Audit and Governance Committee

PLYMOUTH CITY COUNCIL

Date of meeting:	16 September 2025
Title of Report:	**IFRS 16 Update Report**
Lead Member:	Councillor Mark Lowry (Cabinet Member for Finance)
Lead Strategic Director:	Ian Trisk-Grove (Service Director for Finance)
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Your Reference:	CH AG 200825
Key Decision:	No
Confidentiality:	Part I - Official

Purpose of Report

This report provides the Audit and Governance Committee with a summary of the key changes and implications of implementing International Financial Reporting Standard 16 Leases (IFRS 16 Leases).

Recommendations and Reasons

1. To note the contents of this report which contains details of the accounting implications in relation to the introduction of IFRS 16.

   Reason: This report provides the Audit & Governance Committee with a summary of the key changes and implications of implementing accounting standard IFRS 16 Leases.

Alternative options considered and rejected

1 None – the changes are mandatory as required by the CIPFA LASAAC Local Authority Accounting Code Board.

Relevance to the Corporate Plan and/or the Plymouth Plan

The Council's expenditure forms the basis on which the Corporate Plan can be delivered.

Implications for the Medium Term Financial Plan and Resource Implications:

The 2024/25 Statement of Accounts will have implications on the Medium-Term Financial Plan. The level of Working Balance and reserves will affect the level of funding available in future years and variations in service expenditure will also need to be reviewed to assess the effects.

Financial Risks

There will be no direct financial impact for the council as a result of the implementation of the new accounting standard IFRS 16 Leases. The council is already making lease payments for these 'right of use' assets. Adjustments will be required equal to the principal element of the existing lease repayments (which will be included in the annual minimum revenue provision (MRP) charge), and therefore there will be a net nil effect on the council's revenue budget. The number of assets on the council's balance sheet required to be valued at fair value on an annual basis in future years will increase. This may have an impact on costs associated with the independent valuations of the council's assets. It is not possible to assess the scale of this cost at this stage. The cost associated with acquiring these 'right of use' assets will qualify as capital expenditure and in turn will increase the councils CFR and impact on a number of Prudential Indicators.

Legal Implications

It is a requirement of the Local Government Act 2003 and the Accounts and Audit (England) Regulations 2015 that the council's Statement of Accounts is produced in accordance with proper accounting practices. Accounting standard IFRS 16 Leases, was issued by the International Accounting Standards Board in 2016 and was initially due to be implemented in April 2022 but due to issues in local audit, the CIPFA LASAAC Local Authority Accounting Code Board decided to defer mandatory implementation until 1 April 2024. This new standard supersedes the existing accounting standards for leases, International Accounting Standard 17 Leases (IAS 17).

Carbon Footprint (Environmental) Implications:

N/A

Other Implications: e.g. Health and Safety, Risk Management, Child Poverty:

N/A

Appendices

Ref.	**Title of Appendix**	**Exemption Paragraph Number** (if applicable) *If some/all of the information is confidential, you must indicate why it is not for publication by virtue of Part 1of Schedule 12A of the Local Government Act 1972 by ticking the relevant box.*						
		1	**2**	**3**	**4**	**5**	**6**	**7**
A	Accounting Policy							

Background papers:

**Add rows as required to box below*

Please list all unpublished, background papers relevant to the decision in the table below. Background papers are <u>unpublished</u> works, relied on to a material extent in preparing the report, which disclose facts or matters on which the report or an important part of the work is based.

Title of any background paper(s)	**Exemption Paragraph Number** (if applicable) *If some/all of the information is confidential, you must indicate why it is not for publication by virtue of Part 1of Schedule 12A of the Local Government Act 1972 by ticking the relevant box.*						
	1	**2**	**3**	**4**	**5**	**6**	**7**

Sign off:

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Originating Senior Leadership Team member: Oliver Woodhams											

Please confirm the Strategic Director(s) has agreed the report? Yes Date agreed: 01/09/2025
Cabinet Member approval: Cllr Mark Lowry approved by email Date approved: 22/08/2025

IFRS 16 – Leases

1. Background

1.1 IFRS 16 is a financial reporting standard issued by the International Accounting Standards Board (IASB) that primarily deals with lease accounting. The standard is not specifically tailored for the public sector; it applies to both public and private sector entities.

1.2 IFRS 16 introduces a significant change in how leases are accounted for by lessees (defined as the entities that obtain the right to use an asset for a specific period in exchange for lease payments).

1.3 Under the previous standard (IAS 17), lessees classified leases as either operating leases or finance leases, with only finance leases being recognised on the Balance Sheet. Under the new standard (IFRS 16), most leases are now recognised on the Balance Sheet, as the distinction between operating and finance leases is removed. This means lessees are required to recognise a lease liability representing their obligation to make lease payments and a corresponding 'right-of-use' asset, reflecting their right to use the leased asset. PFI liabilities are already on the Balance Sheet but are required to be remeasured under the standard.

