accounting guideline
PSG-5
sale-leaseback transactions

This Guideline is to be read in conjunction with the Introduction to Accounting Guidelines contained in the CPA Canada Public Sector Accounting Handbook.

June 2005 *

PURPOSE AND SCOPE

1 The purpose of this Guideline is to define a sale-leaseback transaction and describe how to account for such transactions when the leaseback involves either a leased tangible capital asset (LTCA) or an operating lease.

2 This Guideline applies to government financial statements applying FINANCIAL STATEMENT PRESENTATION, Section PS 1202. [Former paragraph PSG-5.2, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

3 It may be useful to read this Guideline in conjunction with PUBLIC SECTOR GUIDELINE PSG-2, Leased Tangible Capital Assets.

DEFINITIONS

4 The following definitions have been adopted for the purposes of this Guideline:

(a) A **sale-leaseback transaction** is the sale of property by a government and the leasing of the same property, or a portion thereof, back to the government. The transaction may be effected through a series of concurrent sale transactions involving more than one external party or organization within the government reporting entity, with the end result being that the government retains the use of the property, or a portion thereof.

(b) The **carrying amount** of property is its cost, less both accumulated amortization and the amount of any write-downs.

(c) An **economic gain** results from each of the following circumstances:

(i) The proceeds received for the property are greater than its fair value.

(ii) The present value of the minimum lease payments is less than the fair value of the lease.

(d) An **economic loss** results from each of the following circumstances:

(i) The proceeds received for the property are less than its fair value.

(ii) The present value of the minimum lease payments is greater than the fair value of the lease.

(e) **Fair value** is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

(f) A **holding gain** occurs when the fair value of the property exceeds its carrying amount.

(g) **Impairment** occurs when the fair value of the property is less than the carrying amount of the property.

(h) **Interrelationship** occurs whenever an economic gain / loss attributable to the proceeds received for the property is partially or entirely compensated for by an economic loss / gain attributable to the present value of the minimum lease payments, resulting in the creation of either a loan liability or a prepaid asset.

(i) A **lease** is the conveyance, by a lessor to a lessee, of the right to use a tangible capital asset, usually for a specified period of time in return for rent.

COMPONENTS APPROACH

5 The "interdependence" approach is commonly adopted in accounting for sale-leaseback transactions. It assumes that the terms of the sale and the leaseback are interdependent and cannot be objectively separated. For the purposes of this Guideline, the Public Sector Accounting Board (the Board) has adopted a "components" approach.

6 The components approach assumes that the sale and leaseback can be separated objectively by comparing the terms and conditions of the sale-leaseback to its related fair value information. The comparison enables each component part of the transaction to be accounted for according to its economic substance. The components of a sale-leaseback transaction include the property, lease liability, revenues and expenses (including gains and losses), and any other assets or liabilities that may result from the transaction.

7 In accounting for the economic substance, the components approach:

(a) recognizes that:

(i) there is a substantive difference between an LTCA and an operating lease such that when the leaseback constitutes an LTCA, it is a financing arrangement, and when it constitutes an operating lease, it is a sale of the property; and

(ii) the carrying amount of leased back property remains constant when the government retains substantially all of the benefits and risks incidental to ownership associated with the property (or portion thereof); and

(b) requires that:

(i) holding gains be recognized as revenue only when the government no longer retains substantially all of the benefits and risks incidental to ownership associated with the property (or portion thereof);

(ii) all economic gains and losses arising from a sale-leaseback constituting an LTCA be recognized immediately so that the net effect on operating results reflects the benefit or cost to the government of having to repay less or more than it was loaned;

(iii) all economic gains and losses from the sale portion of a sale-leaseback transaction constituting an operating lease be recognized immediately, because they have been realized;

(iv) all economic gains from the lease portion of a sale-leaseback transaction constituting an operating lease not be recognized immediately, because they have not been realized; and

(v) all economic losses from the lease portion of a sale-leaseback transaction constituting an operating lease be recognized immediately to reflect the obligation to an uneconomic arrangement.

8 The components approach is consistent with FINANCIAL STATEMENT PRESENTATION, Section PS 1202, such that only amounts that meet the definitions of assets and liabilities in Chapter 8 of the Conceptual Framework are presented on the statement of financial position (i.e., the deferral of amounts resulting from sale-leaseback transactions is not permitted as they do not meet these definitions). [Former paragraph PSG-5.8, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.] [Former paragraph PSG-5.8, amended by the Conceptual Framework, retained in Archived Pronouncements.]

9 The use of fair value information is key to applying the components approach. Fair value information for property is necessary in assessing whether a lease constitutes an LTCA.

10 The requirement for fair value information with respect to the "lease contract" itself is an extension of existing fair value information requirements in accounting for sale-leaseback transactions. This type of information is not only important for applying the components approach, but also for determining the economics of entering into a sale-leaseback transaction.

DETERMINING FAIR VALUE IN A SALE-LEASEBACK TRANSACTION

11 Fair value information provides the most appropriate benchmark for determining the components of the transaction. Unlike when determining the existence of an LTCA, when fair value information is only required for the property being leased, applying a components approach requires fair value information for the lease itself. Proceeds received and the

lease payments may be at amounts other than either their carrying amount or fair value. Any differences need to be understood to determine their economic substance and how those differences are to be accounted for.

12 The selection of the most appropriate methodology for determining fair value requires professional judgment. For certain leases or property, such as vehicles and buildings, fair values are often readily obtainable by reference to prices in active markets. However, for other property, such as infrastructure, it may be difficult to establish a fair value because of the absence of an active market.

13 When determining fair values (or a surrogate thereof), the following methodologies would be considered:

(a) when market-based information is available:

(i) value in an active and liquid market for the same or a similar property;

(ii) values for other properties with similar characteristics, circumstances and locations; and

(iii) other market-based evidence, such as a discounted cash flow calculation using market estimates of the cash flows able to be generated by the property and a market-based discount rate; or

(b) in the absence of market-based information:

(i) depreciated replacement cost; and

(ii) depreciated reproduction cost.

14 When a particular fair value within a range of values appears to be a better estimate than any other, that fair value would be used. When uncertainty exists, the fair value used would attempt to ensure that assets, revenues and gains are not overstated and that liabilities, expenses and losses are not understated.

15 When alternative methods for measuring fair value are being considered, the government would evaluate whether the method of measurement selected is appropriate in the circumstances.

16 Evaluating whether the method of measurement of fair value is appropriate in the circumstances requires the use of professional judgment. In making its selection, the government needs to ensure that:

(a) it has sufficiently evaluated and appropriately applied the criteria to support the selected method;

(b) the valuation method is appropriate in the circumstances given the nature of the transaction being valued; and

(c) the valuation method is appropriate in relation to the business, industry and environment in which the transaction has taken place.

17 Because some fair value measurements are inherently more complex than others and involve uncertainty about the occurrence of future events or their outcomes, governments may need to apply assumptions that involve the use of professional judgment as part of the valuation process. Governments would ensure that such assumptions are reasonable and reflect, or are not inconsistent with, any available market information.

18 Assumptions ordinarily are supported by different types of evidence from internal and external sources that provide objective support for the assumptions used. The consideration of whether the assumptions provide a reasonable basis for the fair value measurements relates to the whole set of assumptions as well as to each assumption individually. Assumptions are frequently interdependent and therefore need to be internally consistent. A particular assumption that may appear reasonable when made in isolation may not be reasonable when used in conjunction with other assumptions.

19 In situations when the entire property has been sold and only a portion leased back as an LTCA, quantifying the portion of the property leased back using fair value information becomes essential, and will require professional judgment.

