



STAFF PAPER

June 2019

IFRS® Interpretations Committee meeting

Project	Subsurface Rights (IFRS 16)		
Paper topic	Agenda decision to finalise		
CONTACT	Nicolette Lange	nlange@ifrs.org	+44 (0) 20 7246 6924
	Kathryn Donkersley	kdonkersley@ifrs.org	+44 (0) 20 7246 6970

This paper has been prepared for discussion at a public meeting of the IFRS Interpretations Committee (Committee) and does not represent the views of the International Accounting Standards Board (Board), the Committee or any individual member of the Board or the Committee. Comments on the application of IFRS Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Decisions by the Board are made in public and reported in IASB® *Update*. Decisions by the Committee are made in public and reported in IFRIC® *Update*.

Introduction

1. In March 2019 the IFRS Interpretations Committee (Committee) published a [tentative agenda decision](#) about whether IFRS 16 *Leases*, IAS 38 *Intangible Assets* or neither Standard applies in accounting for a particular contract for subsurface rights.
2. In the fact pattern described in the submission:
 - (a) a pipeline operator (customer) obtains the right to place an oil pipeline in underground space for 20 years in exchange for consideration.
 - (b) the contract specifies the exact location and dimensions (path, width and depth) of the underground space within which the pipeline will be placed.
 - (c) the land owner retains the right to use the surface of the land above the pipeline, but it has no right to access or otherwise change the use of the specified underground space throughout the 20-year period of use; and
 - (d) the customer has the right to perform inspection, repairs and maintenance work (including replacing damaged sections of the pipeline when necessary).
3. In answering the question, the Committee discussed which IFRS Standard an entity considers first. The Committee observed that paragraph 3 of IFRS 16 requires an entity to apply IFRS 16 to all leases, with limited exceptions. Paragraph 9 of IFRS 16

states: ‘At inception of a contract, an entity shall assess whether the contract is, or contains, a lease.’ The Committee also determined that, in the contract described in the request, none of the exceptions in paragraphs 3 and 4 of IFRS 16 apply—in particular, the Committee noted that the underground space is tangible. The Committee therefore concluded that the entity first considers whether the contract contains a lease as defined in IFRS 16.

4. In applying the definition of a lease in IFRS 16, the Committee observed that:
 - (a) the defined underground space occupied by the pipeline is an identified asset because:
 - (i) it is explicitly specified in the contract;
 - (ii) it is physically distinct from the remainder of the land owner’s land; and
 - (iii) the land owner has no substantive substitution rights.
 - (b) the customer has the right to control the use of the defined underground space (ie the identified asset) throughout the 20-year period of use because:
 - (i) the customer has the right to obtain substantially all the economic benefits from use of the underground space throughout the 20-year period of use. The customer has exclusive use of the underground space (and the associated pipeline) throughout the period of use.
 - (ii) the customer has the right to direct the use of the underground space because the conditions in paragraph B24(b)(i) exist. The relevant decisions about how and for what purpose the asset will be used are predetermined, and the customer has the right to operate the asset throughout the 20-year period of use (without the land owner having the right to change those operating instructions).

5. Therefore, the Committee concluded that the contract described in the submission meets the definition of a lease in IFRS 16, and no scope exclusion applies to that contract. Accordingly, the customer applies IFRS 16 in accounting for the lease.

6. The objective of this paper is to:
 - (a) analyse the comments on the tentative agenda decision; and
 - (b) ask the Committee whether it agrees with our recommendation to finalise the agenda decision.
7. There are two appendices to this paper:
 - (a) Appendix A—proposed wording of the agenda decision; and
 - (b) Appendix B—comment letters.

Comment letter summary

8. We received eight comment letters by the comment letter deadline.
9. All comments received, including any late comment letters, are available on our [website](#). Appendix B to this paper reproduces all comments received by the comment letter deadline—the comments included in Appendix B have been analysed in this paper.
10. All eight respondents agree with the Committee’s decision not to add this matter to its standard-setting agenda for the reasons set out in the tentative agenda decision.
11. Although agreeing with the tentative agenda decision, the Canadian Accounting Standards Board (AcSB) notes concerns that the conclusion reached applying IFRS Standards might be different from that reached applying US GAAP.
12. Deloitte suggests an editorial clarification to the wording of the tentative agenda decision.
13. Further details about these matters, together with our analysis, are presented below.

