential is consumed at the point the tenancy is awarded.

Questions	Considerations/Response
	During the period of use the tenant has exclusive use of the asset and therefore will consume the value of the asset in that period.
Does the customer have the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions? (see paragraph B24 of IFRS 16)	The legal framework allows the customer (the tenant) to operate the asset as a tenant and within the scope of the tenancy, without the local authority having rights to change its use. The tenant also generally has the right to direct the use of the underlying property because the tenant decides how and for what purpose the property will be used. There are limitations on what the tenant can do in terms of social behaviour or adaptations to the property, but these are more likely to be protective rights for the authority to maintain the value of the property. So, although there are restrictions and limitations on the use of the property the tenant largely has the right allowing for fair use to use the property and direct its use.
Did the customer design the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use? Consider paragraph B24(b)(ii) of IFRS 16.	N/A, as previous question answered positively.

Conclusion

The table above confirms that it is likely that during the period of the lease:

- the tenant has the right to obtain substantially all of the economic benefits and service potential from use of the council dwelling
- the tenant has the right to direct the use of the council dwelling; and.
- the authority benefits from the service potential in the asset but this is used at the point the tenancy is granted.

Therefore, a secure tenancy is likely to be a lease.

Period of Time

11. The definition of a lease requires the 'right-of-use' to be conveyed for a period of time. It appears that a tenancy has no specified end point, so a question arises whether there is no defined period of time and taking the tenancy outside the scope of IFRS 16. Alternatively, the period of time could be argued to be the 4-week notice period which is constantly renewed.

Other commentary

12. Paragraph 10.3 of the *Housing SORP: 2018 Update Statement of Recommended Practice for Registered Social Housing Providers* (the Housing SORP) considers standard rental agreements for tenanted social housing properties to be operating leases, based on the requirements of FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*. Annex C to this Technical Appendix includes an extract from the Housing SORP.

General Conclusion

13. Most indicators appear to lead to the conclusion that secure housing tenancies in substance are leases.

Section C: If the secure housing tenancy meets the definition of a lease, is it a finance or an operating lease?

14. Paragraph 4.2.2.69 of Appendix F of the 2020/21 Code and IFRS 16 paragraph 62 establish that:

'*A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership of an underlying asset*.'

15. Generally, as established in table 1, economic benefits relate to changes in the value of the property or the ability to generate income. The risks and rewards assessment will focus on those relating to the council dwelling or any residential property ie in the value of the building and the ability to generate income. However, again as local authority assets are held not just for economic benefits but the service potential an authority can derive from the property being used must also be considered.

16. The following consider whether the risks and rewards of owning the council tenancy transfer to the tenant as a regard to the secure tenancy agreement:

- In providing social housing to the tenant the local authority is maximising the service potential in the asset ie it is providing the function it is intended to provide. Housing tenants benefit from the consumption of the asset.

- Local authorities benefit from any increases in the market value of the asset and in the receipt of housing rents from the tenant.

- The most substantial risks to owning the council dwelling lie in the risks relating to the value of the asset. Although housing tenants consume economic benefits during the period of use, the risks relating to any falls in value of the asset lie not with the tenant but with the local authority. The local authority is responsible for the maintenance and upkeep of the fabric of the building and the most substantial fixtures and fittings to maintain the value of the asset.

- Local authorities also lose some service potential while properties are held vacant or are damaged and are not habitable.

17. A more minor reward is that tenants may receive income if they have lodgers.

General Conclusion

18. The risks and rewards of owning the property lie substantially with the local authority.

Examples of Circumstances which Individually or in Combination Would Lead to A Lease Being Classified as a Finance Lease

19. In addition to the assessment of whether a lease transfers substantially all the risks and rewards incidental to ownership of an underlying asset the Code and IFRS 16 (paragraphs 4.2.2.71 and 63, respectively) include the following examples of situations where either individually or in combination a lease would be classified as a finance lease:

Table 2: Examples of situations where a lease would be classified as a finance lease for a local authority secure tenancy

