



# IFRS 16 *Leases*

## Exposure draft 18(01)

### Who are we

The Healthcare Financial Management Association (HFMA) is the representative body for finance staff in healthcare. For the past 60 years, it has provided independent and objective advice to its members and the wider healthcare community. We are a charitable organisation that promotes best practice and innovation in financial management and governance across the UK health economy through our local and national networks. We also analyse and respond to national policy and aim to exert influence in shaping the wider healthcare agenda. We have a particular interest in promoting the highest professional standards in financial management and governance and are keen to work with other organisations to promote approaches that really are ‘fit for purpose’ and effective.

### Question 1:

**Do you agree with the adaptation for the definition of a contract? If so why? If not, why not and what alternatives do you propose?**

Yes, we agree that the definition should be extended to include intra-government agreements. Adopting a different accounting treatment for such arrangements would not be best practice and would result in a lack of comparability.

However, our members are concerned that this adaptation will result in additional work for them as intra-government arrangements tend not to be as well documented as commercial contracts. Also, intra-NHS arrangements will need to be consolidated out at the group level which will add additional pressure to the year-end timetable.

### Question 2:

**Do you agree with the public sector interpretation for short term leases? If so, why? If not, why not and what alternatives do you propose?**

Yes we agree with this interpretation.

### Question 3:

**Do you agree with the proposals for low value leases? If so why? If not, why not and what alternatives do you propose?**

Yes, we agree with this proposal. However, additional guidance may be needed to explain the difference between the capitalisation threshold of £5,000 which is mandated in the NHS and the proposal for low value leases which is left to each organisation's discretion.

**Question 4:**

**Do you agree HM Treasury should set an internal rate of borrowing centrally, for entities to use when they cannot obtain the rate implicit in the lease? If so why? If not, why not and what alternative do you propose?**

We understand that in the corporate sector, which is probably more advanced in its thinking about the adoption of IFRS 16, this is one of the key areas of difficulty. Members would therefore welcome the availability of an HM Treasury set rate which can be used when the rate implicit in the lease is not available.

Our only concern would be that these HM Treasury set rates would need to be available on a timely basis – at the start of the financial year if the rate is to be updated/ reviewed annually. Currently, HM Treasury set interest rates for discounting provisions are published relatively late in the financial year (usually January for the following March year-end). This sometimes causes difficulty for NHS bodies as they have to manage the financial impact of changes in rates at a late stage in the financial year.

For leases, the rate would be needed to make the necessary calculations as the business case for a new asset is being developed (assuming leasing is one of the financing options available) as well as when the lease is signed.

**Question 5:**

**Do you agree that the internal rate of borrowing should be set irrespective of the type of underlying asset? If so why? If not, why not and what alternatives do you propose?**

This seems to be a sensible proposal.

**Question 6:**

**How would you undertake revaluations of right of use assets under IFRS 16? Please provide explanations based on both property and non-property assets.**

We do not have a view on how these revaluations should be undertaken.

However, we would say that the process of revaluation should be as straight forward as possible. Valuation of non-current assets is one of the main area of judgement in NHS accounts and the cost of engaging professional valuers as well as the time taken by finance teams and auditors is not insubstantial.

**Question 7:**

**What valuation methodology do you believe HM Treasury should mandate for the public sector and why? Does your answer change depending on the asset type? If so why? If not, why not?**

Other than the practicality issue raised above, we have no comment to make.

### Question 8:

**Do you agree with the public sector adaptation for peppercorn leases? If so why? If not, why not and what alternatives do you propose?**

We have no comment to make.

### Question 9:

**Are there any disclosure requirements for lessee accounting which you believe are not applicable to the public sector? If so why and what alternatives do you propose? If not, why not?**

See our response to question 6.

### Question 10:

**Do you agree with the proposals for lessor accounting? If so why? If not, why not and what alternative do you propose?**

We agree with the proposals for lessor accounting. However, our members are concerned with the following issues in relation to intra-NHS leases and the impact of the different accounting treatments adopted by lessors and lessees:

- the impact on clinical commissioning groups, and some provider bodies, of the application of this standard to the leases/ arrangements they have with NHS Property Services Ltd. Members tell us that they struggle to agree current arrangements with NHS Property Services Ltd and, in many cases, there is no written lease in place. The lack of documentation is going to make the adoption of IFRS 16 very difficult.
- the impact on the DHSC group consolidation as intra-NHS leases will need to be identified and consolidated out of the group accounts. Members would welcome early sight of the information that they will be required to submit to NHS England and NHS Improvement in order to plan for the year-end

### Question 11:

**Are there any disclosure requirements for lessor accounting which you believe are not applicable to the public sector? If so why and what alternatives do you propose? If not, why not?**

We do not believe that there are any disclosure requirements which are not applicable to the public sector. As the exposure draft emphasises it will be important for the preparers of accounts to consider materiality when preparing the lease disclosures.

### Question 12:

**Do you agree no adaptations or interpretations for the public-sector context is required for sale and leaseback? If so why? If not, why not and what alternatives do you propose?**

We have no comment to make.