Staff analysis

Converged lease definition in IFRS 16 and US GAAP

Matter raised by respondent

14. IFRS 16 and Topic 842 *Leases* (US GAAP) contain the same requirements regarding the definition of a lease, drafted using the same words. The AcSB says it is important that similar conclusions are reached applying the requirements in IFRS 16 and Topic 842 with respect to an identified asset in a lease so that financial statement users are provided with appropriate decision-making information.
15. The AcSB says it is aware of the following discussion points that could affect the accounting applying US GAAP:
 - (a) whether the space is considered tangible or intangible depends on whether the space can be accessed or inhabited.
 - (b) below-ground and above-ground uses are often commercially interchangeable, thus supporting an analogy to air rights (that are outside the scope of Topic 842).
16. The AcSB asks the Committee to explain why the underground space is tangible because such explanation could further support the Committee's observation that the underground space is physically distinct.

Staff analysis

17. In the tentative agenda decision, the Committee notes that underground space is tangible in concluding that none of the scope exceptions in IFRS 16 apply to the fact pattern submitted.
18. IAS 38 *Intangible Assets* defines an intangible asset as [bold added] 'an identifiable non-monetary asset **without physical substance**'. A tangible item is therefore one that has physical substance. We note that 'accessible' and 'habitable'/'inhabitable' are not used in IFRS Standards to distinguish between tangible and intangible items.
19. We think it is a well-established conclusion that, applying IFRS Standards, land is a tangible asset because it has physical substance. Paragraph 37 of IAS 16 *Property*,

Plant and Equipment lists land, and land and buildings, as examples of classes of property, plant and equipment (which is defined in IAS 16 as ‘tangible items...’). The underground space represents a defined physically distinct portion of land.

Accordingly, we continue to support the Committee’s observation that the underground space is tangible. We recommend no change to the agenda decision in this regard.

Editorial Suggestion

Matter raised by respondent

20. Deloitte says contracts for subsurface rights often include non-lease components. Accordingly, Deloitte recommend an editorial change to the tentative agenda decision to highlight that the analysis relates only to the lease component of the contract. Deloitte suggested the following editorial change to the conclusion: ‘The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine ~~its accounting for the contract described in the request~~ whether the contract in the request contains a lease component.’

Staff analysis

21. The agenda decision first describes the request and then explains the Committee’s conclusions regarding that request. The agenda decision notes that the request asked not only whether the contract contains a lease, but first which Standard applies in accounting for the contract. Because the agenda decision discusses both (a) which Standard the entity considers first, and then (b) whether the contract contains a lease, we think the conclusion in the tentative agenda decision more accurately reflects the discussion in the agenda decision. We also note that the contract described at the beginning of the agenda decision does not mention non-lease components, and thus we think there should be no confusion in this respect.

Staff recommendation

22. On the basis of our analysis, we recommend finalising the agenda decision as published in [IFRIC Update](#) in March 2019 with no changes. Appendix A to this paper sets out the proposed wording of the final agenda decision.

Question for the Committee

Does the Committee agree with our recommendation to finalise the agenda decision set out in Appendix A to this paper?

Appendix A—Proposed wording of the agenda decision

A1 We propose the following wording for the final agenda decision, which is unchanged from the tentative agenda decision except to remove the square brackets in the last paragraph.

Subsurface Rights (IFRS 16 Leases)

The Committee received a request about a particular contract for subsurface rights. In the contract described in the request, a pipeline operator (customer) obtains the right to place an oil pipeline in underground space for 20 years in exchange for consideration. The contract specifies the exact location and dimensions (path, width and depth) of the underground space within which the pipeline will be placed. The land owner retains the right to use the surface of the land above the pipeline, but it has no right to access or otherwise change the use of the specified underground space throughout the 20-year period of use. The customer has the right to perform inspection, repairs and maintenance work (including replacing damaged sections of the pipeline when necessary).

