**Type of Leases and Treatment in UNDP Books**

1. This section introduces prescriptive content regarding the different types of Leases for UNDP Country Offices (CO) a Project Office, Sub-Offices, Headquarters (HQs), Office, Out-Posted HQs Units (OHQ) and Policy Centers.

1. The section provides details on how the Leases will be recorded, managed and accounted for by UNDP. It also includes any other related sub-processes associated with the management of leases in line with relevant accounting and operational guidelines. The Leases may either relate to premises or equipment.

1. A **Lease** is “*an agreement whereby the lessor (landlord) conveys to the lessee (UNDP) in return for a payment or series of payments the right to use an asset for an agreed period of time*”.

1. A **Commercial Lease** is an exchange contract between UNDP and a private company, In exchange for the usage of the asset, the landlord/lessor receives a payment or series of payments. Commercial Leases are generally contracted for office space and, in certain cases, for different types of equipment.

1. UNDP has two main types of Leases: Operating Leases and Finance Leases.

1. The classification of a Lease as an Operating Lease or as a Finance Lease is important as the accounting methods are different. Note that the UNDP Standard Lease Agreement is an Operating Lease. An Operating Lease is not considered as an asset and payments to the landlord (Lessor) are accounted for as rent and are expensed.

1. In the rare case that UNDP has a lease agreement that qualifies as a Finance Lease, UNDP has to recognize that as an asset and a liability:

* 1. The asset represents the right to use the asset during the lease term, at the current value of the estimated minimum lease payments

* 1. The liability represents the minimum lease payments UNDP has to pay to the Landlord/Lessor.

1. This asset will be depreciated (i.e. expensed) over its useful life. If there is no reasonable certainty that UNDP will obtain ownership by the end of the lease term, the asset will be fully depreciated over the lease term or its useful life, whichever is the shorter. The accounting entries for a Finance Lease will be done by the GSSC, on behalf of the CO.

# Finance and Operating Leases

9. Under IPSAS there are two types of leases, finance leases and operating leases:

1. A **Finance Lease** is a capital lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred, even though UNDP does not hold legal title during the duration of the lease.

1. An **Operating Lease** is a lease other than a Finance Lease. For office space, a Lease that has been formulated and agreed following [UNDP’s Standard Lease Template](https://popp.undp.org/node/4571) will be an Operating Lease.

# Determination of Lease Type

1. To facilitate the determination of the type of Lease held by UNDP, all Leases must be submitted to the GSSC for its review. The request for Lease review will be submitted to the GSSC by the Premises Focal Points, via the [UNall Portal](https://undp.service-now.com/unall?id=esc_home), together with copies of the relevant supporting documentation (e.g. Lease agreement) uploaded with the submission. All original documentation must be properly filed at the respective office submitting the request.

1. The classification of a lease between Operating Lease and Finance Lease is important as the accounting methods are different. A Finance Lease is considered as an asset (Property) and a liability (amount due to a third party) is concurrently recorded. An Operating Lease is not considered to be an asset; and payments to the landlord are expensed and accounted for as rent.

# Financial Leases

1. Finance Leases are very rare in UNDP. A Finance Lease in UNDP is a lease which meets at least one of the following criteria:

* 1. Ownership of the asset is transferred to UNDP at the end of the lease term;

* 1. The lease contains a bargain purchase option to buy the equipment at less than fair market value (what a rational willing buyer and a rational willing seller would transact the item for in a competitive environment);

* 1. The lease term equals or exceeds 75 percentage of the asset's estimated useful life;

* 1. The present value of the lease payments equals or exceeds 90percentage of the total original cost of the equipment.

1. A Finance Lease is a Lease that substantially transfers all the risks and rewards incidental to ownership of a fixed asset. Title may or may not eventually be transferred. In determining whether a Lease is a Finance Lease, UNDP must examine the substance of the transaction rather than the form of the contract. This means that the operational realities of the Lease arrangement should be reviewed rather than the terms and conditions set out in the Lease agreement.

1. Examples of criteria that, individually or in combination, would normally lead to a Lease being classified as a Finance Lease are as follows:

* 1. The Lease transfers ownership of the asset to UNDP at the end of the Lease term;

* 1. UNDP has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair market value at the date the option becomes exercisable; and UNDP is reasonably certain, at the inception of the Lease , that the option will be exercised;

* 1. The Lease term comprises at least 75% of the economic life of the asset, even if title is not transferred;

* 1. At the inception of the Lease, the current value of the Minimum Lease Payments amounts to at least 90% of the fair market value of the leased asset;

* 1. The leased asset is of such a specialized nature that only UNDP can use it without major modifications;

* 1. The leased asset cannot easily be replaced by another asset

* 1. If UNDP can cancel the Lease, the Landlord’s/Lessor’s losses associated with the cancellation are borne by UNDP;

* 1. Gains or losses from the fluctuation in the fair market value of the residual asset accrue to UNDP. (For example, at the end of the Lease, there is a rent rebate that equals most of the sales proceeds);

* 1. UNDP has the ability to continue the Lease for a secondary period at a rent that is substantially lower than market rent.