A.	*The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.*
A.1	• This does not occur in a secure tenancy. The council dwelling remains under the ownership of the local authority. ***Conclusion: This example situation provides evidence of an operating lease.***
B.	*The lessee has the option to purchase the underlying asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception date, that the option will be exercised.*
B.1	• Except for the circumstances afforded by the Right-to-Buy provisions discussed in the next bullet local authority housing tenants do not have an option to purchase the council dwelling. • Right-to-Buy in England is provided under section 118 of the Housing Act 1985. It does not arise directly from the contract (and is therefore not a part of the definition of a lease which refers to a contract being in place) between the authority and tenant but as a result of the incidental impact of statute and needs to be considered outside IFRS 16, otherwise if the contractual arrangements caused by right-to-buy legislative provisions are considered: • Right-to-buy properties are discounted at less than their market value based on periods of tenancy though this discount has a

	ceiling. The discounted market value will be less than the fair value. • Tenants must have been in public housing for at least three years (in some cases two years) before they are allowed to participate in the right-to-buy scheme so for new tenants at the inception of the lease the right-to buy option is not applicable. Although there may be arguments that a right-to-buy option might arise under a secure tenancy an authority would need to be 'reasonably certain' that the tenant would at the inception of the lease take-up this option. • As at the inception of the lease the tenant has chosen to rent it is arguable that economically at the inception of the lease the tenant cannot afford to choose a different option for housing. • Any other assessments would require the council to be reasonably certain that each tenant expects to exercise the option. At the inception date it is not possible to make this assessment, but economic factors would suggest at the inception of the lease the tenant is not 'reasonably certain' to take up this option. • A local authority could assess how many tenants take up the right-to-buy option but this would only provide some indication of the probability of a tenant taking up a right-to-buy option and would not provide evidence that each tenant is on an individual basis 'reasonably certain' to take up the option. • It should also be noted that the Right-to-Buy provisions depend on the continuation of government policy which is outside the control of either party to the lease. ***Conclusion: This example situation provides evidence of an operating lease.***
C.	*The lease term is for the major part of the economic life of the underlying asset even if title is not transferred.*
C.1	• The lease term is defined in the Code and IFRS 16 as: '*The non-cancellable period for which a lessee has the right to use an underlying asset, together with both:* *a) periods covered by an option to extend the lease if the lessee is reasonably certain to exercise that option; and* *b) periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option.'* • Paragraph 4.2.2.42 b) of the Code (and 18 (b) of IFRS 16) establishes that the lease term is the point up to which it remains 'reasonably certain' that the option will not be exercised. The agreement allows tenants to live in the property for the rest of their lives provided that they do not break the conditions of the tenancy agreement. The tenancy may end the agreement at any point by giving the authority 28 days-notice. So, for housing tenancies we

	would interpret this as the period during which it is not reasonably conceivable that the tenant as lessee could end their agreement. • The question is therefore whether the lease terms is set as a sufficiently long enough period that will allow the transfer of substantially all the risks and rewards incidental to ownership of the underlying asset (paragraph 4.2.2.69 of the Code, paragraph 62 of IFRS 16). • An assessment would be made that the lease term would need to be at least x number of years to meet the definition of a finance lease ie the major part of the economic life of the asset (for this assessment we will assume a minimum 25 years) or for long enough so that the present value of the lease payments represents the fair value of the underlying asset (at this juncture assume this would be the same period though it may be substantially longer). • To ascertain the length of the lease term the lessor would need to consider all relevant facts and circumstances that create an economic incentive for the tenant (the lessee) not to exercise the option before those 25 years. Therefore, the following needs to be considered in accordance with paragraph B37 of IFRS 16. – **Contractual terms and conditions for the optional periods compared with market rates** - this factor might be more relevant as social housing rents are usually below market rates, but it would be difficult to argue that such low rents would mean that tenants would be reasonably certain not to end the tenancy solely because of this. It is arguable, for example, that a local authority tenant could move to a rental property from a social housing landlord. – **Significant leasehold improvements undertaken (or expected to be undertaken) over the term of the contract that are expected to have significant economic benefit for the lessee** – this is not likely to be a significant factor. Local authorities will maintain the fabric of the building, but tenants are required to maintain the condition of the property. It is understood that there are restrictions on the tenant's ability to substantially adapt or modify the property and therefore limitations on their ability to make significant leasehold improvements. – **The importance of that underlying asset to the lessee's operations** – this factor does not apply. – **Conditionality associated with exercising the option** – As there are no conditions which must exist or be met for a tenant to end their agreement, this condition is not relevant this factor does not apply. – Paragraph B40 of IFRS 16 sets out that: *'a lessee's past practice regarding the period over which it has typically used particular types of assets (whether leased or owned), and its economic reasons for doing so, may provide*