1.4 The introduction of IFRS 16 aims to enhance transparency and comparability in financial reporting by bringing leases onto the Balance Sheet.

1.5 The standard was issued in January 2016 and was originally planned to be adopted by local authorities in 2020-21 but was initially deferred to 2021-22. Due to the pressures on finance teams during and after Covid-19, the adoption has been deferred further and was finally adopted for the 2024-25 Statement of Accounts.

1.6 The CIPFA Code of Practice contains specific guidance for local authorities which Finance have considered and incorporated into our accounting policies which are shown in Appendix A.

1.7 As per Note 32 in our 2024-25 accounts, the accounting change required new accounting treatment for approximately 100 assets, of which 59 are property or land, 8 are vehicles and 32 equipment. The Council also has 2 Private Finance Initiatives (PFI), one for the Energy from Waste Plant (EfW) and a separate one for schools.

2 Lease Identification

2.1 The Finance Team have considered all the types of assets which are potentially relevant and have made a judgement as to which assets are within scope of IFRS 16.

2.2 Property lease agreements, vehicles and large contracts were assessed as leases for the purposes of IFRS 16.

2.3 Easements, licences, licences to carry out works, agreements for a lease and office equipment (unless the individual asset value exceeds £5k) are excluded.

2.4 The Council uses a database system (Civica Property) to record information and store relevant documents such as title plans and lease agreements. This is the primary source of information on property leases.

2.5 It is possible for lease agreements to exist as part of a wider service delivery contract. To identify these, an annual review of the Council's Contracts Register was completed to identify any assets which are used in the delivery of a contract and meet the criteria for recognition as a lease under IFRS 16. No embedded leases were identified.

2.6 The Procurement Team are working with Finance to ensure that any new contract awards are assessed for the possibility of an embedded lease.

2.7 The finance team delivered training to all finance staff on the IFRS 16 lease requirements and provided guidance to all budget holders to assist with populating the required corporate returns. This provided some of the lease information used for IFRS 16.

3. Exemptions

3.1 The standard excludes leases which are considered 'short term'. Short term leases are defined as leases that have a lease term of 12 months or less at the commencement date of 1 April 2024. Therefore, leases which have a lease end date of 31 March 2025 or earlier are excluded. The only exception to this is for holding over leases (see Section 4).

3.2 The standard allows authorities to elect not to apply IFRS 16 lease accounting to leases where the underlying asset is of low value. The low value exemption applies to the asset value when it is new, irrespective of its age. The assessment is made on a lease-by-lease basis, and the assessment is on an absolute basis (therefore it applies to individual assets).

3.3 To ensure consistency between capital expenditure accounting for Property, Plant & Equipment, Finance have implemented a low value exemption limit of £10,000 for Property and £5,000 for Plant and Equipment. This ensures that the treatment of both owned and leased assets is presented in the same manner on the Balance Sheet.

3.4 Exempt leases are recognised as an expense over the lease term and are part of the Comprehensive Income & Expenditure Statement.

4. Holding Over Leases

4.1 A remaining lease term is required to calculate the lease liability under IFRS 16. For leases which are still within their lease term, the original lease dates as per the agreement can be used to determine the lease end of the lease period.

4.2 For the context of IFRS 16, holding over leases occur when a tenant stays, with consent from the landlord, in occupation of a lease beyond its expiry date, without renewing or entering a new agreement. The finance team have spoken to the relevant departments with leases that have expired to determine how long the property will continue to be in use.

5. Incremental Borrowing Rates

5.1 On transition, the CIPFA Code of Practice requires lease liabilities to be discounted using the Council's Incremental Borrowing Rate (IBR) at 1 April 2024.

5.2 The IBR is defined in the Code of Practice as the rate of interest a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.

5.3 Both central government and NHS bodies have been prescribed a rate to use. In the absence of this for local authorities, the Public Works Loan Board (PWLB) rates as at the beginning of April 2024 have been used. These rates are appropriate, current, and auditable as historic rates are published and are consistent with the approach in many other local authorities.

5.4 PWLB rates are not available for periods over 50 years. For any leases with a remaining term of over 50 years, the 50-year rate will be used.

6. Non-Commercial Leases

6.1 Leases which are non-commercial in nature (for example a building which the Council rents at a nominal or peppercorn rate) are treated as per the Code of Practice as a donated asset. It is considered that, in substance, the agreements mean the lessor donates the asset to the lessee.

6.2 This means that lease liabilities and right-of-use assets are still calculated in the same way, but the right-of-use asset is uplifted to its fair value. Valuations have been requested for these assets from the Council's internal valuers. The excess of the fair value over the cost of the right-of-use asset is credited as a gain in the surplus or deficit on the provision of services in the Comprehensive Income & Expenditure Statement but neutralised by statutory reversals through the Capital Adjustment Account.

7. Private Finance Initiatives

7.1 Private Finance Initiatives (PFI) are otherwise known as service concession arrangements. The accounting treatment is different when IFRS 16 is adopted.

