



**IGRAP 13**

**ACCOUNTING STANDARDS BOARD**

**INTERPRETATION OF THE STANDARDS OF  
GENERALLY RECOGNISED ACCOUNTING  
PRACTICE**

**OPERATING LEASES – INCENTIVES**

**(IGRAP 13)**

### **Acknowledgement**

This Interpretation of the Standards of Generally Recognised Accounting Practice (IGRAP) is drawn primarily from the equivalent Interpretation of the International Financial Reporting Standard on *Operating Leases – Incentives* (SIC 15) issued by the International Financial Reporting Interpretations Committee (IFRIC) of the International Accounting Standards Board (IASB). The IASB has issued a comprehensive body of IFRICs. Extracts of the IFRIC on *Operating Leases – Incentives* are reproduced in these Interpretations of the Standards of GRAP with the permission of the IASB.

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## **OPERATING LEASES – INCENTIVES**

### **Introduction**

### **Interpretations of the Standards of Generally Recognised Accounting Practice**

The Accounting Standards Board (Board) is required in terms of the Public Finance Management Act, Act No. 1 of 1999, as amended (PFMA), to determine generally recognised accounting practice referred to as Standards of Generally Recognised Accounting Practice (GRAP).

The Board must determine GRAP for:

- (a) departments (national and provincial);
- (b) public entities;
- (c) constitutional institutions;
- (d) municipalities and boards, commissions, companies, corporations, funds or other entities under the ownership control of a municipality; and
- (e) Parliament and the provincial legislatures.

The above are collectively referred to as “entities”.

The Board has approved the application of Statements of Generally Accepted Accounting Practice (GAAP), codified by the Accounting Practices Board (APB) and issued by the South African Institute of Chartered Accountants (SAICA) to be GRAP for:

- (a) government business enterprises (GBEs)(as defined in the PFMA);
- (b) trading entities (as defined in the PFMA);
- (c) any other entity, other than a municipality, whose ordinary shares, potential ordinary shares or debt are publicly traded on the capital markets; and
- (d) entities under the ownership control of any of these entities.

The Board believes that Statements of GAAP are relevant and applicable to financial statements prepared by all such entities including those under their ownership control.

Financial statements should be described as complying with Standards of GRAP only if they comply with all the requirements of each applicable Standard of GRAP and any related Interpretations of the Standards of GRAP.

Any limitation of the applicability of specific Standards or Interpretations of the Standards of GRAP is made clear in those Standards or Interpretations of the Standards of GRAP.



## IGRAP 13

The Interpretation of the Standard of GRAP on *Operating Leases – Incentives* is set out in paragraphs .01 to .09. All paragraphs in this Interpretation of the Standards of GRAP have equal authority. The status and authority of appendices are dealt with in the preamble to each appendix. This Interpretation of the Standards of GRAP should be read in the context of its objective, its basis for conclusions if applicable, the *Preface to Standards of GRAP*, the *Preface to the Interpretations of the Standards of GRAP* and the *Framework for the Preparation and Presentation of Financial Statements*.

Standards of GRAP and Interpretations of Standards of GRAP should also be read in conjunction with any directives issued by the Board prescribing transitional provisions, as well as any regulations issued by the Minister of Finance regarding the effective dates of the Standards of GRAP, published in the Government Gazette.

Reference may be made to a Standard of GRAP that has not been issued at the time of issue of this Interpretation of the Standards of GRAP. This is done to avoid having to change the Standards already issued when a later Standard is subsequently issued. Paragraph .12 of the Standard of GRAP on *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

## **Interpretation of the Standards of GRAP on *Operating Leases – Incentives***

### **References**

- GRAP 1 *Presentation of Financial Statements* (as revised in 2010)
- GRAP 3 *Accounting Policies, Changes in Accounting Estimates and Errors* (as revised in 2010)
- GRAP 13 *Leases* (as revised in 2010)

### **Issue**

- .01 In negotiating a new or renewed operating lease, the lessor may provide incentives for the lessee to enter into the agreement. Examples of such incentives are an up-front cash payment to the lessee or the reimbursement or assumption by the lessor of costs of the lessee (such as relocation costs, leasehold improvements and costs associated with a pre-existing lease commitment of the lessee). Alternatively, initial periods of the lease term may be agreed to be rent-free or at a reduced rent.
- .02 The issue is how incentives in an operating lease should be recognised in the financial statements of both the lessee and the lessor.

