

IFRS 16 Transition submission: guidance

Guidance to accompany form for submission on 28 October 2022

Issued: 30 September 2022

Introduction

IFRS 16 is effective for NHS bodies from 1 April 2022. For public sector bodies, the modified retrospective approach to transition, as set out in paragraphs C5(b) and C8 of the standard, is mandated. This means there will be no restatement of the prior year in accounts and the cumulative effect of initially applying the standard is taken to reserves.

This approach also brings additional disclosure requirements on transition as set out in paragraph C12 and C13 of the standard. This submission focuses on these disclosure requirements to help providers prepare for month 9 and month 12, together with additional transition information required for the elimination of intra-group leases upon national consolidation.

These disclosures will be repeated in month 9 and month 12 TAC schedules.

If you have queries in relation to the completion of this IFRS 16 transition template please contact england.provider.accounts@nhs.net.

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Submission

Completed templates should be submitted on provider portals no later than **Friday 28 October 2022 (noon)**. Please ensure all validation errors have been passed or discussed in advance with the provider accounts team using the contact details above. Please ensure the contact details provided on the cover of the template are for the most appropriate contact to assist with any queries we have.

Completion guidance

Input sheet – Lessees - transition

This sheet focuses on transition disclosures for lessees on 1 April 2022. Part (b) of C12 of IFRS 16 requires entities to disclose:

(b) an explanation of any difference between:

(i) operating lease commitments disclosed applying IAS 17 at the end of the annual reporting period immediately preceding the date of initial application, discounted using the incremental borrowing rate at the date of initial application [0.95% for public sector bodies]; and

(ii) lease liabilities recognised in the statement of financial position at the date of initial application.

Examples of this disclosure can be seen in the accounts of earlier adopters of IFRS 16. For reference, the 2019/20 accounts of the [Department for Digital, Culture, Media and Sport](#)¹ (page 134) and the [Department for Transport](#)² (page 245) are available on Gov.uk.

While the format of this disclosure for local accounts may be adapted, it is necessary to collect this information in a standardised format within the TAC forms for consolidation at a national level. The provider accounts template is also expected to follow this format to aid consistency.

Table 1 – Reconciliation of operating lease commitments at 31 March 2022 to lease liabilities under IFRS 16 at 1 April 2022

Liabilities under PFI schemes are not IFRS 16 lease liabilities so are not part of this disclosure.

Step 1 - Discounting the IAS 17 operating lease commitments:

The first section of this table (subcodes TRA0010 to TRA0050) deals with discounting the operating lease commitments disclosed under IAS 17 at 31 March 2022:

- Operating lease commitments from 2021/22 audited TACs have been pre-populated into TRA0010.

¹https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/949822/DCMS_Annual_Report_2019-20_Web_Accessible_20210105.pdf

²https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/936346/DfT-Annual-Report-and-Accounts-2019-20-web-accessible.pdf

- Some providers may have made an error in their counterparty analysis for this disclosure in 2021/22. TRA0030 allows providers to correct the counterparty analysis if required to ensure commitments and subsequent liabilities are disclosed against the right counterparty type. Any adjustments on this row are required to net to nil. This is not a prior period adjustments row – see step 2 below.
- These commitments should be discounted to present value locally using the HM Treasury published incremental borrowing rate of 0.95% and entered into TRA0050.

An update to the GAM will confirm that where absorption transfers happen on 1 April 2022, the absorption transfer should be recorded before IFRS 16 transition: this will mean divested and received book values will continue to agree.

Step 2: reconciling the discounted commitment to the lease liability after transition:

The next two sections are for providers to quantify the impact of differences between the discounted IAS 17 commitment and the post-transition lease liability. This includes removing items that would have been included in commitments but are not IFRS 16 liabilities as well as adding in additional amounts that are included in the liability but would not have been disclosed as a commitment under IAS 17.