The request asked whether IFRS 16, IAS 38 *Intangible Assets* or another Standard applies in accounting for the contract.

Which IFRS Standard does an entity consider first?

Paragraph 3 of IFRS 16 requires an entity to apply IFRS 16 to all leases, with limited exceptions. Paragraph 9 of IFRS 16 states: ‘At inception of a contract, an entity shall assess whether the contract is, or contains, a lease.’

The Committee observed that, in the contract described in the request, none of the exceptions in paragraphs 3 and 4 of IFRS 16 apply—in particular, the Committee noted that the underground space is tangible. Accordingly, if the contract contains a lease, IFRS 16 applies to that lease. If the contract does not contain a lease, the entity would then consider which other IFRS Standard applies.

The Committee therefore concluded that the entity first considers whether the contract contains a lease as defined in IFRS 16.

The definition of a lease

Paragraph 9 of IFRS 16 states that ‘a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.’

Applying paragraph B9 of IFRS 16, to meet the definition of a lease the customer must have both:

the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use; and

the right to direct the use of the identified asset throughout the period of use.

Identified asset

Paragraphs B13–B20 of IFRS 16 provide application guidance on an identified asset. Paragraph B20 states that ‘a capacity portion of an asset is an identified asset if it is physically distinct.’

But ‘a customer does not have the right to use an identified asset if the supplier has the substantive right to substitute the asset throughout the period of use’ (paragraph B14).

The Committee observed that, in the contract described in the request, the specified underground space is physically distinct from the remainder of the land. The contract’s specifications include the path, width and depth of the pipeline, thereby defining a physically distinct underground space. The space being underground does not in itself affect whether it is an identified asset—the specified underground space is physically distinct in the same way that a specified area of space on the land’s surface would be physically distinct.

The land owner does not have the right to substitute the underground space throughout the period of use. Consequently, the Committee concluded that the specified underground space is an identified asset as described in paragraphs B13–B20.

Right to obtain substantially all the economic benefits from use

Paragraphs B21–B23 of IFRS 16 provide application guidance on the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use. Paragraph B21 specifies that a customer can have that right, for example, by having exclusive use of the identified asset throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to obtain substantially all the economic benefits from use of the specified underground

space throughout the 20-year period of use. The customer has exclusive use of the specified underground space throughout that period of use.

Right to direct the use

Paragraphs B24-B30 of IFRS 16 provide application guidance on the right to direct the use of an identified asset throughout the period of use. Paragraph B24 specifies that a customer has that right if either:

the customer has the right to direct how and for what purpose the asset is used throughout the period of use; or

the relevant decisions about how and for what purpose the asset is used are predetermined and:

(i) the customer has the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions; or (ii) the customer designed the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to direct the use of the specified underground space throughout the 20-year period of use because the conditions in paragraph B24(b)(i) exist. How and for what purpose the specified underground space will be used (ie to locate the pipeline with specified dimensions through which oil will be transported) is predetermined in the contract. The customer has the right to operate the specified underground space by having the right to perform inspection, repairs and maintenance work. The customer makes all the decisions about the use of the specified underground space that can be made during the 20-year period of use.

Consequently, the Committee concluded that the contract described in the request contains a lease as defined in IFRS 16. The customer applies IFRS 16 in accounting for that lease.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine its accounting for the contract described in the request. Consequently, the Committee {decided} not to add the matter to its standard-setting agenda.

Appendix B—Comment letters

International Financial Reporting Standards Interpretations
Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

29 March 2019

Dear IFRS Interpretations Committee members,

Invitation to comment - Tentative Agenda Decision (TAD): Subsurface rights (IFRS 16 Leases) - Agenda Paper 5 (IFRIC Update March 2019)

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the above tentative agenda decision of the IFRS Interpretations Committee (the Committee) published in the March 2019 *IFRIC Update*.