20 The portion of the property being leased back may relate to the physical property itself (for example, one floor of an office tower), or to a portion of the property's remaining economic life (for example, seven years of an estimated life of 10 years). In determining fair value, it is necessary to review the transaction in its entirety and apply professional judgment (for example, leasing 800 square feet of the third floor may not have the same fair value as leasing 800 square feet of the top floor).

21 A comparison of the fair value of the portion of property leased back (as an LTCA) to that of the entire property provides an objective measure of the quantitative size of that portion.

22 Any difference between the proceeds received and the fair value of the property is accounted for in accordance with its economic substance.

23 Similarly, any difference between the present value of the minimum lease payments and the fair value of the lease is also accounted for in accordance with its economic substance.

24 To enable a meaningful comparative analysis of:

(a) the proceeds received compared to the fair value of the property; and

(b) the present value of the minimum lease payments compared to the fair value of the lease;

it is necessary to identify and understand all material components of those proceeds and lease payments. A sale-leaseback transaction can be constructed in various ways in order to suit the specific objectives of the parties involved. These can include economic, social and political objectives. The entire transaction, or component parts of the transaction, may occur at fair value or other than fair value depending on the objectives to be met.

25 Professional judgment would be exercised when assessing the proceeds received and the present value of the minimum lease payments, regardless of the nature of the lease. It is important to determine if there are any other events and arrangements, possibly not directly related to the transaction, that when viewed in their entirety would cause the transaction to be interpreted differently. The same approach is applied here as in PUBLIC SECTOR GUIDELINE PSG-2, Leased Tangible Capital Assets, for determining the minimum lease payments. However, because this Guideline also covers the proceeds received from the transaction, a similar analysis is required of those proceeds.

26 The proceeds received and the minimum lease payments component of the transaction may be "bundled" into a larger contractual arrangement that also includes other items. Examples of items that could be "bundled" into the arrangement, and how they are to be treated, are discussed below:

(a) Executory costs (insurance, maintenance and other costs) that relate to the operation of the property, and ancillary contractual arrangements that pertain to the leased property, would be excluded from the calculation of proceeds received for the property and the minimum lease payments.

(b) Certain types of additional rentals (payments that guarantee a minimum usage of the property) would be included in the calculation of the proceeds received for the property and the minimum lease payments.

(c) The impact of various types of financial assistance (transfers, loans or loan guarantees) to or from the lessor that could influence the amount of the minimum lease payments would be considered in the calculation of the proceeds received for the property and the minimum lease payments.

For example, if the proceeds received for the property are greater than the fair value of the property, the excess could actually have stipulations attached to it specifying the purpose(s) for which the excess is to be used. As such, those surplus proceeds could actually be an externally restricted amount, which may need to be unbundled and accounted for separately in accordance with RESTRICTED ASSETS AND REVENUES, Section PS 3100. The effects of these other types of contractual arrangements would be accounted for in accordance with their economic substance (see Appendix B, Example 1, for an illustration of a "bundled" arrangement).

27 Any impairment in value of the property subject to sale-leaseback would be recognized in accordance with TANGIBLE CAPITAL ASSETS, Section PS 3150, prior to applying the provisions of this Guideline.

SALE-LEASEBACK INVOLVING AN LTCA

28 A sale-leaseback transaction that results in an LTCA is in substance a financing arrangement. The property has simply been used as collateral for a loan, which may be at an amount different than the fair value of the property. From the government's point of view, nothing has changed in relation to that portion of the property leased back, as the government still retains substantially all of the benefits and risks incidental to ownership associated with the property.

Sale and 100 percent leaseback as an LTCA

29 In those situations involving a sale and 100 percent leaseback as an LTCA, the LTCA would be recognized at its carrying amount prior to the transaction. Holding gains would not be recognized in the operating results (see Appendix B, Example 2, Situations 2.I-2.IV).

30 The lease liability, after considering the effects of any arrangements set out in paragraphs 25-26, would be recognized at the present value of the minimum lease payments (see Appendix B, Example 2, Situations 2.I-2.IV).

31 Any economic gains or losses, after considering the effects of any arrangements set out in paragraphs 25-26, would be recognized immediately in the operating results (see Appendix B, Example 2, Situations 2.II-2.IV). By immediately recognizing these economic gains and losses, the net effect on the operating results will be to immediately reflect either:

(a) the realized benefit of a government having entered into an arrangement when it will have to repay less than it has borrowed; or

(b) the future consequence of having entered into an uneconomic arrangement by agreeing to repay more than it has borrowed.

Sale and less than 100 percent leaseback as an LTCA

32 In those situations involving a sale and less than 100 percent leaseback as an LTCA, the government has structured its sale-leaseback with the lessor to result in the government leasing back a portion of the property as an LTCA, with the remainder of the property in substance being sold to the lessor.

33 The LTCA would be reported at its carrying amount in proportion to the amount of the property actually leased back. Holding gains associated with the portion leased back as an LTCA would not be recognized in the operating results. That proportion of the holding gain associated with the portion of the property not leased back as an LTCA would be recognized in the operating results, as there has in substance been a sale of that portion (see Appendix B, Example 3, Situations 3.I-3.V).

34 The lease liability, after considering the effects of any arrangements set out in paragraphs 25-26, would be recognized at the present value of the minimum lease payments (see Appendix B, Example 3, Situations 3.I-3.V).

35 Any economic gain or loss, after considering the effects of any arrangements set out in paragraphs 25-26 on the whole transaction, would be recognized immediately in the operating results (see Appendix B, Example 3, Situations 3.II-3.V). By immediately recognizing these economic gains and losses, the net effect on the operating results will be as described in paragraph 31.

SALE-LEASEBACK INVOLVING AN OPERATING LEASE

36 A sale-leaseback that results in an operating lease is a sale of property. The government, from its point of view, no longer retains substantially all the benefits and risks incidental to ownership associated with the property sold.

37 Professional judgment would be exercised in those situations when property is sold and subsequently leased back as an operating lease. In some instances, there can be a unique relationship whereby an economic gain and an economic loss can be attained on the same transaction (an "interrelationship", see paragraphs 43-51).

38 When determining the amount of proceeds received and the present value of the minimum lease payments, consideration would be given to the effects of any arrangements discussed in paragraphs 25, 26 and 37.

39 Any holding gains would be immediately recognized in the operating results (see Appendix B, Example 4, Situations 4.I-4.V).

Sale-leaseback without interrelationship

40 In those situations involving an operating lease without interrelationship, all economic gains and losses associated with proceeds received would be recognized immediately in operating results, because they have been realized (see Appendix B, Example 4, Situations 4.II-4.III).

41 Economic gains associated with the present value of the minimum lease payments being less than the fair value of the lease would not be immediately recognized in the operating results, because they are not realized. Such gains will be recognized as they are realized over the life of the lease, by virtue of the government paying lower than fair value rent and recognizing this lower amount as expense (see Appendix B, Example 4, Situation 4.IV).

42 Economic losses associated with the present value of the minimum lease payments being greater than the fair value of the lease would be recognized immediately in the operating results. Immediate recognition ensures that the operating results reflect the future consequence from having entered into an uneconomic obligation. In substance, the economic loss constitutes a form of contribution payable to the lessor; therefore, a liability for the amount of the economic loss would be recognized and settled in proportion to the minimum lease payments (see Appendix B, Example 4, Situation 4.V).

Sale-leaseback with interrelationship

43 In those situations involving an operating lease that result in the creation of an economic gain and a compensatory economic loss, there will be interrelationship occurring within that transaction. Determining the amount of that interrelationship is necessary to enable the substance of the transaction to be reported.

44 The interrelationship exists because both the government and the lessor have knowingly agreed to incur either an economic gain or economic loss for their respective component of the transaction in exchange for the other party agreeing to an offsetting and equalizing economic gain or economic loss.