7.2 The most significant difference between IFRS 16 and IAS 17 is in relation to the treatment for lessees. Under IAS 17, finance lease liabilities are not remeasured when the value of payments changes in a way which is not predetermined in the lease contract; for example, where payments are increased in line with an inflation index such as RPI or CPI. The increase in payments arising from indexation is treated in the same way as finance costs and simply expensed in the period to which the payment relates. This additional payment is known as 'contingent rent'.

Under IFRS 16 a different treatment is applied: where indexation or changes in a rate affect future payments, the lease liability is remeasured. Instead of expensing the additional (or reduced) payment, the net present value of future payments that comprise the liability is recalculated based on the revised level of payments.

7.3 The Council employed treasury management consultants Arlingclose to review the financial models for the PFI schemes. The overall impact of the changes to the models has meant a reduction in the lease liability of £11.076m for the EfW and an increase of £0.092m for the schools PFI. The overall net movement of £10.985m can be seen in note 31 Capital Financing Requirement to the Statement of Accounts.

8. Assessing the Lease Term

8.1 It is a requirement of IFRS 16 to assess the lease term where there are options to terminate or extend. Adjustments to lease terms are made based on judgements of the likelihood of the Council taking up any available options.

8.2 With the nature of services and requirements of the Council for property changing as a result of policy decisions in the Council. Finance will work with the property team to review lease options on an annual basis to ensure that the appropriate lease term is chosen based on the likelihood of them being continued. As this is a judgement at a fixed point in time, it is possible these options will need to be amended in the following financial year to best reflect the latest position.

9. Valuations

9.1 Valuations are not required for all right of use assets in the same way they are for freehold land and buildings. This is because the IFRS 16 guidance allows them to be measured at the value of the lease liability, adjusted for certain eligible costs and reductions.

9.2 However, where there are no provisions in the lease for market-based rent reviews or these have not been undertaken, or where the reviews are at periods of more than five years then a valuation is required.

9.3 In addition, a valuation must be obtained for any right of use assets under non-commercial leases (e.g. where we are paying a peppercorn rent).

9.4 This has increased the number of valuations we require from our internal valuer and will be an ongoing requirement to fulfil the obligations required from implementing IFRS 16.

9.5 Vehicle leases do not require valuations as there are not any significant changes to the lease terms and conditions during the lifetime of the lease agreement.

10. Lessor Accounting

10.1 The impact of IFRS 16 on lessor accounting is relatively unchanged compared to lessees.

10.2 Lessors must classify each lease as either a finance or operating lease. This will determine how the lease is accounted for.

10.3 The main change under lessor accounting is in relation to sub-leases. When a lessor sub-leases an asset, its classification will depend to an extent on the nature of the head lease.

11. Capital Financing Requirement (CFR)

11.1 The application of IFRS 16 will impact on statutory reporting and capital finance requirements for leased assets which refer to finance leases. The recognition of 'right of use' assets brings leases into the scope of the Prudential Code.

11.2 The Right of Use (ROU) asset becomes an asset on the balance sheet and an unfunded liability of the outstanding lease payments. This in turn increases the Authority's Capital Financing Requirement (CFR) and its authorised debt limits.

11.3 The cost of the 'right of use' asset serves a dual role. As well as providing the basis for the balance sheet entries it also constitutes capital expenditure, resulting in an increase to the Council's CFR.

11.4 An annual charge is posted to revenue for the use of assets through the council's depreciation policy. This policy will also apply to new 'right of use' assets brought onto the balance sheet. IFRS 16 requires these assets to be depreciated on a straight-line basis over the remaining useful life of the asset or the remaining years on the associated liability.

11.5 In line with statutory accounting requirements, depreciation is not a recognised charge to revenue and is reversed out of the general fund balance in the Movement in Reserves Statement (MiRS).

11.6 The CFR is reduced each year as resources are set aside to finance the capital expenditure either from capital receipts, grants and contributions or by annual charges of Minimum Revenue Provision (MRP). Whilst the CIPFA Code does not stipulate what the associated MRP charge should be for 'right of use' type assets, common treatment (as per the statutory guidance) is to set aside an amount by which the lease liability has been written down by payments in the year.

11.7 As the council is already making lease payments for these 'right of use' assets, an adjustment is made to remove these entries and replace them with MRP.

12 Conclusion

12.1 The Council has reviewed the policy requirements of IFRS 16 and the amended policies are shown in Appendix A.

12.2 The finance team were under pressure to implement IFRS 16 effectively due to the requirement under the Backstop Legislation to publish all outstanding Statement of Accounts for 2019/20 to 2022/23 by the 13 December 2024 and the 2023/24 Statement of Accounts by the 28 February 2025. As this was the first year for implementing the standard, the finance team are now revisiting the papers for IFRS 16 for 2024/25 to ensure compliance with the standard and to make sure that the correct valuations have been applied.

12.3 Going forward, the Finance team will work with the Procurement, Legal and Property teams to ensure that all potential leases are identified and reviewed and to embed the identification of leases into the processes within the Council.