### **Consensus**

- .03 All incentives for the agreement of a new or renewed operating lease shall be recognised as an integral part of the net consideration agreed for the use of the leased asset, irrespective of the incentive's nature or form or the timing of payments.
- .04 The lessor shall recognise the aggregate cost of incentives as a reduction of rental revenue over the lease term, on a straight-line basis unless another systematic basis is representative of the time pattern over which the benefit of the leased asset is diminished.
- .05 The lessee shall recognise the aggregate benefit of incentives as a reduction of rental expense over the lease term, on a straight-line basis unless another systematic basis is representative of the time pattern of the lessee's benefit from the use of the leased asset.
- .06 Costs incurred by the lessee, including costs in connection with a pre-existing lease (for example costs for termination, relocation or leasehold improvements),

shall be accounted for by the lessee in accordance with the Standard of GRAP on *Leases* (as revised in 2010) applicable to those costs, including costs which are effectively reimbursed through an incentive agreement.

### **Transitional provisions**

- .07 All changes resulting from the application of this Interpretation of the Standards of GRAP shall be accounted for in accordance with the requirements of the Standard of GRAP on Accounting Policies, Changes in Accounting Estimates and Errors (as revised in 2010).***

### **Effective date**

#### **Initial adoption of the Standards of GRAP**

- .08 This Interpretation of the Standards of GRAP becomes effective with reference to the effective date of the applicable Standards of GRAP as determined by the Minister of Finance in a regulation to be published in accordance with section 91(1)(b) of the Public Finance Management Act, Act No. 1 of 1999, as amended.***

#### **Entities already applying Standards of GRAP**

- .09 An entity shall apply this Interpretation of the Standards of GRAP for annual financial statements covering periods beginning on or after 1 April 2011.***

## Appendix

### Illustrative examples

*This appendix is illustrative only and does not form part of this Interpretation of the Standards of GRAP. The purpose of the appendix is to illustrate the application of this Interpretation to assist in clarifying its meaning.*

### Example application of this Interpretation

#### Example 1

**An entity agrees to enter into a new lease arrangement with a new lessor. The lessor agrees to pay the lessee's relocation costs as an incentive to the lessee for entering into the new lease. The lessee's moving costs are R1 000. The new lease has a term of 10 years, at a fixed rate of R2 000 per year.**

The accounting is:

The lessee recognises relocation costs of R1 000 as an expense in Year 1. Net consideration of R19 000 consists of R2 000 for each of the 10 years in the lease term, less a R1 000 incentive for relocation costs. Both the lessor and lessee would recognise the net rental consideration of R19 000 over the 10 year lease term using a single amortisation method in accordance with paragraphs .04 and .05 of this Interpretation.

#### Example 2

**An entity agrees to enter into a new lease arrangement with a new lessor. The lessor agrees to a rent-free period for the first three years as incentive to the lessee for entering into the new lease. The new lease has a term of 20 years, at a fixed rate of R5 000 per year for years 4 through 20.**

The accounting is:

Net consideration of R85 000 consists of R5 000 for each of 17 years in the lease term. Both the lessor and lessee would recognise the net consideration of R85 000 over the 20 year lease term using a single amortisation method in accordance with paragraphs .04 and .05 of this Interpretation.

## **Comparison with the Interpretation of IFRS on *Operating Leases - Incentives* (SIC 15) (December 1998)**

This Interpretation of the Standards of GRAP on *Operating Leases - Incentives* (IGRAP 13) is drawn primarily from the Interpretation of IFRS on *Operating Leases - Incentives* (SIC 15). The main differences between this Interpretation and SIC 15 are as follows:

- This Interpretation uses different terminology, in certain instances, from SIC 15. The most significant example is the use of the term “revenue”. The equivalent term in SIC 15 is “income”.