45 The compensatory amount could constitute the entire economic gain and economic loss (when the gain and loss are equal), or could be embedded within the economic gain and economic loss (when the gain and loss are of different amounts). Ultimately, the amount of the interrelationship is limited to the extent to which offset can occur between the economic gain and economic loss.

46 In substance, an economic gain and economic loss that are compensatory are an artificial economic gain and economic loss, and would therefore be treated as discussed below. Having accounted for the interrelationship, any remaining "real" economic gain (see Appendix B, Example 5, Situation 5.III) and economic loss would be treated in accordance with paragraphs 40-42.

47 When determining if an interrelationship exists, consideration also would be given to those factors set out in paragraphs 25-26.

48 In substance, interrelationships create specific rights and obligations, because the government has entered into an arrangement that has established a present entitlement or obligation. This occurs because proceeds received and the present value of the minimum lease payments are both either:

(a) less than their respective fair values; or

(b) greater than their respective fair values.

49 When the proceeds received and the present value of the minimum lease payments are both less than their respective fair values, the amount of interrelationship is in substance a prepayment (a non-financial asset). The government has taken a portion of the proceeds received and instructed the lessor to immediately apply it against the present value of the minimum lease payments. The amount of the interrelationship would be recognized as a prepaid expense (a non-financial asset) (see Appendix B, Example 5, Situation 5.I).

50 When the proceeds received and the present value of the minimum lease payments are both greater than their respective fair values, the amount of interrelationship is in substance a loan payable (a liability). The government has received additional funds from the lessor with repayment factored into the present value of the minimum lease payments. The amount of the interrelationship would be recognized as a loan payable (see Appendix B, Example 5, Situation 5.II).

51 Loans payable and prepayments are settled in proportion to the minimum lease payments.

PRESENTATION AND DISCLOSURE

Disclosure

52 Sale-leaseback transactions can be a significant means of financing and can include significant obligations. Accordingly, separate disclosure of information about such transactions is useful in identifying the costs and risks associated with such transactions, as well as their effect on the future revenue requirements of government.

53 In addition to the disclosure requirements of PUBLIC SECTOR GUIDELINE PSG-2, Leased Tangible Capital Assets, gains (both holding and economic) and economic losses that are material, either individually or in the aggregate, should be disclosed. A description should be provided of individually material sale-leaseback transactions.

Statement of cash flow

54 When the leased back property constitutes an LTCA, the transaction should be recorded as a financing transaction in the statement of cash flow.

EFFECTIVE DATE AND TRANSITIONAL PROVISIONS

55 This Guideline applies to all sale-leaseback transactions entered into during fiscal years beginning on or after April 1, 2005.

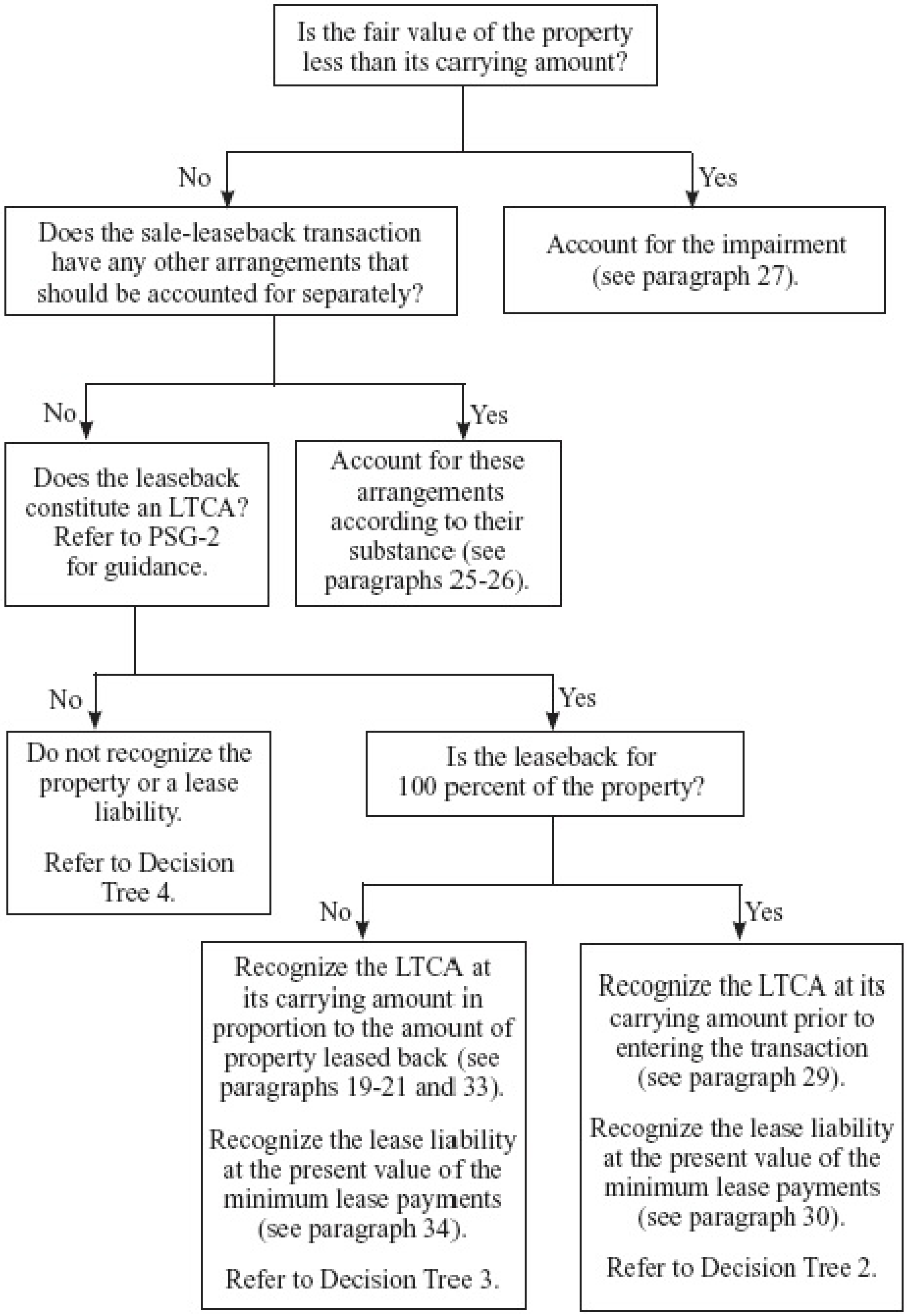
56 [Former paragraph PSG-5.56, deleted by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

57 FINANCIAL STATEMENT PRESENTATION, Section PS 1202, issued in October 2023, amended paragraphs PSG-5.2 and PSG-5.8 and the description to the Illustrative Examples in Appendix B and removed paragraph PSG-5.56. The amendments are applicable at the same time as Section PS 1202, for fiscal years beginning on or after April 1, 2026. Earlier adoption is permitted if Section PS 1202 is also early adopted. Prior period amounts would need to be restated to conform to the requirements for comparative financial information in Section PS 1202.

