Mae'r ddogfen hon ar gael yn Gymraeg **Agenda Item 12**

Report to	**Audit Committee**
Date	**27 March 2025**
Lead Officer	**Helen MacArthur, Assistant Chief Fire Officer**
Contact Officer	**Elgan Roberts, Head of Finance and Procurement**
Subject	**IFRS 16 Implementation for 2024/25**

PURPOSE OF REPORT

1 The purpose of this report is to provide Members of the North Wales Fire and Rescue Authority (the Authority) with an update about the necessary changes required for the implementation of International Financial Reporting Standards 16 (IFRS 16) for the 2024/25 annual accounts.

2 It also provides assurances regarding the steps being taken to ensure compliance and the impact on financial reporting.

EXECUTIVE SUMMARY

3 This paper outlines the necessary changes for the implementation of IFRS 16 for the 2024/25 annual accounts of local government associations, focusing on the recognition of leases on the balance sheet to enhance transparency and comparability.

4 The Audit Committee is requested to approve a deminimus level of £10,000 for lease recognition and the use of the borrowing cost as of 1 April 2024 or the commencement of the lease as the discount rate.

5 The paper provides assurances on compliance with IFRS 16 by the effective date, detailing the implementation plan, impact assessment, and stakeholder engagement to ensure a smooth transition and maintain the integrity of financial reporting.

RECOMMENDATIONS

6 It is recommended that Members:

i) Note the legislative change for IFRS 16;
ii) approve a deminimus level of £10k for lease recognition; and
iii) approve the discount rate to be based on the borrowing cost as of 1 April 2024, or at commencement of the lease.

Background

7 IFRS 16, which replaces International Accounting Standards 17 (IAS 17), introduces significant changes in lease accounting by requiring lessees to recognise most leases on the balance sheet. This includes the right-of-use (ROU) asset and the associated lease liability. The primary goal of this change is to enhance transparency and comparability in financial statements, addressing issues like off-balance sheet financing that were prevalent under IAS 17.

8 The implementation of IFRS 16 aims to reflect the economic reality of lease transactions more accurately. By recognising lease assets and liabilities, the standard provides a clearer picture of a company's financial commitments and resources. It also impacts key financial metrics, improving the assessment of a company's operating performance. Additionally, IFRS 16 aligns lease accounting with other standards, promoting consistency and reducing complexity in financial reporting.

Key Changes and Requirements

9 The principal change under IFRS 16 is the recognition of leases on the balance sheet. All leases, except for short-term leases and leases of low-value assets below a set deminimus, must be recognised on the balance sheet. This entails the recognition of a ROU asset and a corresponding lease liability. Lease liabilities are to be measured at the present value of lease payments over the lease term, using the interest rate implicit in the lease or, if not readily determinable, the lessee's incremental borrowing rate.

10 The introduction of ROU assets and lease liabilities will impact key financial metrics, such as debt ratios and net assets. Additionally, there will be changes in the presentation of the income statement, with lease expenses being replaced by depreciation of the ROU asset and interest on the lease liability. Enhanced disclosures are required to provide information about the nature, amount, timing, and uncertainty of cash flows arising from leases, including both qualitative and quantitative information about leasing activities.

Implementation Plan

11 To ensure readiness for IFRS 16, a comprehensive assessment is underway to identify all existing leases and ensure the completeness of lease data. Current systems and processes have also been evaluated to determine their capability to handle the new requirements. All necessary lease documentation will be gathered and validated to ensure accuracy, capturing all relevant lease terms such as renewal options and variable lease payments.

12 For 2024/25 IFRS 16 impact will be calculated using excel spreadsheets, however, for 2025/26 systems and processes will be reviewed and developed, to review capability within Tech One to manage lease accounting under IFRS 16 to automate compliance with the standard.

13 Training and guidance have been received by CIPFA, Audit Wales, and collaborative working between Welsh Local Government Organisations. This knowledge will be rolled-out and provided to finance and procurement teams on the new requirements and their implications, and the changes will continue to be communicated to all relevant stakeholders, including external auditors. Additional advice has and can be sought by CIPFA Finance Advisory Network (FAN) who provide support with technical accounting queries.

Identified Leases

14 As at the end of February 2025 the following leases have been identified:

Lease Description	Number of leases	Annual Value (£)
Buildings as Lessee	3	£224,000
Joint buildings	14	£0
Vehicles	62	£152,000
Printers/Franking Machines	21	<£10,000

15 IFRS 16 allows an organisation to determine its own deminimus level for lease recognition. Following internal review and in consultation with other Local government organisations and CIPFA, it is recommended that the authority proceed with a deminimus level of £10,000 for lease recognition.

16 Establishing a deminimus level of £10,000 ensures that only leases with a significant financial impact are recognised on the balance sheet. This threshold helps to streamline the accounting process by excluding minor leases that would otherwise require disproportionate administrative effort relative to their financial significance. It also aligns with the principle of materiality and is the same value as the Capital deminimus level, ensuring that financial statements remain clear and focused on the most relevant information to benefit the users.

17 Similarly, a discount rate needs to be determined to calculate the lease liability, it is recommended that the Authority proceed with a discount rate to be based on the Public Works Loan Board rate as of 1 April 2024.

18 Any lease that commenced following 1 April 2024, will need the discount rate to be calculated based on the rate implicit in the lease. If the interest rate implicit in the lease cannot be readily determined, the lessee should use their incremental borrowing rate.

19 The above approach provides a consistent and transparent method for calculating the present value of lease payments, aligning with the principles of IFRS 16 and ensuring comparability across financial periods.

Conclusion

20 The implementation of IFRS 16 represents a significant shift in lease accounting, requiring lessees to recognise most leases on the balance sheet. This change enhances transparency and comparability in financial statements, providing a clearer picture of a company's financial commitments and resources. The Authority has taken comprehensive steps to ensure compliance with IFRS 16, including setting a deminimus level for lease recognition and determining an appropriate discount rate. These measures, along with thorough training and stakeholder engagement, will facilitate a smooth transition to the new standard.

IMPLICATIONS

Wellbeing Objectives	None
Budget	Impact of IFRS 16 was captured during budget setting and revenue costs are budgeted.
Legal	Statutory requirement to comply with accounting standards.
Staffing	None.
Equalities / Human Rights / Welsh Language	None.
Risks	IFRS 16 changes create a material impact on the annual accounts.

Appendix 1: Definitions

Lease: A lease is a legal agreement between two parties: the lessor (owner) and the lessee (tenant). Under this contract, the lessor grants the lessee the right to use a property, asset, or service for a specified period in exchange for regular payments. Leases are commonly used for building, vehicles, and equipment.

Sublease: A sublease is an arrangement where the original tenant (lessee) of a property leases it out to a third party (sublessee). In this scenario, the original tenant becomes the sublessor. The sublease agreement allows the sublessee to use the property for a specified period, while the original lease between the landlord (lessor) and the original tenant remains in effect.

Right-of-use Asset (ROU Asset): A Right-of-Use (ROU) Asset is recorded when a company leases something for a set period and has control over its use, under IFRS 16. It applies to long-term leases of buildings, office space, vehicles, machinery, treating them similarly to owned assets. However, short-term leases (12 months or less), low-cost items like laptops, service contracts (e.g., software subscriptions), and leases bundled with services (where only the lease portion counts) are not considered ROU assets.

Lease Liability: A lease liability is a financial obligation that a lessee (the person or company renting an asset) must make lease payments over the lease term. This liability is calculated as the present value of the future lease payments, discounted to reflect the time value of money