The Committee received a request about a particular contract for subsurface rights, which asked whether IFRS 16, IAS 38 *Intangible Assets* or another standard applies in accounting for such contract.

We agree with the Committee's conclusion that the contract described in the request contains a lease as defined in IFRS 16. We also agree that the principles and requirements in IFRS standards provide an adequate basis for an entity to determine its accounting for the contract described in the request.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas at the above address or on +44 [0]20 7951 3152.

Yours faithfully

Ernst + Young Global Limited

10th May, 2019

Ms Sue Lloyd,
Chair, IFRS Interpretations committee,
IFRS Foundation,
London, UK

Dear Ms Sue,

Subject: Tentative Agenda Decision (TAD) March, 2019 – Public Comments by May 15th, 2019

The Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (the ICAI) welcomes the following four tentative agenda decisions of IFRS Interpretations Committee published in March 2019:

1. Costs to Fulfil a Contract (IFRS 15)
2. Holdings of Cryptocurrencies
3. Effect of a Potential Discount on Plan Classification (IAS 19)
4. Subsurface Rights (IFRS 16)

We agree with the above mentioned clarifications.

With kind regards

CA. M.P Vijay Kumar

Chairman
Accounting Standards Board
Institute of Chartered Accountants of India

14 May 2019

Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
United Kingdom
E14 4HD

Dear Ms Lloyd

Tentative agenda decision – IFRS 16 Leases: Subsurface rights

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the March 2019 IFRIC Update of the tentative decision not to take onto the Committee's agenda the request for clarification on the Standard applicable (IFRS 16, IAS 38 or another Standard) in accounting for a contract for subsurface rights.

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision.

We note that contracts with respect to subsurface rights often include compensation to the supplier for elements other than the subsurface rights, for example compensation for inconvenience to the landowner if the customer needs to access the subsurface to perform repairs and maintenance work. Accordingly, we suggest that the agenda decision specifies that the analysis relates only to the lease component included in contracts for subsurface rights. This may be achieved by the following editorial change (blacklined) to the penultimate paragraph:

"...provide an adequate basis for an entity to determine whether the contract in the request contains a lease component."

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely



Veronica Poole
Global IFRS Leader

15 May 2019

Ms. Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd

Tentative Agenda Decisions

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the following Tentative Agenda Decisions:

- (1) Tentative Agenda Decision – Subsurface Rights (IFRS 16 *Leases*).
- (2) Tentative Agenda Decision – Effect of a Potential Discount on Plan Classification (IAS 19 *Employee Benefits*).
- (3) Tentative Agenda Decision – Holdings of Cryptocurrencies.

We agree with the Interpretations Committee's reasons set out in the respective Tentative Agenda Decisions for not adding these items onto its agenda.

If you need further clarification, please contact the undersigned by email at beeleng@masb.org.my or at +603 2273 3100.

Thank you.

Yours sincerely,



TAN BEE LENG
Executive Director



IKATAN AKUNTAN INDONESIA
(INSTITUTE OF INDONESIA CHARTERED ACCOUNTANTS)

Nomor : 0638/DSAK/IAI/V/2019

Jakarta, 8 May 2019

International Financial Reporting Standards Interpretations Committee
Columbus Building, 7 Westferry Circus
Canary Wharf, London
E14 4HD

Invitation to comment – Tentative Agenda Decision (TAD): Subsurface rights (IFRS 16 Leases) – Agenda Paper 5 (IFRIC Update March 2019)

Dear IFRS Interpretations Committee members,

Dewan Standar Akuntansi Keuangan (DSAK) - The Indonesian Financial Accounting Standards Board, as part of Ikatan Akuntan Indonesia (IAI) - the Institute of Indonesia Chartered Accountants, is the national accounting standard-setter in Indonesia.