	information that is helpful in assessing whether the lessee is reasonably certain to exercise, or not to exercise, an option'. As local authorities will only have minimal information about previous tenancies with other landlords (ie information collected through pre-tenancy reference checks) an authority might be able to consider that a tenant has already rented the property for 5 years but will not be able to argue with any reasonable certainty that an individual tenant will be locked into the tenancy for the following 20 years or even 10. Historical information on other tenants would not be relevant (even if there is evidence that some tenants will stay in the tenancies for long periods). • The sub-group considered that it would not only consider the 'reasonably certain' test but would also consider whether it was probably the case that the lease term is a major part of the economic life of the asset. • Investigations with stakeholders have indicated that generally local authorities do not keep information on the length of secure tenancies. Government statistical information[1] indicates that for 2018/19 total lets as a percentage of local authority stock at year end (stock turnover) is 6.7%. So, a crude assessment of tenancies across England based on the stock turnover of 6.7% would indicate that the average length of all tenancies is 15 years. This also agrees with the average length of a secure tenancy based on CIPFA/LASAAC's feedback from an earlier investigation where one authority was able to establish the length of secure tenancies at 15 years. An alternative source (the English Housing Survey[2]) based on a sample of 1,432 renting households in England in 2018/19 shows that 24 percent of households had lived in their home for 20 years or more, indicating that roughly 76 percent had lived in their homes for less than 20 years. Although economic life information is not available, a further sample of 40 local housing authorities in England (note that this sample is statistically significant) showed a varying range of useful lives. Local authorities normally presented a lower and upper range of useful lives including those used for componentisation so the average upper limit for useful lives was 53 years with the lower rate being 23 years. The lower rate is likely to include housing components such as kitchens etc. Based on the average length of a tenancy of 15 years and the useful lives from the sample (and not economic life) it would appear that the length of the lease is not for the 'major part' of the tenancy agreement. ***Conclusion: This example situation provides evidence of an operating lease.***
D.	*At the inception date, the present value of the lease payments amounts to at least substantially all of the fair value of the underlying asset.*

[1] Local Authority Housing Statistics, or it predecessors, Housing Strategy Statistical Appendix (HSSA) and the Housing Investment Programme (HIP) returns.

[2] Initial findings from the English Housing Survey 2018 to 2019

D.1	• As the rent for social housing is below market rates it is unlikely at the inception date that the present value of the lease payments amounts to at least substantially all of the fair value of the underlying asset (see calculations below). *Present value of lease payments test against the fair value of the underlying assets* Average local authority social rent in England was £85.97 per week[3] in 2018/19. Assume an average lease terms of 15 years (based on total local authority stock turnover information of 6.7% see C.1) assuming with no CPI or other increase in rent and based on a PWLB fixed rate annuity of 2.12% (15 year rate) the present value of the lease payments is £62.4k. Local authorities in England do not hold information on market rates in their financial statements. However, the closest estimate of market or fair value would be the undiscounted current value in their financial statements ie removing the discount factor set by government. Using the same sample of 40 authorities average undiscounted value of is £179.1k. Therefore at the inception date the present value of the lease payments does not represent substantially all of the fair value of the underlying asset. • There is no definition of "substantially all". Practitioners might set a relatively high indicative percentage below which positive support for a finance lease from other situations or indicators will be required. However, as this albeit crude assessment is below 50% and is in fact just over a third of the value this has been assessed as an operating lease. ***Conclusion: This example situation provides evidence of an operating lease.***
E.	*The underlying asset is of such a specialised nature that only the lessee can use it without major modifications.*
E.1	• Council dwellings are not typically specialised so that they cannot be used by the prospective tenants. Some houses will have adaptations for those tenants with specific needs. However, it is considered in most cases that these can be removed. ***Conclusion: This example situation provides evidence of an operating lease.***

General Conclusion

20. The example situations specified by the Code and IFRS 16 do not provide evidence that housing tenancies are finance leases and therefore **the conclusion is that secure tenancies are operating leases**.

[3] Local Government Housing Statistics Table 702 Local authority average weekly (social and affordable) rents, by district, England 1998-99 to 2018-19

21. Paragraph 4.2.2.72 of the Code and paragraph 64 of IFRS 16 have a further set of indicators to of situations that individually or in combination could also lead to a lease being classified as a finance lease.

Table 3: Indicators of situations that could lead to a lease being classified as a finance lease

Indicators of situations that could lead to a lease being classified as a finance lease	Local authority housing tenancy agreement
If the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee.	• If a tenant cancels the tenancy there are no losses borne by the tenant. • The only costs which might be borne by the tenant would be those that might be required to reinstate the condition of the property. These costs are not related to the cancellation.
Gains or losses from the fluctuation in the fair value of the residual accrue to the lessee.	• Any gains or losses from changes in the fair value of the council dwelling do not accrue to the tenant. Changes in the fair value of the property have no direct impact on the rent for social housing.
The lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.	• If the assumption is made that anything beyond the first 28-day period of a tenancy is a secondary period, the secondary period rent will not be substantially lower than the preceding period. • There are no secondary periods which could involve rent reductions.