### Question 13:



**Do you agree with the public-sector interpretation on grandfathering existing lease classifications? If so why? If not, why not and what alternatives do you propose?**

We agree that the adoption of the option to grandfather contracts should be mandatory.

Under IAS 17 and IFRIC 4, the accounting for a service contract and an operating lease was more or less the same (albeit with different disclosure requirements). This means that some contracts were not assessed under IAS 17 and IFRIC 4 so are not currently classified as containing a lease possibly incorrectly. In our recent year-end survey, only twenty-five (31% of respondents) were satisfied that all of their contracts which involve the use of an asset have been assessed under IAS 17 and IFRIC 4.

Our members have raised questions about how those arrangements should be treated under IFRS 16 and whether the grandfathering arrangements can still apply. Some guidance would therefore be welcomed.

**Question 14:**

**Do you agree with the transition approach for the proposed amendments? If so why? If not, why not and what alternatives do you propose?**

Yes, we agree with the transition approach.

**Question 15:**

**Do you agree with the public-sector interpretation for asset measurement upon transition? If so, why? If not, why not and what alternatives do you propose?**

Yes.

**Question 16:**

**Do you agree with the public sector interpretation on practical expedients when applying IFRS 16 upon transition? If so why? If not, why not and what alternatives do you propose?**

Yes.

**Question 17:**

**Do you agree with the transition proposals for lessee accounting and disclosures? If so why, if not why not and what alternatives do you propose?**

Yes.

**Question 18:**

**Do you agree with the transition proposal for lessor accounting? If so why, if not why not and what alternatives do you propose?**

Yes.

**Question 19:**



**Do you have any comments on the impacts IFRS 16 will have on consolidation? Please explain any comments, including providing alternatives HM Treasury should consider.**

See our response to question 10.

### **Question 20:**

**Do you agree with the proposals for aligning the accounting of service concession arrangements that contain a lease with IFRS 16? If so why? If not why not, and what alternatives do you propose?**

We have no comment to make.

### **Question 21:**

**Do you agree with the proposed effective date for the public-sector implementation of IFRS 16? If so why? If not, why not and what alternatives do you propose?**

In our year-end survey of NHS bodies, IFRS 16 is the top issue that our members would like to see more guidance on. This is confirmed by members at meetings, where they have asked for training sessions on the new lease accounting standard. Many members are waiting for additional guidance on the application of the standard to the public sector.

Only two respondents to the survey indicated that they are ready for the implementation of the standard.

51% of the eighty-two NHS bodies that responded to a question about lease registers confirmed that have a lease register in place and only twenty-seven NHS bodies stated that it was comprehensive and up to date.

It is therefore fair to say that it will take a lot of hard work to be ready to adopt this standard from 1 April 2019.

The key question that our members are asking is what impact the adoption of IFRS 16 will have on capital funding and capital allocations. We are aware that some NHS bodies changing their existing practices to move away from using operating leases to purchasing assets. We think that this is the critical issue which needs to be resolved before the standard can be adopted in the public sector. If it has not been resolved by autumn 2018, then we would urge that the adoption of the standard is deferred for a year so that bodies can assess the impact on their capital programmes.

### **Question 22:**

**Are there any other areas not covered by the questions which you would like to comment on? Please explain any comments, including providing alternatives HM Treasury should consider.**

As indicated in our response to question 21, our members are particularly concerned about the impact of this standard on capital funding and the measurement of performance against the capital departmental expenditure limit (CDEL). Some guidance on this would be welcomed.

Our members are also concerned about the data that will be needed for the national accounts. Those NHS bodies which are party to PFI agreements already maintain dual accounting records for those agreements. That is additional work but is not too onerous as such agreements are relatively

uncommon and the information needed for ESA 10 accounting was usually prepared as part of the business case anyway.

Dual accounting is not a practical solution for leases as there are too many of them and the work required to assess leases as operating or finance as well as the IFRS 16 requirements would be too onerous.

### Question 23:

**Are there any options available in IFRS 16 that your entity would be significantly concerned about adopting, were HM Treasury try to align with ESA 10? Please explain any comments, including providing alternatives HM Treasury should consider.**

As we indicated above, members are concerned about the work necessary to adopt this standard and some are waiting for guidance before they start. In the absence of any other guidance, the FRAB papers and this exposure draft are being used to start the analysis necessary to adopt IFRS 16 from 1 April 2019.

Our main concern would be that aligning with ESA 10 would mean that some of the transition arrangements would not be the ones which HM Treasury is currently favouring. The time to implement this standard is already short and any change to the adaptation and interpretation of the standard would cause additional work which may not be able to be completed on time.

We do not have any specific concerns about the options under IFRS 16 – although some are clearly more onerous to adopt than others. Our concern is that where an interpretation or approach is to be mandated, this should be made clear as soon as possible and not then subject to change.

### Contact

If you would like to discuss any of our comments in more detail please contact Debbie Paterson, policy and technical manager, [debbie.paterson@hfma.org.uk](mailto:debbie.paterson@hfma.org.uk).