On behalf of DSAK IAI, I am writing to respond regarding on the TAD: Subsurface rights (IFRS 16 Leases). DSAK IAI welcomes the opportunity to offer its views on the above TAD of the IFRS Interpretations Committee (IFRIC) published in the March 2019 *IFRIC Update*. We agree with the IFRIC's conclusion that based on the contract described in the request contains a lease as defined in IFRS 16. We also agree that the principles and requirements in IFRS standards provide an adequate basis for an entity to determine its accounting for the contract described in the request.

We hope that our responses could contribute to the IFRIC's future deliberations. Should you have further concerns regarding our responses, please do not hesitate to contact us at dsak@iaiglobal.or.id.

Yours sincerely,


IKATAN AKUNTAN INDONESIA
(Institute of Indonesia Chartered Accountants)

Djohan Pinnarwan

Chairman

The Indonesian Financial Accounting Standards Board
Institute of Indonesia Chartered Accountants

GRHA AKUNTAN, Jalan Sindanglaya No. 1, Menteng, Jakarta 10310 - INDONESIA

Telp.: (62-21) 3190 4232 Hunting, Fax.: (62-21) 315 2076, E-mail: iai-info@iaiglobal.or.id, Home Page: <http://www.iaiglobal.or.id>

(NBAA)



THE NATIONAL BOARD OF ACCOUNTANTS AND AUDITORS
TANZANIA

TEL NOS: +255 26 2963318-9
E-MAIL: info@nbaa.go.tz
WEBSITE: www.nbaa.go.tz

NATIONAL AUDIT OFFICE "AUDIT HOUSE",
8TH FLOOR, 4 UKAGUZI ROAD,
P. O. BOX 1271,
41104 TAMBUKARELI,
DODOMA, TANZANIA

Date: 15th May, 2019

Chief Executive Officer,
IFRS Foundation
Columbus Building
7 West ferry Circus
Canary Wharf
London E14 4HD

Dear Sir/Madam

RE: COMMENTS ON THE TENTATIVE AGENDA–SURBSURFACE RIGHTS (IFRS 16)

Refer to the heading above.

NBAA as the PAO responsible for the professional training, development and regulation of the accountancy profession in Tanzania and as the member board of the International Federation of Accountants welcomes the opportunity to provide you with our comments on the Exposure Draft for onerous contract – cost of fulfilling a contract.

In principle, we are supportive of the decision that has been made by the IFRS Interpretation Committee for the request of guidance in respect of a particular contract for subsurface rights that the contract described in the request contains a lease as defined in IFRS 16 and thus, the customer applies IFRS 16 in accounting for that lease due to the following:-

In the contract described in the request, the customer has the right to direct the use of the specified underground space throughout the 20-year period of use because the conditions in paragraph B24(b)(i) exist.

- How and for what purpose the specified underground space will be used (ie to locate the pipeline with specified dimensions through which oil will be transported) is predetermined in the contract.
- The customer has the right to operate the specified underground space by having the right to perform inspection, repairs and maintenance work.
- The customer makes all the decisions about the use of the specified underground space that can be made during the 20-year period of use.

Thank you in advance for your cooperation.

Yours sincerely,



CPA Angyelile V. Tende
For: EXECUTIVE DIRECTOR



Member of International Federation of Accountants (IFAC) & Pan African Federation of Accountants (PAFA)



All communication to be addressed to the Executive Director NBAA



Canadian Accounting Standards Board
277 Wellington Street West,
Toronto, ON Canada M5V 3H2
T. 416 977.3222 F. 416 204.3412
www.frascanada.ca

May 15, 2019

(By e-mail to ifric@ifrs.org)

IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Sirs,

Re: Tentative agenda decision on IFRS 16 Leases – Subsurface Rights

This letter is the response of the staff of the [Canadian Accounting Standards Board](http://www.frascanada.ca) (AcSB) to the IFRS Interpretations Committee's (Committee) tentative agenda decision on subsurface rights. This tentative agenda decision was published in the March 2019 IFRIC® Update.

The views expressed in this letter take into account discussions with practitioners and individual members of the AcSB staff.

