

May 8, 2019

Ms. Sue Lloyd, Chair  
International Financial Reporting Standards Interpretations Committee  
Columbus Building  
7 Westferry Circus  
Canary Wharf  
London E14 4HD  
United Kingdom

Dear Ms. Lloyd,

**Tentative Agenda Decision—Subsurface Rights (IFRS 16)**

The Financial Accounting Issues Task Force of the Taiwan Financial Reporting Standards Committee (TFRSC) of Accounting Research and Development Foundation in Taiwan appreciates the opportunity to respond to the above tentative agenda decision.

The attachments (Attachment 1) are our comments to this tentative agenda decision. The comments are those of the Financial Accounting Issues Task Force and do not necessarily represent official opinions of the TFRSC.

If you have any question about our comments, please contact me (via my email: [ccliu@management.ntu.edu.tw](mailto:ccliu@management.ntu.edu.tw)) or Ms. Margaret Tsui (via her email: [margaret@ardf.org.tw](mailto:margaret@ardf.org.tw)).

Sincerely Yours,



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Chi-Chun Liu, Ph.D.  
Chairman,  
Taiwan Financial Reporting Standards Committee,  
Accounting Research and Development Foundation, Taiwan

## Attachment 1

### Comments from ARDF Taiwan on Tentative Agenda Decision—Subsurface Rights (IFRS 16)

## Tentative Agenda Decision—Subsurface Rights (IFRS 16)

### Question

The IFRS Interpretations Committee (Committee) discussed the following matter and tentatively decided not to add it to its standard-setting agenda. The Committee will reconsider this tentative decision, including the reasons for not adding the matter to its standard-setting agenda, at a future meeting. The Committee invites comments on its tentative agenda decision. All comments will be on the public record and posted on our website unless a responder requests confidentiality and we grant that request. We do not normally grant such requests unless they are supported by good reason, for example, commercial confidence.

Tentative agenda decision

The Committee received a request about a particular contract for subsurface rights. In the contract described in the request, a pipeline operator (customer) obtains the right to place an oil pipeline in underground space for 20 years in exchange for consideration. The contract specifies the exact location and dimensions (path, width and depth) of the underground space within which the pipeline will be placed. The land owner retains the right to use the surface of the land above the pipeline, but it has no right to access or otherwise change the use of the specified underground space throughout the 20-year period of use. The customer has the right to perform inspection, repairs and maintenance work (including replacing damaged sections of the pipeline when necessary).

The request asked whether IFRS 16, IAS 38 Intangible Assets or another Standard applies in accounting for the contract.

Which IFRS Standard does an entity consider first?

Paragraph 3 of IFRS 16 requires an entity to apply IFRS 16 to all leases, with limited exceptions. Paragraph 9 of IFRS 16 states: ‘At inception of a contract, an entity shall assess whether the contract is, or contains, a lease.’

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The Committee observed that, in the contract described in the request, none of the exceptions in paragraphs 3 and 4 of IFRS 16 apply—in particular, the Committee noted that the underground space is tangible. Accordingly, if the contract contains a lease, IFRS 16 applies to that lease. If the contract does not contain a lease, the entity would then consider which other IFRS Standard applies.

The Committee therefore concluded that the entity first considers whether the contract contains a lease as defined in IFRS 16.

The definition of a lease

Paragraph 9 of IFRS 16 states that ‘a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.’ Applying paragraph B9 of IFRS 16, to meet the definition of a lease the customer must have both:

the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use; and

the right to direct the use of the identified asset throughout the period of use.

Identified asset

Paragraphs B13–B20 of IFRS 16 provide application guidance on an identified asset. Paragraph B20 states that ‘a capacity portion of an asset is an identified asset if it is physically distinct.’ But ‘a customer does not have the right to use an identified asset if the supplier has the substantive right to substitute the asset throughout the period of use’ (paragraph B14).

The Committee observed that, in the contract described in the request, the specified underground space is physically distinct from the remainder of the land. The contract’s specifications include the path, width and depth of the pipeline, thereby defining a physically distinct underground space. The space being underground does not in itself affect whether it is an identified asset—the specified underground space is physically distinct in the same way that a specified area of space on the land’s surface would be

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physically distinct.

The land owner does not have the right to substitute the underground space throughout the period of use. Consequently, the Committee concluded that the specified underground space is an identified asset as described in paragraphs B13–B20.

Right to obtain substantially all the economic benefits from use

Paragraphs B21–B23 of IFRS 16 provide application guidance on the right to obtain substantially all the economic benefits from use of an identified asset throughout the period of use. Paragraph B21 specifies that a customer can have that right, for example, by having exclusive use of the identified asset throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to obtain substantially all the economic benefits from use of the specified underground space throughout the 20-year period of use. The customer has exclusive use of the specified underground space throughout that period of use.

Right to direct the use

Paragraphs B24–B30 of IFRS 16 provide application guidance on the right to direct the use of an identified asset throughout the period of use. Paragraph B24 specifies that a customer has that right if either:

the customer has the right to direct how and for what purpose the asset is used throughout the period of use; or

the relevant decisions about how and for what purpose the asset is used are predetermined and: (i) the customer has the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions; or (ii) the customer designed the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

The Committee observed that, in the contract described in the request, the customer has the right to direct the use of the specified underground space throughout the 20-year period of

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use because the conditions in paragraph B24(b)(i) exist. How and for what purpose the specified underground space will be used (ie to locate the pipeline with specified dimensions through which oil will be transported) is predetermined in the contract. The customer has the right to operate the specified underground space by having the right to perform inspection, repairs and maintenance work. The customer makes all the decisions about the use of the specified underground space that can be made during the 20-year period of use.

Consequently, the Committee concluded that the contract described in the request contains a lease as defined in IFRS 16. The customer applies IFRS 16 in accounting for that lease.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine its accounting for the contract described in the request. Consequently, the Committee [decided] not to add the matter to its standard-setting agenda.

Deadline for submitting comment letters: 15 May 2019. The Committee will consider all comments received in writing by that date; agenda papers analysing comments received will include analysis only of comments received by that date.

### Response to the above Question:

Agreeing with your analysis, we support this tentative decision; that is, IFRS16, instead of other Standards, applies to the subsurface right and the matter discussed need not adding to the standard-setting agenda.

The controversy is over whether the subsurface of the land is an identified asset. The contract, according to the request, specified the exact location and dimension of the underground space within which the pipeline will be placed. That clearly proves that the subsurface of the land is identified because it is physically distinct and can be explicitly specified in a contract (see paragraph B13 and BC116 of IFRS16). Since the subsurface of

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the land, according to the term of the contract, is an indentified asset, we think the contract in the request which conveyed the right to control the use of that subsurface of the land for a period of time contains a lease.