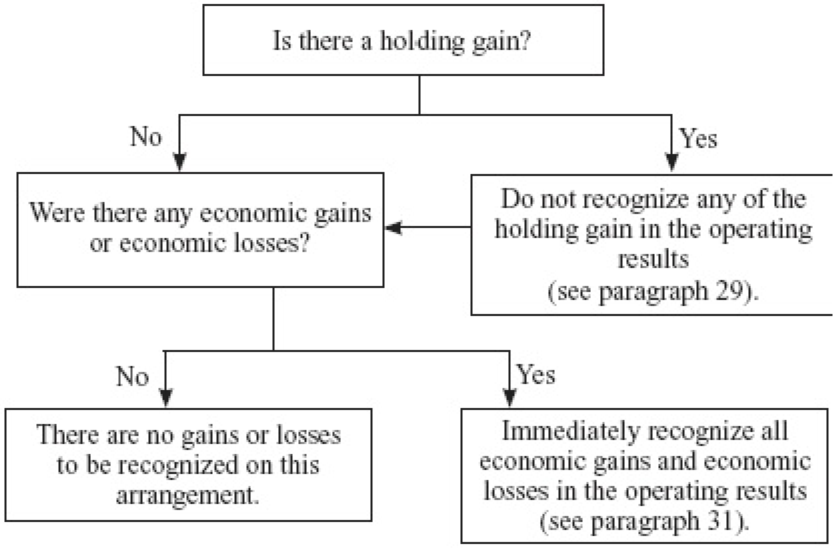
APPENDIX A — DECISION TREES

These decision trees are illustrative only. While illustrative, this Appendix is a primary source of GAAP, as identified in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, paragraph PS 1150.03(d)(iii).

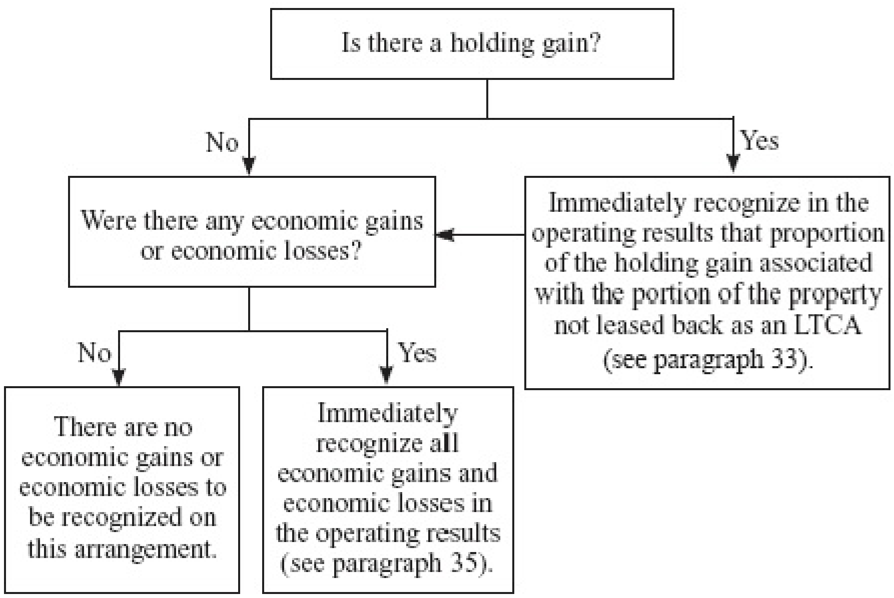
DECISION TREE 1 — DETERMINING TREATMENT OF AN LTCA OR OPERATING LEASE



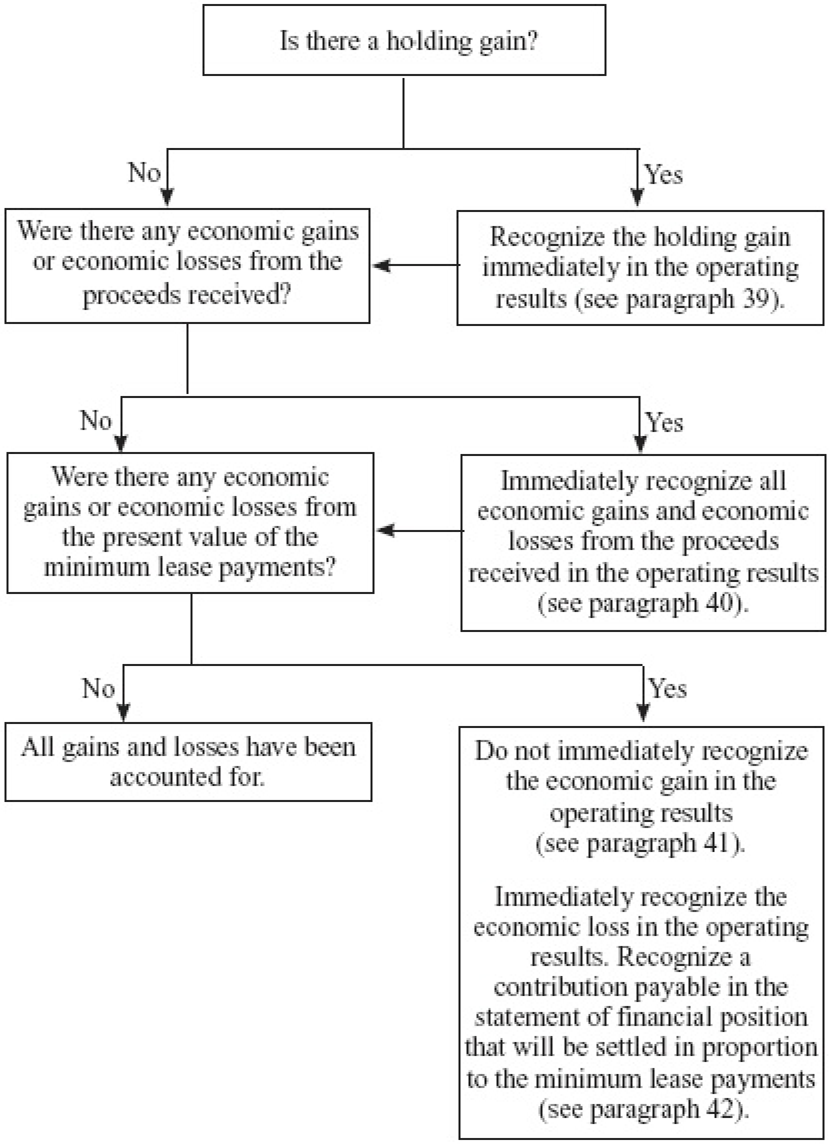
DECISION TREE 2 — TREATMENT OF GAINS AND LOSSES ON SALE AND 100 PERCENT LEASEBACK AS AN LTCA



DECISION TREE 3 — TREATMENT OF GAINS AND LOSSES ON SALE AND LESS THAN 100 PERCENT LEASEBACK AS AN LTCA



DECISION TREE 4 — TREATMENT OF GAINS AND LOSSES ON SALE-LEASEBACK AS AN OPERATING LEASE WITHOUT INTERRELATIONSHIP



APPENDIX B

ILLUSTRATIVE EXAMPLES

The following examples have been prepared to illustrate how the guidance in this Guideline might be implemented when a government enters into a sale-leaseback transaction.

The examples are illustrative only and matters of principle relating to particular situations should be decided in the context of the Guideline. They are not intended to indicate preferred formats nor to prescribe standardized note disclosure, as variations in format and wording will be necessary to meet the requirements of differing circumstances. While illustrative, this Appendix is a primary source of GAAP, as identified in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, paragraph PS 1150.03(d)(iii).

For ease of presentation, selections are made from accounting alternatives permitted by the Guideline.

In reviewing the examples, it will be helpful to consider the following:

(a) Despite the probability of occurrence, a broad range of examples is presented to assist with understanding this Guideline.

(b) The terminology of holding gains, economic gains and economic losses is used in the financial statements for illustrative purposes only.

(c) In the statement of financial position, the impact on the accumulated surplus or deficit may not be the same as the impact on net financial assets or net financial liabilities. [Former description to the Illustrative Examples for

PSG-5, amended by FINANCIAL STATEMENT PRESENTATION, Section PS 1202, retained in Archived Pronouncements.]

(d) The proceeds received and the minimum lease payments are not bundled with other contractual arrangements (except in Example 1).