22. None of the secondary indicators therefore give rise to the consideration that council dwelling contractual arrangements are finance leases.

General Conclusion

23. **On examination of the secondary indicators secure housing tenancy agreements are in substance operating leases**.

Overall Conclusion

24. **When taking into consideration all three assessments secure housing tenancies can be considered in substance to be operating leases**.

Section D: Dependent on the classification decided on in section C what disclosure requirements will be needed by the users of local authority financial information relating to housing tenancies and the related assets?

25. Annex D to this Technical Appendix includes an extract of the reporting requirements for operating leases under the Code's adoption of IFRS 16.

26. The main disclosures include:

- lease income, separately disclosing income relating to variable lease payments that do not depend on an index or a rate
- how the lessor manages the risk associated with any rights it retains in underlying assets. A lessor is required to disclose its risk management strategy for the rights it retains in underlying assets, including any means by which the lessor reduces that risk, and
- a maturity analysis of lease payments showing the undiscounted lease payments to be received on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years.

Lease income, separately disclosing income relating to variable lease payments that do not depend on an index or a rate

27. The lease income disclosure is required by paragraph 4.2.4.13 b) of the provisions included in Appendix F of the Code. This information is covered by the presentation of the housing income streams on the face of the HRA Income and Expenditure Statement which gives this information substantial profile in local authority accounts and no further information is required as this would lead to duplication.

Information on the nature of the authority's leasing activities and the risks it retains in the underlying assets

28. Paragraph 4.2.4.15 requires that local authorities report on the nature of their leasing activities and provide information that helps users assess how it manages the risk associated with any rights it retains in the underlying assets. It sets out that the lessor is required to disclose its risk management strategy for the rights it retains in underlying assets, including any means by which the lessor reduces that risk. The nature of local authorities' leasing activities is provided in the narrative description on the Housing Revenue Account Income and Expenditure Statement. In England local authorities are required by The Housing Revenue Account (Accounting Practices) Directions 2016 to provide detailed disclosures on Housing Revenue Account housing stock. These disclosures are not directly related to the risks associated with the rights it retains in the council dwellings (e.g. freehold ownership), but they allow for monitoring movements in the housing stock and consideration of the state of these assets.

29. The examples in IFRS 16 and the Code suggest that this disclosure may include a commentary on residual value guarantees (the other examples of means by which a lessor may reduce the risks associated with the rights it retains are not considered relevant to council dwellings stock). The guarantees mitigate against

the risk that the underlying asset may sell for an amount lower than anticipated. In order to maximise their service potential, it will be the objective of local authorities to keep letting council dwellings to new tenants. As there is no intention to realise the residual values of these assets, this disclosure is not deemed to be relevant to the management of local authority housing stock.

30. It might be argued that that there are risks to the rights that a local authority retains in the underlying asset from the Right-to-Buy scheme. However, evidence from initial investigations indicate that this is an increasingly low percentage of a local authority's housing stock and this is therefore not likely to be a material risk. This is supported by information shown by the 'heat' map which demonstrates across England that RTB sales which are over 1% per 1000 dwellings in a local authority area has a relatively low incidence. See heat map for English authorities reproduced in Annex E.

31. It is arguable that the disclosures provided when this requirement is applied to Housing Tenancies are not useful to users. Providing this information has the potential to clutter the notes to the HRA account. **Therefore, it is recommended that it is not included in the specifications for disclosures for local authority council dwellings tenancies**

Maturity analysis of lease payments

32. Paragraph 4.2.4.20 requires that local authorities present the undiscounted lease payments to be received on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years.

33. As the secure housing tenancy agreement cannot ensure lease payments for anything longer than the following four week period and possibly for some tenancies for less than this as they may have been ended or subject to default it is likely to be difficult for accounts preparers to provide any maturity analysis of guaranteed payments and certainly this information would not be available for greater than one year. The objective of the IFRS 16 disclosures on leases is to enable users to more accurately forecast future lease cash flows and estimate liquidity risk). This is not considered particularly relevant in the context of housing tenancies, and not relevant enough to justify introducing an additional disclosure (given the current information already included in the notes to the HRA account).

34. In FRS 102 *The Financial Reporting Standard Applicable in the UK and Republic of Ireland,* on which the provisions of the Housing SORP are based, paragraph 20.30 includes the requirements for a similar disclosure though it does this for non-cancellable leases and also includes a requirement to disclose contingent rents. CIPFA/LASAAC has considered a sample of ten registered social landlords. Only one disclosed information on a maturity analysis and one had taken the decision that its tenancy agreements are not leases though this was reporting under IFRS 16.