We agree with the Committee's decision not to add this item to its agenda for the reasons set out in the tentative agenda decision. However, we have heard concerns that the conclusion reached for this fact pattern under IFRS Standards might be different from the conclusion reached under U.S. GAAP. Some of the discussion points we're aware of that could affect the accounting under U.S. GAAP include:

- whether the space is considered tangible or intangible depends on if the space can be accessed or inhabited; and
- below-ground and above-ground uses are often commercially interchangeable, hence supporting an analogy of subsurface rights to air rights (which is outside the scope of the leases standard in U.S. GAAP).

Considering the above points, we suggest that the Committee explain why the underground space is tangible. The explanation could further support the Committee's observation that the underground space is physically distinct. Given the requirements in IFRS 16 *Leases* and ASU 842 *Leases* are converged in the area of determining an identified asset in a lease, we think it is important that similar conclusions are reached so that financial statement users are provided with appropriate decision-making information.

We would be pleased to elaborate on our comments in more detail if you require. If so, please contact me at +1 416 204-3487 (e-mail awhite@acsbcanada.ca), or, alternatively, Davina Tam, Principal, Accounting Standards at +1 416 204-3514 (e-mail dtam@acsbcanada.ca).

Yours truly,



Andrew White, CPA, CA
Senior Principal, Canadian Accounting Standards Board
awhite@acsbcanada.ca
+1 416 204-3487

May 8, 2019

Ms. Sue Lloyd, Chair
International Financial Reporting Standards Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd,

Tentative Agenda Decision—Subsurface Rights (IFRS 16)

The Financial Accounting Issues Task Force of the Taiwan Financial Reporting Standards Committee (TFRSC) of Accounting Research and Development Foundation in Taiwan appreciates the opportunity to respond to the above tentative agenda decision.

The attachments (Attachment 1) are our comments to this tentative agenda decision. The comments are those of the Financial Accounting Issues Task Force and do not necessarily represent official opinions of the TFRSC.

If you have any question about our comments, please contact me (via my email: ccliu@management.ntu.edu.tw) or Ms. Margaret Tsui (via her email: margaret@ardf.org.tw).

Sincerely Yours,



Chi-Chun Liu, Ph.D.
Chairman,
Taiwan Financial Reporting Standards Committee,
Accounting Research and Development Foundation, Taiwan

Attachment 1

Comments from ARDF Taiwan on Tentative Agenda Decision—Subsurface Rights (IFRS 16)

Tentative Agenda Decision—Subsurface Rights (IFRS 16)

Question

The IFRS Interpretations Committee (Committee) discussed the following matter and tentatively decided not to add it to its standard-setting agenda. The Committee will reconsider this tentative decision, including the reasons for not adding the matter to its standard-setting agenda, at a future meeting. The Committee invites comments on its tentative agenda decision. All comments will be on the public record and posted on our website unless a responder requests confidentiality and we grant that request. We do not normally grant such requests unless they are supported by good reason, for example, commercial confidence.

Tentative agenda decision

The Committee received a request about a particular contract for subsurface rights. In the contract described in the request, a pipeline operator (customer) obtains the right to place an oil pipeline in underground space for 20 years in exchange for consideration. The contract specifies the exact location and dimensions (path, width and depth) of the underground space within which the pipeline will be placed. The land owner retains the right to use the surface of the land above the pipeline, but it has no right to access or otherwise change the use of the specified underground space throughout the 20-year period of use. The customer has the right to perform inspection, repairs and maintenance work (including replacing damaged sections of the pipeline when necessary).

The request asked whether IFRS 16, IAS 38 Intangible Assets or another Standard applies in accounting for the contract.

Which IFRS Standard does an entity consider first?

Paragraph 3 of IFRS 16 requires an entity to apply IFRS 16 to all leases, with limited exceptions. Paragraph 9 of IFRS 16 states: ‘At inception of a contract, an entity shall assess whether the contract is, or contains, a lease.’

Attachment 1

Comments from ARDF Taiwan on Tentative Agenda Decision—Subsurface Rights (IFRS 16)

The Committee observed that, in the contract described in the request, none of the exceptions in paragraphs 3 and 4 of IFRS 16 apply—in particular, the Committee noted that the underground space is tangible. Accordingly, if the contract contains a lease, IFRS 16 applies to that lease. If the contract does not contain a lease, the entity would then consider which other IFRS Standard applies.

