

A Study On Analysis of Indian Leasing Finance Companies In 2019-20 As Per Indian Accounting Standard-17: Accounting For Leases

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Abstract

The leasing and finance industry is one of many service-centric industries. The leasing finance industry has changed incessantly, breeding new combinations of risk of both the known and the unknown types. This thesis is based on a case study of First Leasing Company of India Ltd in 2019-20.

In leasing finance industry, First Leasing Company of India Ltd is taken since it is one of the Top 100 Finance-Leasing & Hire Purchase Companies in India. This paper represents the implication of Ind. AS-17 in First Leasing Company of India Ltd for the year 2019-20. For this, operating lease & financial lease are considered. This paper indicates the difference among AS-19, IFRS/IAS-17 and US GAAP. For this purpose empirical research is made to study the accounting for lease in First Leasing Company of India Ltd for the year 2019-20. With the publicly available information through the annual reports of the respective companies during 2019-20, effectiveness in terms of substance and quality of reporting of lease are analyzed.

Keywords: Operating lease, Finance lease, lease finance company, lessor and the lessee.

Introduction

A lease is an agreement whereby the lessor 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. A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred. An operating lease is a lease other than a finance lease.

The commencement of the lease term is the date from which the lessee is entitled to exercise its right to use the leased asset. It is the date of initial recognition of the lease. The lease term is the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership. Because the transaction between a lessor and a lessee is based on a lease agreement between them, it is appropriate to use consistent definitions. The application of these definitions to the differing circumstances of the lessor and lessee may result in the same lease being classified differently by them. For example, this may be the case if the lessor benefits from a residual value guarantee provided by a party unrelated to the lessee.

This paper represents the implication of Ind. AS-17 in First Leasing Company of India Ltd for the year 2019-20. For this, operating lease & financial lease are considered. This paper indicates the difference among AS-19, IFRS/IAS-17 and US GAAP. For this purpose empirical research is made to study the accounting for lease in First Leasing Company of India Ltd for the year 2019-20. With the publicly available information through the annual reports of the respective companies during 2019-20, effectiveness in terms of substance and quality of reporting of lease are analyzed.

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Objective of the Study	<p>The objective of this Standard is to prescribe for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases. The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee.</p> <p>A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.</p>
Leases in the financial statements of lessees	<p>Lease payments under an operating lease shall be recognised as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.</p>
Operating Leases	
Finance Leases	<p>At the commencement of the lease term, lessees shall recognise finance leases as assets and liabilities in their balance sheets at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. The discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate shall be used. Any initial direct costs of the lessee are added to the amount recognised as an asset.</p> <p>Minimum lease payments shall be apportioned between the finance charge and the reduction of the outstanding liability. The finance charge shall be allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents shall be charged as expenses in the periods in which they are incurred</p> <p>A finance lease gives rise to depreciation expense for depreciable assets as well as finance expense for each accounting period. The depreciation policy for depreciable leased assets shall be consistent with that for depreciable assets that are owned, and the depreciation recognized shall be calculated in accordance with IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life.</p>
Leases in the financial statements of lessors	<p>Lessors shall present assets subject to operating leases in their balance sheets according to the nature of the asset. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets, and depreciation shall be calculated in accordance with IAS 16 and IAS 38. Lease income from operating leases shall be recognised in income on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished</p>
Operating Leases	
Finance Leases	<p>Lessors shall recognize assets held under a finance lease in their balance sheets and present them as a receivable at an amount equal to the net investment in the lease. The recognition of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease.</p> <p>Manufacturer or dealer lessors shall recognize selling profit or loss in the period, in accordance with the policy followed by the entity for outright sales. If artificially low rates of interest are quoted, selling profit shall be restricted to that which would apply if a market rate of interest were charged. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease shall be recognized as an expense when the selling profit is recognized.</p>

Sale and leaseback transactions

A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent because they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.