35. Lease information might not have been included for RSLs because FRS 102 refers to 'non-cancellable' operating leases. This distinction is not made in IFRS 16 but is included in IAS 17 *Leases* as adopted by the 2020/21 Code and earlier editions of the Code.

36. The presentation of rental information for a four-week period is unlikely to be useful to the users of local authority financial statements. **It is recommended that this is not included as a requirement for local authorities to avoid raising the expectation that the disclosure would need to be provided and avoid adding clutter to local authority financial statements.**

ANNEXES

ANNEX A. CONSIDERATION OF WHETHER HOUSING TENANCIES ARE LEASES UNDER IAS 17 LEASES AND IFRIC 4 DETERMINING WHETHER AN ARRANGEMENT CONTAINS A LEASE

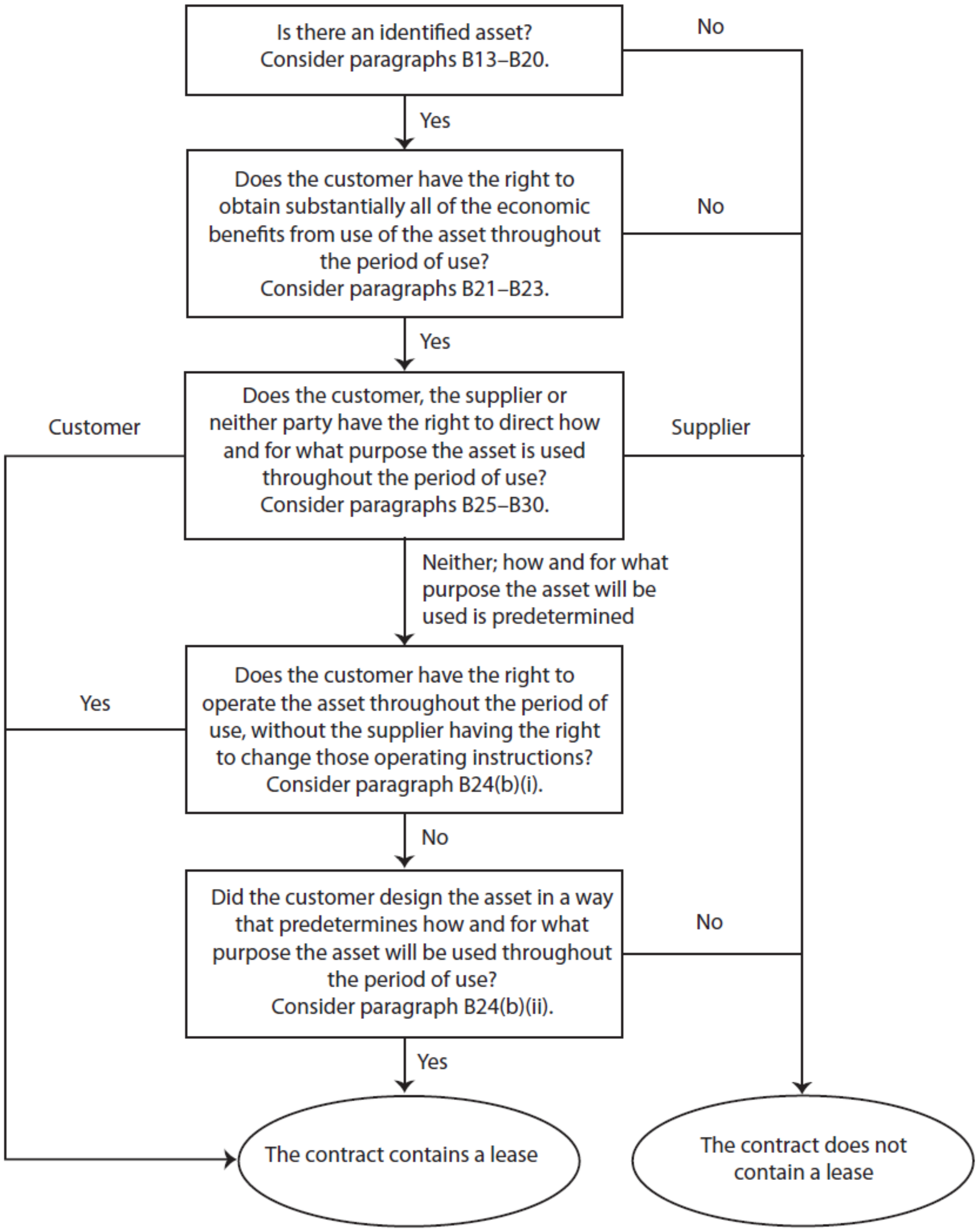
A.1 The Code and IAS 17 *Leases* defines a lease as an:

'*agreement whereby a lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time*.'