Summary of examples

Example 1 — Bundled contractual arrangement

Example 2 — Sale and 100 percent leaseback as an LTCA

Example 3 — Sale and less than 100 percent leaseback as an LTCA

Example 4 — Sale-leaseback as an operating lease without interrelationship

Example 5 — Sale-leaseback as an operating lease with interrelationship

Example 1 — Bundled contractual arrangement

The government owns a historic building that is of cultural significance to the community. The government wishes to refurbish and restore the building while at the same time maintaining an element of continued use. The government enters into a sale-leaseback transaction, leasing back a portion of the building. The lessor specializes in building restoration.

The terms and conditions of the arrangement result in the government agreeing to the following:

Proceeds provided by the purchaser / lessor	$150,000
Total lease payments	80,000

In order to account for the substance of the transaction, this Guideline requires a review of the entire transaction to determine if there are any other events and arrangements, possibly not directly related to the transaction, that when viewed in its entirety would cause the transaction to be interpreted differently. Closer examination of the transaction reveals the proceeds provided by the lessor and total lease payments as follows:

Proceeds provided by the purchaser / lessor

Lease incentive payment from lessor	$ 10,000
Proceeds attributable to the property	140,000
	$150,000
	=======

Total lease payments

Insurance contribution (at fair value)	$15,000
Refurbishment contribution (at fair value)	25,000
Payments attributable to using the property	40,000
	$80,000
	======

For the purposes of this Guideline, proceeds received would be $140,000, and the present value of the minimum lease payments would be $40,000. Having unbundled the transaction, these amounts would then be accounted for as discussed in Example 4, Situation 4.III (assuming the same set of circumstances). All other items that were bundled into this transaction would be accounted for according to their economic substance.

Example 2 — Sale and 100 percent leaseback as an LTCA

SITUATION 2.I
Entire Transaction Occurs at Fair Value

Carrying amount of property (CA)	$100,000
Proceeds received	150,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	150,000
Fair value of the lease (FVL)	150,000
Holding gain (FV – CA)	50,000
Economic gains / losses	—

This is a financing transaction and not a sale of the property. The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has agreed to repay $150,000 (at the FVL). Nothing has changed with respect to the government's control over the property — in substance it has secured a loan.

Because nothing has changed with respect to the government's control over the property, the LTCA would be recognized at the same carrying amount as it was prior to entering into the transaction, with the holding gain not recognized in the operating results. Given that the proceeds received and the PVMLP equal their respective fair values, there are no economic gains or losses associated with this transaction, resulting in no effect on the operating results or the accumulated surplus of the government.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$150,000
Building	100,000	100,000
Total assets	100,000	250,000
Liabilities		
Lease liability	$ —	$150,000
Total liabilities	0	150,000
Accumulated surplus	$100,000	$100,000
	=======	=======

Statement of Operations

	After
Revenues	
Total revenues	$ —
Expenses	
Total expenses	—
Annual surplus / (deficit)	$ 0
	===

SITUATION 2.II
Entire Transaction Occurs at Less than Fair Value

Carrying amount of property (CA)	$100,000
Proceeds received	130,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	130,000
Fair value of the lease (FVL)	150,000
Holding gain (FV – CA)	50,000
Economic loss from proceeds received (compared to FV)	(20,000)
Economic gain from PVMLP (compared to FVL)	20,000

This is a financing transaction and not a sale of the property. The government has received proceeds of $130,000 ($20,000 less than the FV), and in turn has agreed to repay $130,000 ($20,000 less than the FVL). Nothing has changed with respect to the government's control over the property — in substance it has secured a loan.

Because nothing has changed with respect to the government's control over the property, the LTCA would be recognized at the same carrying amount as it was prior to entering into the transaction, with the holding gain not recognized in the operating results. The economic loss of $20,000 from the proceeds received and the compensating economic gain of $20,000 from the PVMLP would be recognized immediately in the operating results. This produces operating results of nil and no change in the accumulated surplus.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$130,000
Building	100,000	100,000
Total assets	100,000	230,000
Liabilities		
Lease liability	$ —	$130,000
Total liabilities	0	130,000
Accumulated surplus	$100,000	$100,000
	=======	=======

Statement of Operations

	After
Revenues	
Economic gain from PVMLP	$20,000
Total revenues	20,000
Expenses	
Economic loss from proceeds received	$20,000
Total expenses	20,000
Annual surplus / (deficit)	$ 0
	======

SITUATION 2.III
Proceeds Received Are Greater than Fair Value, with the Present Value of the Minimum Lease Payments at the Fair Value of the Lease

Carrying amount of property (CA)	$100,000
Proceeds received	170,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	150,000
Fair value of the lease (FVL)	150,000
Holding gain (FV – CA)	50,000
Economic gain from proceeds received (compared to FV)	20,000

This is a financing transaction and not a sale of the property. The government has received proceeds of $170,000 ($20,000 greater than the FV), and in turn has agreed to repay $150,000 (at the FVL). Nothing has changed with respect to the government's control over the property — in substance it has secured a loan.

Because nothing has changed with respect to the government's control over the property, the LTCA would be recognized at the same carrying amount as it was prior to entering into the transaction, with the holding gain not recognized in the operating results. The economic gain of $20,000 from the proceeds received would be recognized immediately in the operating results. This produces an operating surplus of $20,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$170,000
Building	100,000	100,000
Total assets	100,000	270,000
Liabilities		
Lease liability	$ —	$150,000
Total liabilities	0	150,000
Accumulated surplus	$100,000	$120,000
	=======	=======

Statement of Operations

	After
Revenues	
Economic gain from proceeds received	$20,000
Total revenues	20,000
Expenses	
Total expenses	$ —
Annual surplus	$20,000
	======

SITUATION 2.IV
Present Value of the Minimum Lease Payments Is Greater than the Fair Value of the Lease, with the Proceeds Received at Fair Value

Carrying amount of property (CA)	$100,000
Proceeds received	150,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	170,000
Fair value of the lease (FVL)	150,000
Holding gain (FV – CA)	50,000
Economic loss from PVMLP (compared to FVL)	(20,000)

This is a financing transaction and not a sale of the property. The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has agreed to repay a larger amount of $170,000 ($20,000 greater than the FVL). Nothing has changed with respect to the government's control over the property — in substance it has secured a loan.

Because nothing has changed with respect to the government's control over the property, the LTCA would be recognized at the same carrying amount as it was prior to entering into the transaction, with the holding gain not recognized in the operating results. The economic loss of $20,000 from the PVMLP is recognized immediately in the operating results. This produces an operating deficit of $20,000 and a decrease in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$150,000
Building	100,000	100,000
Total assets	100,000	250,000
Liabilities		
Lease liability	$ —	$170,000
Total liabilities	0	170,000
Accumulated surplus	$100,000	$ 80,000
	=======	======

Statement of Operations

	After
Revenues	
Total revenues	$ —
Expenses	
Economic loss from PVMLP	20,000
Total expenses	20,000
Annual deficit	$(20,000)
	=======

Example 3 — Sale and less than 100 percent leaseback as an LTCA

SITUATION 3.I
60 percent Leaseback — Entire Transaction Occurs at Fair Value — Positive Net Impact

		60%	40%
Carrying amount of property (CA)	$100,000	$60,000	$40,000
Proceeds received	150,000	N/A	N/A
Fair value of property (FV)	150,000	90,000	60,000
Present value of the minimum lease payments (PVMLP)	90,000	90,000	N/A
Fair value of the lease (FVL)	90,000	90,000	N/A
Holding gain (FV – CA)	50,000	30,000	20,000
Economic gains / losses	—	—	—

Two transactions are occurring:

(a) a financing transaction using 60 percent of the property as collateral; and

(b) the remaining 40 percent of the property being sold.

The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has agreed to repay $90,000 (at the FVL). In substance, nothing has changed with respect to the government's control over the 60 percent of the property leased back as an LTCA. However, the government has relinquished control over the remaining 40 percent of the property as it has been sold.

