Basis for Conclusions on SIC Interpretation 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*

This Basis for Conclusions accompanies, but is not part of, SIC-27.

[The original text has been marked up to reflect the revision of IAS 39 in 2003 and subsequently the issue of IFRS 4: new text is underlined and deleted text is struck through. References to the Framework *are to IASC's* Framework for the Preparation and Presentation of Financial Statements*, adopted by the IASB in 2001. In September 2010 the IASB replaced the* Framework *with the* Conceptual Framework for Financial Reporting.*]*

12 Paragraph 9 of IAS 11 *Construction Contracts* requires a group of contracts to be treated as a single contract when the group of contracts is negotiated as a single package, the contracts are so closely interrelated that they are, in effect, part of a single project with an overall profit margin, and the contracts are performed concurrently or in a continuous sequence. In such a situation, a series of transactions that involve the legal form of a lease are linked and accounted for as one transaction, because the overall economic effect cannot be understood without reference to the series of transactions as a whole.

13 An agreement is accounted for as a lease in accordance with IAS 17 when it conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time. For information to represent faithfully the transactions it purports to represent, paragraph 35 of the *Framework*[1] indicates that it is necessary that transactions are accounted for and presented in accordance with their substance and economic reality, not merely their legal form.

14 When an Entity does not control the assets that will be used to satisfy the lease payment obligations, and is not obligated to pay the lease payments, it does not recognise the assets and lease payment obligations, because the definitions of an asset and a liability have not been met. This is different from the circumstance when an Entity controls the assets, is obligated to pay the lease payments, and then later transfers assets to a third party (including a trust). In that circumstance, the transfer of assets (sometimes called an 'in-substance' defeasance) does not by itself relieve the Entity of its primary obligation, in the absence of legal release. A financial asset and a financial liability, or a portion of either, are derecognised only when the requirements of paragraphs 15–37, 39–42, AG36–AG52 and AG57–AG63 of IAS 39 are met.

15 IFRS 4 provides guidance for recognising and measuring financial guarantees and similar instruments that provide for payments to be made if the debtor fails to make payments when due, if that contract transfers significant insurance risk to the issuer. Financial guarantee contracts that provide for payments to be made in response to changes in relation to a variable (sometimes referred to as an 'underlying') are subject to IAS 39.

1 superseded by Chapter 3 of the *Conceptual Framework*. References to the *Framework* are to IASC's *Framework for the Preparation and Presentation of Financial Statements*, adopted by the IASB in 2001. In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*.

16 IAS 18 addresses the accounting treatment of revenue. Paragraph 75 of the *Framework*[2] indicates that gains are no different in nature from revenue. Therefore, the requirements of IAS 18 apply by analogy or otherwise. Example 14(c) in the illustrative examples accompanying IAS 18 states that a fee earned on the execution of a significant act, which is much more significant than any other act, is recognised as income when the significant act has been completed. The example also indicates that it is necessary to distinguish between fees earned on completion of a significant act and fees related to future performance or risks retained.

2 now paragraph 4.30 of the *Conceptual Framework*