A.2 As discussed in the Technical Appendix the tenancy agreement for secure tenancies is an agreement and the local authority receives payments from the tenant. However, other than for fixed term tenancies it is less clear whether the tenancy is for an 'agreed period of time' ie a term with a fixed start date and end dates agreed between the two parties. With secured tenancies, the agreements allow tenants to live in the property for the rest of their lives provides that they do not break the conditions of the tenancy agreement and have rights to pass the tenancy agreement on to close family members. It is arguable therefore that secure tenancies do not meet the definition of a lease. Some flexible tenancies are offered for a fixed term, but most council tenancies are secure tenancies.

A.3 IFRIC 4 *Determining Whether an Arrangement Contains a Lease* provides guidance on how to determine whether an arrangement which doesn't take the legal form of a lease is, or contains, a lease as defined in IAS 17. As the secure tenancy agreements don't meet the definition of a lease in IAS 17, IFRIC 4 does not apply.

ANNEX B. EXTRACT FROM IFRS 16 LEASES OF THE FLOW CHART TO ASSIST ENTITIES IN MAKING THEIR ASSESSMENT ON WHETHER A CONTRACT IS OR CONTAINS A LEASE



ANNEX C. EXTRACT OF HOUSING SORP: 2018 UPDATE STATEMENT OF RECOMMENDED PRACTICE FOR REGISTERED SOCIAL HOUSING PROVIDERS PROVISIONS ON RENTAL AGREEMENTS

‘10.3 This SORP considers that standard rental agreements for tenanted social housing properties, such as general needs properties, and most relationships between social landlords who own properties but allow other charitable or social landlords to use them for particular purposes, to be operating leases as defined in Section 20 of FRS 102, Leases. Paragraphs 20.24 to 20.31 of FRS 102 set out the accounting and disclosure requirements for operating leases, and in applying these paragraphs to rental agreements for tenanted social housing properties, a social landlord must:

- include the housing properties in the statement of financial position based on the nature of the asset as set out in Section 8 of this SORP, *Housing properties*
- recognise the rental income from the lease arrangements as income in the Statement of Comprehensive Income on a straight-line basis (unless the points highlighted at 20.25 (a) and 20.25 (b) of FRS 102 are considered relevant)
- recognise as expenditure in the Statement of Comprehensive Income any costs incurred in earning the lease income, for example depreciation and maintenance costs.

10.4 A social landlord must include the following disclosures in the financial statements in accordance with paragraph 20.30 of FRS 102:

(a) The future minimum lease payments under non-cancellable operating leases for each of the following periods:

(i) not later than one year

(ii) later than one year and not later than five years

(iii) later than five years

(b) total contingent rents recognised as income

(c) a general description of the significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, and restrictions imposed by lease arrangements.’

ANNEX D. EXTRACT FROM APPENDIX F OF THE 2020/21 CODE ON OPERATING LEASE DISCLOSURES FOR LESSORS

Lessor disclosures

4.2.4.12 The objective of the disclosures is for lessors to disclose information in the notes that, together with the information provided in the Balance Sheet, Comprehensive Income and Expenditure Statement and Cash Flow Statement, gives 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 lessor.

4.2.4.13 A lessor shall disclose the following amounts for the reporting period:

a) for finance leases:

   i) selling profit or loss

   ii) finance income on the net investment in the lease, and

   iii) income relating to variable lease payments not included in the measurement of the net investment in the lease

b) for operating leases, lease income, separately disclosing income relating to variable lease payments that do not depend on an index or a rate.

4.2.4.14 A lessor shall provide the disclosures specified in paragraph 4.2.4.13 in a tabular format, unless another format is more appropriate.

4.2.4.15 A lessor shall disclose additional qualitative and quantitative information about its leasing activities necessary to meet the disclosure objective in paragraph 4.2.4.12. This additional information includes, but is not limited to, information that helps users of financial statements to assess:

a) the nature of the lessor's leasing activities, and:

b) how the lessor manages the risk associated with any rights it retains in underlying assets. In particular, a lessor shall disclose its risk management strategy for the rights it retains in underlying assets, including any means by which the lessor reduces that risk. Such means may include, for example, buy-back agreements, residual value guarantees or variable lease payments for use in excess of specified limits.