Because nothing has changed with respect to the government's control over 60 percent of the property, the LTCA would be recognized at 60 percent of its carrying amount prior to entering into the transaction, with no recognition of the associated holding gain in the operating results. The remaining 40 percent of the holding gain is recognized in the operating results as it relates to the sale of the 40 percent.

Given that the proceeds received and the PVMLP both equal their respective fair values, there are no economic gains or losses associated with this transaction. This produces an operating surplus of $20,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$ 150,000
Building	100,000	60,000
Total assets	100,000	210,000
Liabilities		
Lease liability	$ —	$ 90,000
Total liabilities	0	90,000
Accumulated surplus	$100,000	$120,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain — portion sold	$20,000
Total revenues	20,000
Expenses	
Total expenses	$ —
Annual surplus	$20,000
	======

SITUATION 3.II
60 percent Leaseback — Proceeds Received Are Less than Fair Value, with the Present Value of the Minimum Lease Payments at the Fair Value of the Lease — Nil Net Impact

		60%	40%
Carrying amount of property (CA)	$100,000	$60,000	$40,000
Proceeds received	130,000	N/A	N/A
Fair value of property (FV)	150,000	90,000	60,000
Present value of the minimum lease payments (PVMLP)	90,000	90,000	N/A
Fair value of the lease (FVL)	90,000	90,000	N/A
Holding gain (FV – CA)	50,000	30,000	20,000

Economic loss from proceeds received (compared to FV)	(20,000)	N/A	N/A

Two transactions are occurring:

(a) a financing transaction using 60 percent of the property as collateral; and

(b) the remaining 40 percent of the property being sold.

The government has received proceeds of $130,000 ($20,000 less than the FV), and in turn has agreed to repay $90,000 (at the FVL). In substance, nothing has changed with respect to the government's control over the 60 percent of the property leased back as an LTCA. However, the government has relinquished control over the remaining 40 percent of the property as it has been sold.

Because nothing has changed with respect to the government's control over 60 percent of the property, the LTCA would be recognized at 60 percent of its carrying amount prior to entering into the transaction, with no recognition of the associated holding gain in the operating results. The remaining 40 percent of the holding gain is recognized in the operating results as it relates to the sale of the 40 percent.

The economic loss of $20,000 on the proceeds received is recognized immediately in the operating results. The economic loss of $20,000 offsets the holding gain of $20,000, producing operating results of nil and the accumulated surplus remaining the same.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$130,000
Building	100,000	60,000
Total assets	100,000	190,000
Liabilities		
Lease liability	$ —	$ 90,000
Total liabilities	0	90,000
Accumulated surplus	$100,000	$100,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain — portion sold	$20,000
Total revenues	20,000
Expenses	
Economic loss from proceeds received	$20,000
Total expenses	20,000
Annual surplus / (deficit)	$ 0
	======

SITUATION 3.III
60 percent Leaseback — Proceeds Received Are Less than Fair Value, with the Present Value of the Minimum Lease Payments at the Fair Value of the Lease — Positive Net Impact

	60%	40%

Carrying amount of property (CA)	$100,000	$60,000	$40,000
Proceeds received	140,000	N/A	N/A
Fair value of property (FV)	150,000	90,000	60,000
Present value of the minimum lease payments (PVMLP)	90,000	90,000	N/A
Fair value of the lease (FVL)	90,000	90,000	N/A
Holding gain (FV – CA)	50,000	30,000	20,000
Economic loss from proceeds received (compared to FV)	(10,000)	N/A	N/A

Two transactions are occurring:

(a) a financing transaction using 60 percent of the property as collateral; and

(b) the remaining 40 percent of the property being sold.

The government has received proceeds of $140,000 ($10,000 less than the FV), and in turn has agreed to repay $90,000 (at the FVL). In substance, nothing has changed with respect to the government's control over the 60 percent of the property leased back as an LTCA. However, the government has relinquished control over the remaining 40 percent of the property as it has been sold.

Because nothing has changed with respect to the government's control over 60 percent of the property, the LTCA would be recognized at 60 percent of its carrying amount prior to entering into the transaction, with no recognition of the associated holding gain in the operating results. The remaining 40 percent of the holding gain is recognized in the operating results as it relates to the sale of the 40 percent.

The economic loss of $10,000 on proceeds received is recognized immediately in the operating results. The economic loss of $10,000 against the $20,000 holding gain produces an operating surplus of $10,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$140,000
Building	100,000	60,000
Total assets	100,000	200,000
Liabilities		
Lease liability	$ —	$ 90,000
Total liabilities	0	90,000
Accumulated surplus	$100,000	$110,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain — portion sold	$20,000
Total revenues	20,000
Expenses	
Economic loss from proceeds received	$10,000
Total expenses	10,000

Annual surplus	$10,000
	======

SITUATION 3.IV
60 percent Leaseback — Proceeds Received Are Less than Fair Value, with the Present Value of the Minimum Lease Payments at the Fair Value of the Lease — Negative Net Impact

		60%	40%
Carrying amount of property (CA)	$100,000	$60,000	$40,000
Proceeds received	120,000	N/A	N/A
Fair value of property (FV)	150,000	90,000	60,000
Present value of the minimum lease payments (PVMLP)	90,000	90,000	N/A
Fair value of the lease (FVL)	90,000	90,000	N/A
Holding gain (FV – CA)	50,000	30,000	20,000
Economic loss from proceeds received (compared to FV)	(30,000)	N/A	N/A

Two transactions are occurring:

(a) a financing transaction using 60 percent of the property as collateral; and

(b) the remaining 40 percent of the property being sold.

The government has received proceeds of $120,000 ($30,000 less than the FV), and in turn has agreed to repay $90,000 (at the FVL). In substance, nothing has changed with respect to the government's control over the 60 percent of the property leased back as an LTCA. However, the government has relinquished control over the remaining 40 percent of the property as it has been sold.

Because nothing has changed with respect to the government's control over 60 percent of the property, the LTCA would be recognized at 60 percent of its carrying amount prior to entering into the transaction, with no recognition of the associated holding gain in the operating results. The remaining 40 percent of the holding gain is recognized in the operating results as it relates to the sale of the 40 percent.

The economic loss of $30,000 on proceeds received is recognized immediately in the operating results. The economic loss of $30,000 against the holding gain of $20,000 produces an operating deficit of $10,000, decreasing the accumulated surplus by the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$120,000
Building	100,000	60,000
Total assets	100,000	180,000
Liabilities		
Lease liability	$ —	$ 90,000
Total liabilities	0	90,000
Accumulated surplus	$100,000	$90,000
	=======	======

Statement of Operations

	After

Revenues	
Holding gain — portion sold	$ 20,000
Total revenues	20,000
Expenses	
Economic loss from proceeds received	$ 30,000
Total expenses	30,000
Annual deficit	$(10,000)
	=======

SITUATION 3.V
60 percent Leaseback — Proceeds Received at Fair Value, with the Present Value of the Minimum Lease Payments at Greater than the Fair Value of the Lease — Nil Net Impact

		60%	40%
Carrying amount of property (CA)	$100,000	$60,000	$40,000
Proceeds received	150,000	N/A	N/A
Fair value of property (FV)	150,000	90,000	60,000
Present value of the minimum lease payments (PVMLP)	110,000	110,000	N/A
Fair value of the lease (FVL)	90,000	90,000	N/A
Holding gain (FV – CA)	50,000	30,000	20,000
Economic loss from PVMLP (compared to FVL)	(20,000)	N/A	N/A

Two transactions are occurring:

(a) a financing transaction using 60 percent of the property as collateral; and

(b) the remaining 40 percent of the property being sold.

The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has agreed to repay $110,000 ($20,000 greater than the FVL). In substance, nothing has changed with respect to the government's control over the 60 percent of the property leased back as an LTCA. However, the government has relinquished control over the remaining 40 percent of the property as it has been sold.