Analysis of Leasing Companies Finance, Investment & Leasing Companies in India

Top cities	Companies
Mumbai	315
Jaipur	254
Thiruvananthapuram	169
Kota	160
Bangalore	158
Delhi	155
Chennai	145
Ahmedabad	143
Vellore	128
Calicut	110
All listing of Finance, Investment & Leasing Companies in India	3469

List of some of the Top 100 Finance - Leasing & Hire Purchase Companies
(Net Profit as per the latest Profit & Loss Account available)

Company Name	Net Profit (Rs. cr)(2019-20)
Shriram TransFi	1,229.88
M&M Financial	463.11
Sundarmfin	295.23
Manappuram Fin	282.66
Bajaj Finance	246.96
Shriram City	240.59
SREI Infra	134.30
Magma Fincorp	114.43
First Leasing	70.87
Cholamandalam	62.18
LKP Finance	26.12

Akanksha Cell	15.59
Pioneer Invest	13.89
BCC Finance	10.39
Motor and Gen F	9.62
Ratnabali Cap	9.61
Consolidated Se	8.10
Sakthi Finance	7.94
Brescon Finance	5.87

(Source:<http://www.moneycontrol.com/stocks/top-companies-in-india/net-profit-bse/finance-leasing-hire-purchase.html>)

Difference among AS-19, IFRS/IAS-17 and US GAAP

1. Under AS-19 and IAS-17 classification of lease into finance lease or operating lease is a matter of judgement. However, under US GAAP classification of operating lease and capital lease is less judgmental, as there are detailed rules to decide the classification.
2. Under US GAAP finance lease is referred as capital lease and further classified as sales type lease or direct financing leases or leveraged leases for the purpose of accounting where there is no such further classification of finance lease as per AS-19 or IAS-17.
3. AS-19 is not applicable to lease agreement to use land whereas IAS-17 and US GAAP (FAS-13) is applicable to lease agreement to use land.
4. There is difference among US GAAP, AS-19 and IAS-17 regarding accounting treatment of sale and lease back transactions.

Similarities

The overall accounting for leases under US GAAP and IFRS and IAS 17 *Leases*, respectively) is similar, although US GAAP has more specific application guidance than IFRS.

Both focus on classifying leases as either capital (IAS 17 uses the term "finance") or operating, and both separately discuss lessee and lessor accounting.

Case Study

first leasing company of india limited

AS-19 - Leases: (1) Leases:

1. Aggregate of Minimum lease payments - Rs. 26,089.71 Lacs (Rs. 24,855.26 Lacs)
2. Net carrying amount - Rs. 19,991.96 Lacs (Rs. 16,787.44 Lacs)
3. Maturity pattern of Gross / Net receivable:

Particulars	Gross (Rs. in Lacs)	Net (Rs. in Lacs)
Not later than 1 year	8,125.20 (7,764.26)	6,268.56 (5,782.96)
later than 1 year and not later than 5 years	17,964.51 (15,443.57)	13,723.40 (11,750.19)
Later than 5 years	0.00 (1,647.43)	0.00 (1,619.65)

1. Unearned Finance income - Rs. 6,097.75 Lacs (Rs. 5,702.46 Lacs)
2. All initial direct costs are recognised as expenses in the Profit and Loss account at the inception of the lease.

3. Accumulated provision for uncollectible minimum lease payments receivable - Rs. 181.88 Lacs (Rs. 45.80 Lacs)

Stock on Hire

1. Aggregate of Minimum Hire Rentals - Rs 1,37,192.38 Lacs (Rs. 1,20,041.75 Lacs)
2. Net carrying amount - Rs. 1,23,145.02 Lacs (Rs. 1,09,420.66 Lacs)
3. Maturity pattern of Gross / Net receivable:

Particulars	Gross (Rs. in Lacs)	Net (Rs. in Lacs)
Not later than 1 year	54,856.57 (49,187.20)	48,414.74 (43,315.97)
later than 1 year and not later than 5 years	82,335.81 (70,854.55)	74,730.28 (66,104.69)
Later than 5 years	Nil	Nil

1. Unearned Finance income - Rs. 14,047.36 Lacs (Rs. 10,621.09 Lacs)
2. Accumulated provision for uncollectible hire payments receivable is Rs. 167.39 Lacs (Rs. 193.20 Lacs)

(Source: 37th Annual Report 2019-2020 of First Leasing Company of India Ltd.)

Conclusion

IAS-17 is studied to prescribe for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases. There is difference among AS-19, IFRS/IAS-17 and US GAAP. There are also similarities of leases under US GAAP and IFRS and IAS 17. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

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