…

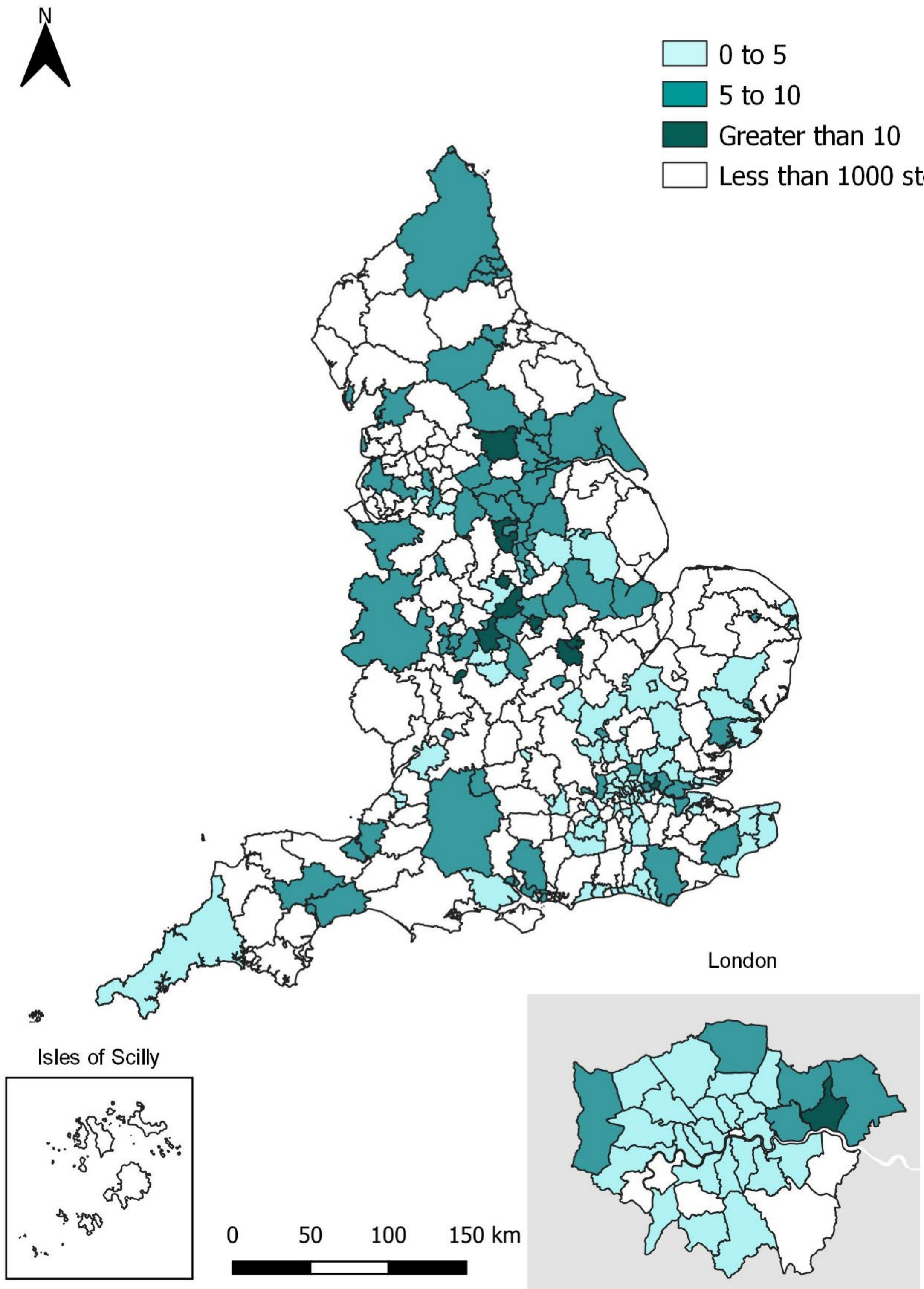
Operating leases

4.2.4.18 For items of property, plant and equipment subject to an operating lease, a lessor shall apply the disclosure requirements of Section 4.1. In applying the disclosure requirements in Section 4.1, a lessor shall disaggregate each class of property, plant and equipment into assets subject to operating leases and assets not subject to operating leases. Accordingly, a lessor shall provide the disclosures required by IAS 16 for assets subject to an operating lease (by class of underlying asset) separately from owned assets held and used by the lessor.

4.2.4.19 A lessor shall apply the disclosure requirements in Section 4.4 (Investment Property), Section 4.5 (Intangible Assets) and Section 4.7 (Impairment of Assets) for assets subject to operating leases.