# Operational Lease

1. The standard template for UNDP leases is an Operating Lease. When a Country Office signs a new lease it should upload the lease to the [SharePoint](https://intranet.undp.org/docs/lease/Lists/UNDP%20Property%20Leases/AllItems.aspx) and also submit a request to the GSSC for lease review through the [UNall Portal](https://undp.service-now.com/unall?id=esc_home). General Operations/Bureau for Management Services need this information for the purpose of financial statement reporting on leases and their terms while the GSSC staff will review all submissions for lease review together with leases uploaded into the SharePoint to assess whether or not the lease qualifies to be recorded as a Finance Lease.

1. Country Offices need to ensure that they upload all newly-signed leases (whether renewal or new) on a timely basis, within **the same month** of signature. The uploading into the SharePoint and submission of request to GSSC is part of the bi-annual certification process and offices will be required to confirm that these two actions are carried out.

1. An Operating Lease is a Lease other than a Finance Lease. For office space, a Lease that has been formulated and agreed following UNDP’s [Standard Lease Template](https://popp.undp.org/node/4571) will be an Operating Lease.

**Finance Lease**

# Inception of lease

18. The inception date of the Lease is the earlier of either the date of the Lease agreement or the date of commitment by the parties to the principal provisions or requirements of the Lease. The Lease is classified, from the applicable date, as either an Operating or a Finance Lease; and, for a Finance Lease, the amounts to be recognized at the commencement of the Lease term are determined.

# Lease term and duration

1. The Lease term is different from the Lease Duration. The Lease Term is the non-cancellable period for which UNDP has contracted to lease the asset (the premises or equipment) together with any further terms for which UNDP 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 UNDP expects to exercise that option. The duration of the Lease is the period that UNDP actually uses the asset.

1. For example, UNDP can have a Lease Term of 5 years but be able to stay in the premises for 20 years because the contract includes a contractual “first right option” to extend. The Lease Duration would, therefore, be 20 years because, at the inception, UNDP expects to stay for 20 years although it only signed an initial 5 years Lease. It is important to assess the Lease Term and Duration at the inception of the Lease.

1. If a renewal period is reasonably assured and failure to renew the Lease will result in penalty for UNDP, the renewal period should be considered as part of the Lease Term.

1. UNDP is required to disclose “*the total of future minimum Lease payments under Non-Cancellable Operating Leases*”. This information will be published in UNDP’s financial statements and is subject to audit.

1. A Cancellable Lease is one that has a termination clause such as “this Lease may be terminated upon provision of 30 days’ notice”; and is one of the key criteria used in determining whether a Lease is a Finance or an Operating Lease. A Non-Cancellable Lease is one that does not have such a clause in the agreement.

# Minimum lease payments

24. Minimum Lease payments are UNDPs liability for entering into a lease; and comprise:

1. The payments over the Lease Term that UNDP is, or can be, required to make in accordance with the payment plan for the Lease Term (not the Lease Duration). Contingent rent, costs for services and any taxes to be paid by and reimbursed to the landlord are not to be included; and

1. The payment required to exercise an option to purchase the asset at a price that is expected to be lower than the fair market value at the date the option becomes exercisable (This only applies when UNDP is reasonably certain, at the inception of the Lease, that it will exercise that option.) The minimum payments comprise the minimum payments payable over the Lease Term up until the date the option becomes exercisable; plus the amount required to exercise the option to purchase.

For example: if UNDP has a 2 Year Lease with an annual rent of $400,000; and has the option (that it expects to exercise) at the end of the two years, to purchase the building for $200,000, the computation of the minimum lease payments is:

Rent: $400,000 x 2 years = $ 800,000

Option to Buy = $ 200,000

Total Minimum Lease Payment = $ 1,000,000

# Government lease

1. UNDP has two standard forms of Government Leases:

* 1. Standard Basic Assistance Agreement (SBAA) Countries Leases. According to the SBAA and as a partner of UNDPs involvement in the country, the recipient government is required to provide UNDP “an appropriate office with equipment and supplies, adequate to serve as local headquarters for the UNDP in the country” and “the government shall have the option of providing facilities in kind […]”. When the recipient government chooses to provide facilities in kind, an agreement between the government and UNDP is signed. The facilities are usually provided rent-free and the duration can vary.

* 1. Other Government Leases. In some circumstances, UNDP receives the right to use an asset at no cost even though they are not programme implementing partners. Such is the case for example of the rent free premises provided by the German government (the UNV premises in Bonn) or the Danish government (the Copenhagen premises) to UNDP.