- Providers are not expected to require all of these rows. We have sought to split out as many reconciling differences as possible to aid understanding and consolidation. Not all circumstances will apply locally.
- If your local circumstances give rise to a reconciling item not listed please contact england.provider.accounts@nhs.net so we can consider whether an additional row is required in the template (either by fixer or at month 9).
- **Please note** – as the opening commitment is discounted in step 1, these reconciling items will also need to be discounted for consistency. If this is not done, the disclosure will not cast.
- A row is included for adjusting the impact of immaterial errors in the 31 March IAS 17 commitments disclosure. Providers are not expected to restate prior year disclosures for immaterial errors therefore such amounts should be disclosed as reconciling items. If you have discovered a material error in your prior year operating lease commitments disclosure please email england.provider.accounts@nhs.net to discuss how best to proceed.

Existing IAS 17 finance leases are not amended on transition to IFRS 16. Where these include variable lease payments that vary in line with an index or rate that were previously not part of the lease liability under IAS 17, these will now fall within the lease liability under IFRS 16 but these will only be included when the liability is remeasured following the next change in lease payment: this is not a transition adjustment.

Once complete, the closing balance on this table should be your 1 April 2022 lease liability immediately after IFRS 16 transition. This is before the impact of any new leases commencing on 1 April, The closing balance is expected to match the value included in tab 05a of your monthly PFR form. Where this is not the case, please ensure that this transition disclosure and your monthly PFR form are brought in line ahead of month 9 when the two will be linked and validated.

Table 2 – Right of use assets under IFRS 16 as at 1 April 2022

This table reconciles the post-transition lease liability calculated in table 1 to the right of use asset value recognised on SoFP at the same point in time. Providers must apply paragraph C8(b)(ii) on transition therefore reconciling items between the lease liability and the right of use asset value upon transition are expected to be limited to:

- Peppercorn leased assets recognised at valuation which are not included in the lease liability
- Adjustments for prepaid and accrued lease payments and lease incentives previously recognised in working capital
- Initial direct costs (only if providers have not exercised the practical expedient in C10(d))
- Impairments of right of use assets at the date of initial application.
- The difference between the asset value and lease liability at 31 March 2022 on existing finance leases.

No adjustments to the right of use asset value for dilapidation provisions are made on transition therefore this is not included in the table.

While this reconciliation is not required to be disclosed in accounts by IFRS 16, it is required for consolidation adjustments at a national level. Providers may wish to include this in local transition disclosures if it adds value to a reader of the accounts.

Input sheet – Lessors – additional info

This sheet is only required to be completed by lessors of finance leases with other bodies within the government accounting boundary (including the DHSC group). We expect this to apply to fewer than a dozen providers based on historically collected finance lease receivables plus any who have derecognised assets as lessors in intra-government peppercorn lease arrangements. If your trust is not the lessor of any finance leases with other government bodies then you can ignore this tab.

IFRS 16 presents significant challenges to preparers of consolidated accounts where intra-group leasing arrangements exist. Lessor and lessee accounting treatments are misaligned resulting in double counted assets and inconsistent measurements and assumptions. Consolidation adjustments from 2022/23 will therefore be significantly more complex than they have been previously.

The outcome from consolidation adjustments must result in assets appearing on the consolidated SoFP once only, and they must be measured at the value of the underlying assets rather than the value of any rights to use them. In order to achieve this, on consolidation, all lessee accounting entries for intra-group right of use assets will be removed. Where the lessor has an operating lease, the underlying asset is already disclosed on balance sheet. However, assets that have been derecognised by lessors under finance leases will need to be added back in national numbers. This will require the national bodies to collect additional information for these derecognised assets from the lessors of intra-government finance leases.

Table 3 – Assets derecognised by lessors under intra-group finance leases

This table has been pre-populated with finance lease receivables at 31 March 2022 as disclosed in audited 2021/22 TACs. Where providers may not have completed the counterparty analysis correctly at 31 March, this can be corrected in subcode TRA1020. Any adjustments between counterparties must net to nil.