Because nothing has changed with respect to the government's control over 60 percent of the property, the LTCA would be recognized at 60 percent of its carrying amount prior to entering into the transaction, with no recognition of the associated holding gain in the operating results. The remaining 40 percent of the holding gain is recognized in the operating results as it relates to the sale of the 40 percent.

The economic loss of $20,000 on the PVMLP is recognized immediately in the operating results. The economic loss of $20,000 offsets the holding gain of $20,000, producing operating results of nil and the accumulated surplus of the government remaining the same.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$150,000
Building	100,000	60,000
Total assets	100,000	210,000
Liabilities		
Lease liability	$ —	$110,000

Total liabilities	0	110,000
Accumulated surplus	$100,000	$100,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain — portion sold	$20,000
Total revenues	20,000
Expenses	
Economic loss from PVMLP	$20,000
Total expenses	20,000
Annual surplus / (deficit)	$ 0
	======

Example 4 — Sale-leaseback as an operating lease without interrelationship

SITUATION 4.I
Entire Transaction Occurs at Fair Value

Carrying amount of property (CA)	$100,000
Proceeds received	150,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	40,000
Fair value of the lease (FVL)	40,000
Holding gain (FV – CA)	50,000
Economic gain / loss	—

The government no longer has control over the property — this is a sale. The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has entered into an operating lease (at the FVL). Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses.

The holding gain is recognized in the operating results as it relates to the sale of the property. Given that the proceeds received and the PVMLP both equal their respective fair values, there are no economic gains / losses associated with this transaction. This produces an operating surplus of $50,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$150,000
Building	100,000	—
Total assets	100,000	150,000
Liabilities		
Total liabilities	$ —	$ —

Accumulated surplus	$100,000	$150,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000
Total revenues	50,000
Expenses	
Total expenses	$ —
Annual surplus	$50,000
	======

SITUATION 4.II
Proceeds Received Are Greater than Fair Value, with the Present Value of the Minimum Lease Payments at the Fair Value of the Lease

Carrying amount of property (CA)	$100,000
Proceeds received	170,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	40,000
Fair value of the lease (FVL)	40,000
Holding gain (FV – CA)	50,000
Economic gain from proceeds received (compared to FV)	20,000

The government no longer has control over the property — this is a sale. The government has received proceeds of $170,000 ($20,000 greater than the FV), and in turn has entered into an operating lease (at the FVL) resulting in an economically advantageous arrangement for the government. Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses.

The holding gain is recognized in the operating results as it relates to the sale of the property. The economic gain of $20,000 from the proceeds received is recognized immediately in the operating results as it is realized. This produces an operating surplus of $70,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$170,000
Building	100,000	—
Total assets	100,000	170,000
Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$100,000	$170,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000
Economic gain from proceeds received	20,000
Total revenues	70,000
Expenses	
Total expenses	$ —
Annual surplus	$70,000
	======

SITUATION 4.III
Proceeds Received Are Less than Fair Value, with the Present Value of the Minimum Lease Payments at the Fair Value of the Lease

Carrying amount of property (CA)	$100,000
Proceeds received	140,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	40,000
Fair value of the lease (FVL)	40,000
Holding gain (FV – CA)	50,000
Economic loss from proceeds received (compared to FV)	(10,000)

The government no longer has control over the property — this is a sale. The government has received proceeds of $140,000 ($10,000 less than the FV), and in turn has entered into an operating lease (at the FVL) resulting in an uneconomic arrangement for the government. Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses.

The holding gain is recognized in the operating results as it relates to the sale of the property. The economic loss of $10,000 from the proceeds received is recognized immediately in the operating results. This produces an operating surplus of $40,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$140,000
Building	100,000	—
Total assets	100,000	140,000
Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$100,000	$140,000
	=======	=======

Statement of Operations

	After
Revenues	

Holding gain	$50,000
Total revenues	50,000
Expenses	
Economic loss from proceeds received	$10,000
Total expenses	10,000
Annual surplus	$40,000
	======

SITUATION 4.IV
Present Value of the Minimum Lease Payments Is Less than the Fair Value of the Lease, with the Proceeds Received at Fair Value

Carrying amount of property (CA)	$100,000
Proceeds received	150,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	40,000
Fair value of the lease (FVL)	50,000
Holding gain (FV – CA)	50,000
Economic gain from PVMLP (compared to FVL)	10,000

The government no longer has control over the property — this is a sale. The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has entered into an operating lease (at less than the FVL) resulting in an economically advantageous arrangement for the government. Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses.

The holding gain is recognized in the operating results as it relates to the sale of the property. The economic gain of $10,000 from the PVMLP is not recognized immediately in the operating results, because it is not realized. Such gains will be recognized as they are realized over the life of the lease by virtue of the government paying lower than fair value rent and recognizing this lower amount as expense. This produces an operating surplus of $50,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$150,000
Building	100,000	—
Total assets	100,000	150,000
Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$100,000	$150,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000

Total revenues	50,000
Expenses	
Total expenses	$ —
Annual surplus	$50,000
	======

SITUATION 4.V
Present Value of the Minimum Lease Payments Is Greater than the Fair Value of the Lease, with Proceeds Received at Fair Value

Carrying amount of property (CA)	$100,000
Proceeds received	150,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	60,000
Fair value of the lease (FVL)	40,000
Holding gain (FV – CA)	50,000
Economic loss from PVMLP (compared to FVL)	(20,000)

The government no longer has control over the property — this is a sale. The government has received proceeds of $150,000 (equal to 100 percent of the FV), and in turn has entered into an operating lease (at greater than the FVL) resulting in an uneconomic arrangement for the government.

In substance, the economic loss on the PVMLP represents a contribution to the lessor payable over the term of the lease. Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses.

The holding gain is recognized in the operating results as it relates to the sale of the property. The economic loss of $20,000 on the PVMLP is recognized immediately in the operating results with a corresponding "contribution payable" (liability). The liability is settled in proportion to the minimum lease payments. Initial recognition of the transaction produces an operating surplus of $30,000 and an increase in the accumulated surplus of the same amount.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$150,000
Building	100,000	—
Total assets	100,000	150,000
Liabilities		
Contribution payable	$ —	$ 20,000
Total liabilities	0	20,000
Accumulated surplus	$100,000	$130,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000

Total revenues	50,000
Expenses	
Economic loss from PVMLP	$20,000
Total expenses	20,000
Annual surplus	$30,000
	======

The lease is for a 10-year term with lease payments spread equally over this term.

One year after inception, the first lease payment of $6,000 is made. Lease expense is recognized at its fair value ($4,000) and the contribution payable is reduced by the excess of the lease payment over the fair value of the lease expense ($2,000). This results in an operating deficit of $4,000 and a decrease in the accumulated surplus of the same amount.

Statement of Financial Position — One Year Later

	Before	After
Assets		
Cash	$150,000	$144,000
Total assets	150,000	144,000
Liabilities		
Contribution payable	$ 20,000	$ 18,000
Total liabilities	20,000	18,000
Accumulated surplus	$130,000	$126,000
	=======	=======

Statement of Operations — One Year Later

	After
Revenues	
Total revenues	$ —
Expenses	
Lease expense	$ 4,000
Total expenses	4,000
Annual deficit	$(4,000)
	======

Example 5 — Sale-leaseback as an operating lease with interrelationship

SITUATION 5.I
Proceeds Received and the Present Value of the Minimum Lease Payments Are Both Less than their Fair Values by the Same Amount — Prepaid Non-Financial Asset

Carrying amount of property (CA)	$100,000
Proceeds received	130,000
Fair value of property (FV)	150,000

Present value of the minimum lease payments (PVMLP)	40,000
Fair value of the lease (FVL)	60,000
Holding gain (FV – CA)	50,000
Economic loss from proceeds received (compared to FV)	(20,000)
Economic gain from PVMLP (compared to FVL)	20,000

The government no longer has control over the property — this is a sale. The government has received proceeds of $130,000 ($20,000 less than the FV), and in turn has entered into an operating lease (at less than the FVL). Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses. Because there is both an economic gain and a compensating economic loss, this transaction has an element of interrelationship. Further, because they offset exactly, this transaction has occurred at fair value.