1. Under Government Lease, there is no transfer of cash between UNDP and the government. As such, the right to use the premises is treated as revenue from non-exchange transactions. The donated right to use the premises must be reviewed to assess whether it is an Operating Lease or a Finance Lease. In most UNDP scenarios, the donated right will not qualify as a Finance Lease, when the criteria set out above are applied. Consequently, UNDP will recognize such premises in its books as assets by booking the fair market rent value as an In-Kind Contribution from the government and the same amount as a Rent expense, i.e. the value of the in-kind rent is revenue for UNDP and also an expense, even though there is no cash exchange.

1. UNDP offices must continue providing related Leases and MOUs to the GSSC for its review. The request for Lease review will be submitted to the GSSC by the Premises Focal Points, via the [UNall Portal](https://undp.service-now.com/unall?id=esc_home), together with copies of the relevant supporting documentation (e.g. the Lease agreement). All original documentation must be properly filed at the respective office submitting the request.

# Common premises

1. The deciding factor in the treatment of common premises is to determine if the lead agency has exclusive ownership or control over the property or if the lead agency acts as an agent on behalf of the other participating agencies. In other words, the lead agency can assume all the risks of leasing the property but allow the other agencies to use it or it can be a joint arrangement with all the participating agencies bearing the risks in proportion to their share of occupancy.

1. Either of these two arrangements can occur for commercial operating leases and donated right to use property and the accounting treatment will be as follows:

| **Scenarios** | **Type of Arrangement** |  | **Accounting Treatment** |
| --- | --- | --- | --- |
| **1. Commercial Operating Lease** | 1a. The Lead Agency acts as Principal and bears all the risks of the Lease |  | 1a.  Record the full amount of rent as an expense and the portion of rent recovered from the participating Agencies should also be recorded as revenue in the books of the Lead Agency. All the participating Agencies should record their rent paid as an expense. |
| 1b.  The Lead Agency acts as an Agent on behalf of all the UN Agencies |  | 1b. Record each participating Agency's share of the rent paid, including the Lead Agency,  as an expense in their books. |
|  |  |  |  |
| **2.**  **Donated Right to Use Building** | 2a.  Building donated exclusively to the Lead Agency to use |  | 2a.  Record the expense and corresponding revenue as in kind contribution in the books of the Lead Agency using the FMV of annual rent. The participating Agencies should record an expense and corresponding revenue as in kind contribution using the FMV of the annual rent paid in proportion to the space occupied |
| 2b.  Building donated to the UN System to use |  | 2b.  Both the Lead Agency and participating Agencies should record an expense and corresponding revenue as in kind contribution using the FMV of the annual rent paid in proportion to the space occupied |

Payment methods

30. Where applicable the Rent due from participating agencies where UNDP acts as the lead agency, should be billed monthly in advance with accounting entries booked to Receivable and Revenue Accounts. Ideally, rental payments from the other agencies should be received in advance but may also be received in arrears. Where rental payment is received in advance for future years, this should be recorded as Deferred Revenue (a liability); and, for the current year, it should be off-set against the monthly rental raised. Where rental payment is received on a monthly basis in arrears, this amount will be offset against the Accounts Receivable raised. On the other hand, the Lease agreement between UNDP and the Landlord is assessed by the GSSC to determine whether it is a Finance Lease or an Operating Lease, using the classification criteria set out above. When an agreement is signed between UNDP and the other agencies, the request for Lease review will be submitted to the GSSC by the Premises Focal Point, via the [UNall Portal](https://undp.service-now.com/unall?id=esc_home), together with copies of the relevant supporting documentation (e.g. the Lease agreement). All original documentation must be properly filed at the respective office submitting the request.

# Determining if a Lease Should be Capitalized

31. At the inception, GSSC should be requested to analyze a Lease to determine the appropriate accounting treatment. The request for Lease review will be submitted to the GSSC by the Premises Focal Point, via the [UNall Portal](https://undp.service-now.com/unall?id=esc_home), together with copies of the relevant supporting documentation (Lease agreement, MOU etc.). All original documentation must be properly filed at the respective office submitting the request. In the review, the GSSC will adhere to the following steps:

1. The Lease must be analyzed to determine whether it is an Operating or a Finance Lease; the period of the Lease term; the total amount of the Lease payments due (the benchmark is similar commercial leases); and the fair market rental value of the asset (building or equipment); etc. For government Leases in SBAA countries, the estimated Lease payments are already included in the GLOC target.

1. If the analysis concludes the Lease is an Operating Lease, then no right to use is recorded in the balance sheet. UNDP will, however, record in its books two transactions:

the Lease expense and the contribution from the government.

1. If the analysis concludes the Lease is a Finance Lease, then the estimated Lease payment (the benchmark is similar commercial Lease) is used to determine the value of the right to use, i.e. the lower of fair market value; and the current value of the estimated Minimum Lease Payments. An asset is booked based on this value.

1. In a Finance Lease, UNDP recognizes a corresponding commitment (liability) for the Lease payments using the same value. This asset and liability will be recorded by the GSSC.