All providers with an intra-government finance lease receivable are asked to provide the gross cost or valuation and accumulated depreciation of the underlying asset as though the asset were still on the provider's SoFP. This will provide us with an estimate value for the assets we will reinstate on consolidation in 2022/23 accounts. An 'external to government' column is included in the first part of the table to aid reconciliation from finance lease receivables in 2021/22 TAC schedules. If the Trust only has external to government finance lease receivables (no intra-government) and no assets have been derecognised under intra-government peppercorn leases, then no further information is required.

Some providers may also have leased assets (as a lessor) no longer on their SoFP but have no finance lease receivable disclosed in TACs at 31 March 2022. This is likely to be one of three circumstances:

- 1) The receivable exists but was not split out in TACs at 31 March 2022. Where this is the case, please enter the value receivables not previously separately disclosed in TAC on subcode TRA1030.
- 2) The trust is a lessor in a peppercorn lease arrangement. The asset has been derecognised, but no receivable (or a trivial receivable) is recognised. Where this is the case, please include details of the derecognised asset and confirm this is a peppercorn lease in response to 'justify or change' check 14.
- 3) The lessee has paid all remaining lease payments up front. Where this is the case, please include details of the derecognised asset and confirm this is the case in response to 'justify or change' check 14.

Further detailed movements on these assets will need to be collected in TAC forms from 2022/23 onwards to drive consolidation adjustments. At this stage only this high level information is required.

Key technical reminders

The DHSC GAM 2022/23 as updated for IFRS 16 is essential reading for all bodies. It sets out the key principles of IFRS 16 and also the public sector adaptations applicable to the NHS. However, entities will also need to refer directly to the standard for more detailed guidance. When preparing your IFRS 16 models and these transitional disclosures, please remember the following technical points:

- Public sector bodies are implementing IFRS 16 using the cumulative catch-up approach on 1 April 2022 and not restating the prior year. As a result, IFRS 16 requires the incremental borrowing rate (set by HMT) to be used as the discount rate on all existing operating leases coming on SoFP on 1 April. This applies even where an interest rate is implicit in the lease. HM Treasury sets a discount rate for each calendar year. For 2022, this rate is 0.95%.
- The DHSC GAM removes the option for NHS bodies to apply IFRS 16 to intangible assets. No adjustments should be made for existing operating leases of intangible assets however any existing finance leases of intangible assets should continue to be treated as leases until the lease term ends.
- Irrecoverable VAT should not be included in the lease liability and therefore not in the value of the right of use asset. Any irrecoverable VAT previously included in the lease commitment under IAS 17 will be a reconciling item in the transitional disclosure (subcode TRA0090). Any VAT included in existing finance lease liabilities under IAS 17 should remain unchanged on transition.
- Leasehold improvements paid for by the tenant do not form part of the right of use asset value. These are recognised under IAS 16. Existing leasehold improvements should not be reclassified as 'right of use assets' on 1 April and new leasehold improvements should be capitalised as 'owned' assets. Leasehold improvements are not impacted by IFRS 16 so and will not form part of the asset reconciliation in Table 2.
- Variable lease payments that depend on an index or a rate are included in the initial lease liability. These payments are initially measured using the index or rate as at the commencement date (or transition date for existing leases). Where payments are linked to inflation this means measuring future lease payments in the initial liability assuming that RPI or CPI will not move (ie no inflation). An estimate of future inflation is not included in the initial lease liability on transition. This will arise as a subsequent remeasurement.
- Where the lessee is liable for restoration costs (dilapidations), IFRS 16 requires the expenditure to be capitalised in the right of use asset value. Note that for existing leases, no new dilapidation provisions arise on transition to IFRS 16 and no adjustments are made to the right of use asset value in respect of amounts already provided and charged to expenditure in a previous year. Dilapidation provisions are therefore not a reconciling item between the 1 April lease liability and the 1 April right of use asset value in Table 2.