4.2.4.20 A lessor shall disclose a maturity analysis of lease payments, showing the undiscounted lease payments to be received on an annual basis for a minimum of each of the first five years and a total of the amounts for the remaining years.

ANNEX E: LOCAL AUTHORITY RIGHT TO BUY SALES PER 1000 DWELLINGS OF EXISTING LOCAL AUTHORITY HOUSING STOCK, IN ENGLAND, YEAR ENDING JUNE 2020



The non-stock holding authorities have transferred all their stock to Private Registered Providers and are shown as white on the map above.

Source: Right to Buy Sales in England: Statistical Release January to June 2020

4.2 LEASES

4.2.1 Introduction

4.2.1.1 Authorities shall account for leases in accordance with IFRS 16 *Leases*, except where adaptations to fit the public sector are detailed in the Code. IPSAS 13 *Leases* is based on IAS 17 *Leases* (and does not adopt IFRS 16) and should only be considered for additional guidance where it does not contradict the provisions of IFRS 16. Transport for London is permitted, but not required, to apply the Code requirements relating to IFRS 16implementation for the 2019/20 and 2020/21 financial years with a date of initial application of 1 April 2019. Early application by other local authorities is not permitted. It is anticipated that the standard will have a date of initial application of 1 April 2021

4.2.1.2 This section of the Code shall be applied in accounting for all leases except licences of intellectual property granted by a lessor within the scope of Section 2.7 and IFRS 15 *Revenue from Contracts with Customer*s, service concession arrangements within the scope of Section 4.3 of the Code and IFRIC 12 *Service Concession Arrangements*, and rights held by a lessee under licensing agreements within the scope of Section 4.5 of the Code and IAS 38 *Intangible Assets*. Leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources and of biological assets within the scope of IAS 41 *Agriculture* are also excluded from the scope of this section of the Code, however these are unlikely to apply to local authorities.

4.2.1.3 A lessee may but is not required to apply this section of the Code to leases of intangible assets other than those described in paragraph 4.2.1.2. Leases relating to heritage assets are accounted for in accordance with this section of the Code subject to the specific requirements of Section 4.10 (Heritage Assets).

Adaptation for the public sector context

4.2.1.4 The following adaptations of IFRS 16 apply:

Scope

- The Code adapts IFRS 16 to remove the phrase “in exchange for consideration” from the definition of a lease. All other IFRS 16 *Leases* requirements for lease identification apply.
- ~~The Code adapts IFRS 16 *Leases* to remove Housing Revenue Account tenancy agreements from the requirements of IFRS 16 *Leases*.~~

Interpretation for the public sector context

4.2.1.5 For transition arrangements the Code applies the following interpretations:

- Authorities shall not reassess whether a contract is or contains a lease at the date of initial application, except for leases for nil consideration
- For lessee arrangements transition will be undertaken to restate balances at the date of initial application for the cumulative effect of initial application. The option to retrospectively restate prior period comparative information is not permitted.
- For lessee arrangements the option to make adjustments on transition where the underlying asset is of low value is not permitted.
- For lessee arrangements the option to make adjustments on transition for leases where the lease term ends within 12 months is not permitted.

- For lessees, nil consideration leases are required to be identified with measurement of the right-of-use asset required, and a gain on transition recognised where applicable.
- For lessors, nil consideration finance leases are required to be identified, with the asset provided to the third party required to be derecognised, and any unguaranteed residual value recognised, where applicable.

The following interpretations of IFRS 16 apply in accounting for leases and lease type arrangements after transition to IFRS 16 *Leases*:

- The Code interprets IFRS 16 to require local authorities to apply the recognition exemption to short-term leases (see paragraph 4.2.2.32).
- The Code interprets IFRS 16 to specify in more detail the accounting requirements for leases at peppercorn or nominal lease payments, or for nil consideration by following the principles in the Code for the treatment of donated assets.
- The Code interprets IFRS 16 to require that the subsequent measurement of the right- of-use asset where the underlying asset is an item of property, plant and equipment is measured in accordance with Section 4.1 of the Code (see paragraph 4.2.2.53). This includes the use of the cost model in IFRS 16 as a proxy for current value for most right- of-use assets.
- The Code interprets IFRS 16 so that housing tenancies are deemed to be operating leases which shall be accounted for under this section of the Code. CIPFA LASAAC has also considered the disclosure requirements for operating leases as lessors. The Board is of the view that this information is either already provided on the face of the Housing Revenue Account Income and Expenditure Statement or is not relevant for housing tenancies and therefore confirms that operating leases disclosures for lessor's shall not apply.