The Committee therefore concluded that the entity first considers whether the contract contains a lease as defined in IFRS 16.

The definition of a lease

Paragraph 9 of IFRS 16 states that ‘a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.’ Applying paragraph B9 of IFRS 16, to meet the definition of a lease the customer must have both:

the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use; and

the right to direct the use of the identified asset throughout the period of use.

Identified asset

Paragraphs B13–B20 of IFRS 16 provide application guidance on an identified asset. Paragraph B20 states that ‘a capacity portion of an asset is an identified asset if it is physically distinct.’ But ‘a customer does not have the right to use an identified asset if the supplier has the substantive right to substitute the asset throughout the period of use’ (paragraph B14).

The Committee observed that, in the contract described in the request, the specified underground space is physically distinct from the remainder of the land. The contract’s specifications include the path, width and depth of the pipeline, thereby defining a physically distinct underground space. The space being underground does not in itself affect whether it is an identified asset—the specified underground space is physically distinct in the same way that a specified area of space on the land’s surface would be

Attachment 1

Comments from ARDF Taiwan on Tentative Agenda Decision—Subsurface Rights (IFRS 16)

physically distinct.

The land owner does not have the right to substitute the underground space throughout the period of use. Consequently, the Committee concluded that the specified underground space is an identified asset as described in paragraphs B13–B20.

Right to obtain substantially all the economic benefits from use

Paragraphs B21–B23 of IFRS 16 provide application guidance on the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use. Paragraph B21 specifies that a customer can have that right, for example, by having exclusive use of the identified asset throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to obtain substantially all the economic benefits from use of the specified underground space throughout the 20-year period of use. The customer has exclusive use of the specified underground space throughout that period of use.

Right to direct the use

Paragraphs B24–B30 of IFRS 16 provide application guidance on the right to direct the use of an identified asset throughout the period of use. Paragraph B24 specifies that a customer has that right if either:

the customer has the right to direct how and for what purpose the asset is used throughout the period of use; or

the relevant decisions about how and for what purpose the asset is used are predetermined and: (i) the customer has the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions; or (ii) the customer designed the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to direct the use of the specified underground space throughout the 20-year period of

Attachment 1

Comments from ARDF Taiwan on Tentative Agenda Decision—Subsurface Rights (IFRS 16)

use because the conditions in paragraph B24(b)(i) exist. How and for what purpose the specified underground space will be used (ie to locate the pipeline with specified dimensions through which oil will be transported) is predetermined in the contract. The customer has the right to operate the specified underground space by having the right to perform inspection, repairs and maintenance work. The customer makes all the decisions about the use of the specified underground space that can be made during the 20-year period of use.

Consequently, the Committee concluded that the contract described in the request contains a lease as defined in IFRS 16. The customer applies IFRS 16 in accounting for that lease.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine its accounting for the contract described in the request. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Deadline for submitting comment letters: 15 May 2019. The Committee will consider all comments received in writing by that date; agenda papers analysing comments received will include analysis only of comments received by that date.

Response to the above Question:

Agreeing with your analysis, we support this tentative decision; that is, IFRS16, instead of other Standards, applies to the subsurface right and the matter discussed need not adding to the standard-setting agenda.

The controversy is over whether the subsurface of the land is an identified asset. The contract, according to the request, specified the exact location and dimension of the underground space within which the pipeline will be placed. That clearly proves that the subsurface of the land is identified because it is physically distinct and can be explicitly specified in a contract (see paragraph B13 and BC116 of IFRS16). Since the subsurface of

Attachment 1

Comments from ARDF Taiwan on Tentative Agenda Decision—Subsurface Rights (IFRS 16)

the land, according to the term of the contract, is an indentified asset, we think the contract in the request which conveyed the right to control the use of that subsurface of the land for a period of time contains a lease.