The holding gain is recognized in the operating results as it relates to the sale of the property.

The economic loss of $20,000 from the proceeds received is artificial, as it is compensated for by the economic gain of $20,000 on the PVMLP. These artificial economic gains and losses do not affect the statement of operations. The compensatory relationship between them results in a form of prepayment by the government to the lessor, necessitating lower rentals over the lease term. Initial recognition of the transaction produces an operating surplus of $50,000 and an increase in the accumulated surplus of the same amount. A prepayment of $20,000 is also recognized in the statement of financial position as a non-financial asset, which is settled in proportion to the minimum lease payments.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$130,000
Building	100,000	—
Prepayment	—	20,000
Total assets	100,000	150,000
Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$100,000	$150,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000
Total revenues	50,000
Expenses	
Total expenses	$ —
Annual surplus	$50,000
	======

The lease is for a 10-year term with lease payments spread equally over this term.

One year after inception, the first lease payment of $4,000 is made. Lease expense is recognized at its fair value ($6,000) and the prepayment is reduced by the excess of the fair value of the lease expense over the lease payment ($2,000). This results in an operating deficit of $6,000 and a decrease in the accumulated surplus of the same amount.

Statement of Financial Position — One Year Later

	Before	After
Assets		
Cash	$130,000	$126,000
Prepayment	20,000	18,000
Total assets	150,000	144,000
Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$150,000	$144,000
	=======	=======

Statement of Operations — One Year Later

	After
Revenues	
Total revenues	$ —
Expenses	
Lease expense	$ 6,000
Total expenses	6,000
Annual deficit	$(6,000)
	======

SITUATION 5.II
Proceeds Received and the Present Value of the Minimum Lease Payments Are Both Greater than Their Fair Values by the Same Amount — Loan Liability

Carrying amount of property (CA)	$100,000
Proceeds received	170,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	60,000
Fair value of the lease (FVL)	40,000
Holding gain (FV – CA)	50,000
Economic gain on proceeds received (compared to FV)	20,000
Economic loss on PVMLP (compared to FVL)	(20,000)

The government no longer has control over the property — this is a sale. The government has received proceeds of $170,000 ($20,000 greater than the FV), and in turn has entered into an operating lease (at greater than the FVL). Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses. Because there is both an economic gain and a compensating economic loss, this transaction has an element of interrelationship. Further, because they offset exactly, this transaction has occurred at fair value.

The holding gain is recognized in the operating results as it relates to the sale of the property.

The economic gain of $20,000 from the proceeds received is artificial, as it is compensated for by the economic loss of $20,000 on the PVMLP. These artificial economic gains and losses do not affect the statement of operations. The compensatory relationship between them results in a form of financing by the lessor to the government necessitating repayment through higher lease payments over the term of the lease.

Initial recognition of the transaction produces an operating surplus of $50,000 and an increase in the accumulated surplus of the same amount. A $20,000 loan liability is also recognized in the statement of financial position, which is settled in proportion to the minimum lease payments.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$170,000
Building	100,000	—
Total assets	100,000	170,000
Liabilities		
Loan liability	$ —	$ 20,000
Total liabilities	0	20,000
Accumulated surplus	$100,000	$150,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000
Total revenues	50,000
Expenses	
Total expenses	—
Annual surplus	$50,000
	======

The lease is for a 10-year term with lease payments spread equally over this term.

One year after inception, the first lease payment of $6,000 is made. Lease expense is recognized at its fair value ($4,000) and the loan liability is reduced by the excess of the lease payment over the fair value of the lease expense ($2,000). This results in an operating deficit of $4,000 and a decrease in the accumulated surplus of the same amount.

Statement of Financial Position — One Year Later

	Before	After
Assets		
Cash	$170,000	$164,000
Total assets	170,000	164,000
Liabilities		
Loan liability	$ 20,000	$ 18,000
Total liabilities	20,000	18,000
Accumulated surplus	$150,000	$146,000
	=======	=======

Statement of Operations — One Year Later

	After
Revenues	
Total revenues	$ —
Expenses	
Lease expense	$ 4,000
Total expenses	4,000
Annual deficit	$(4,000)
	======

SITUATION 5.III
Proceeds Received and the Present Value of the Minimum Lease Payments Are Both Less than their Fair Values by Different Amounts — Prepaid Non-Financial Asset and Economic Gain

Carrying amount of property (CA)	$100,000
Proceeds received	120,000
Fair value of property (FV)	150,000
Present value of the minimum lease payments (PVMLP)	20,000
Fair value of the lease (FVL)	60,000
Holding gain (FV – CA)	50,000
Economic loss from proceeds received (compared to FV)	(30,000)
Economic gain from PVMLP (compared to FVL)	40,000

The government no longer has control over the property — this is a sale. The government has received proceeds of $120,000 ($30,000 less than the FV), and in turn has entered into an operating lease (at less than the FVL). Because this is an operating lease, the proportion of the property leased back is not relevant to determining the calculation of any economic gains / losses. In reality, because there is an economic gain and a partially compensating economic loss, this transaction has an element of interrelationship, even though the economic gain and loss are not equal. The financial statements would reflect this reality.

The holding gain is recognized in the operating results as it relates to the sale of the property.

The economic loss of $30,000 from the proceeds received is artificial, as it is offset by the economic gain of $40,000 on the PVMLP. To the extent they are compensatory, these artificial economic gains and losses do not affect the statement of operations. In this case, the relationship between them results in a form of prepayment by the government to the lessor of $30,000. The remaining $10,000 real economic gain from the PVMLP is not recognized immediately in the operating results, because it is not realized. It is recognized as it is realized over the life of the lease by virtue of the government paying lower than fair value rent and the lower amount being recognized as expense.

Initial recognition of the transaction produces an operating surplus of $50,000 and an increase in the accumulated surplus of the same amount. A $30,000 prepayment is also recognized in the statement of financial position as a non-financial asset, which is settled in proportion to the minimum lease payments.

Statement of Financial Position

	Before	After
Assets		
Cash	$ —	$120,000
Building	100,000	—
Prepayment	—	30,000
Total assets	100,000	150,000

Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$100,000	$150,000
	=======	=======

Statement of Operations

	After
Revenues	
Holding gain	$50,000
Total revenues	50,000
Expenses	
Total expenses	$ —
Annual surplus	$50,000
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The lease is for a 10-year term with lease payments spread equally over this term.

One year after inception, the first lease payment of $2,000 is made. The prepayment is reduced in proportion to the lease payment ($3,000) and lease expense is recognized at its fair value, reduced by the portion of the economic gain from the PVMLP that is now realized ($6,000 – $1,000 = $5,000). This results in an operating deficit of $5,000 and a decrease in the accumulated surplus of the same amount.

Statement of Financial Position — One Year Later

	Before	After
Assets		
Cash	$120,000	$118,000
Prepayment	30,000	27,000
Total assets	150,000	145,000
Liabilities		
Total liabilities	$ —	$ —
Accumulated surplus	$150,000	$145,000
	=======	=======

Statement of Operations — One Year Later

	After
Revenues	
Total revenues	$ —
Expenses	
Lease expense	5,000
Total expenses	5,000
Annual deficit	$(5,000)

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Footnotes

* Guideline revised February 2007, December 2022 and October 2023.