Tasmanian Audit Office

Accounting Standards Update

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May 2019

Jeff Tongs

Accounting Standards Update
Agenda

- Are you ready for:

Australian Accounting Standard	Effective Date – Year beginning on or after	30 June Year-end
AASB 9 *Financial Instruments*	1 January 2018	30 June 2019
AASB 15 *Revenue from Contracts with Customers*	1 January 2018 (For-profit) 1 January 2019 (Not-for-profit)*	30 June 2019 30 June 2020*
AASB 1058 *Income of NFP Entities*	1 January 2019	30 June 2020
AASB 16 *Leases*	1 January 2019	30 June 2020

** AASB 2016-7 Amendments to Australian Accounting Standards – Deferral of AASB 15 for Not-for-Profit Entities*

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AASB 9 - *Financial Instruments*

- Applicable now
- Application is retrospective (comparatives required)
- Replaces AASB 139 *Financial Instruments: Recognition and Measurement*
- Associated amendments to AASB 7: *Financial Instruments: Disclosures*
- *Brings together classification, measurement, impairment and hedge accounting*
- *Moves from an "instrument" to a "principles" based approach*

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AASB 9 - *Financial Instruments*

Objective

- Establish principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of the entity's future cash flows.

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Recognition of Financial Assets

- Recognise when entity becomes party to the contractual provisions.
- De-recognise when contractual rights to cash flows expire or transfer.

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Initial Measurement

- A financial asset (or liability) shall be measured at its fair value plus or minus transaction costs directly attributable
- If FV differs from transaction price:
  - ➢ Quoted price in an active market or a valuation technique that uses only observable market data
  - ➢ In all other cases defer the difference

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Contractual cash flow characteristics (step 1)

- Financial assets with contractual cash flows that are **solely payments of principal and interest (SPPI)** are measured at amortised cost *(or FVOCI depending on the business model in which the asset is held).*
- Principal = amount transferred by holder (fair value at initial recognition)
- Interest is consideration or return on principal consistent with lending arrangements for:
  - time value of money and credit risk;
  - other lending risks (for example, liquidity risk);
  - other associated costs (for example, admin costs); and
  - a profit margin

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AASB 9 – Financial Assets
The Business Model (step 2)

Classification Key Criteria:

a. The entity's business model for managing the financial assets and

b. How does the entity intend to obtain the benefit from the financial asset

   1. Hold to collect cash flows? or

   2. Collect cash flows and sale ?

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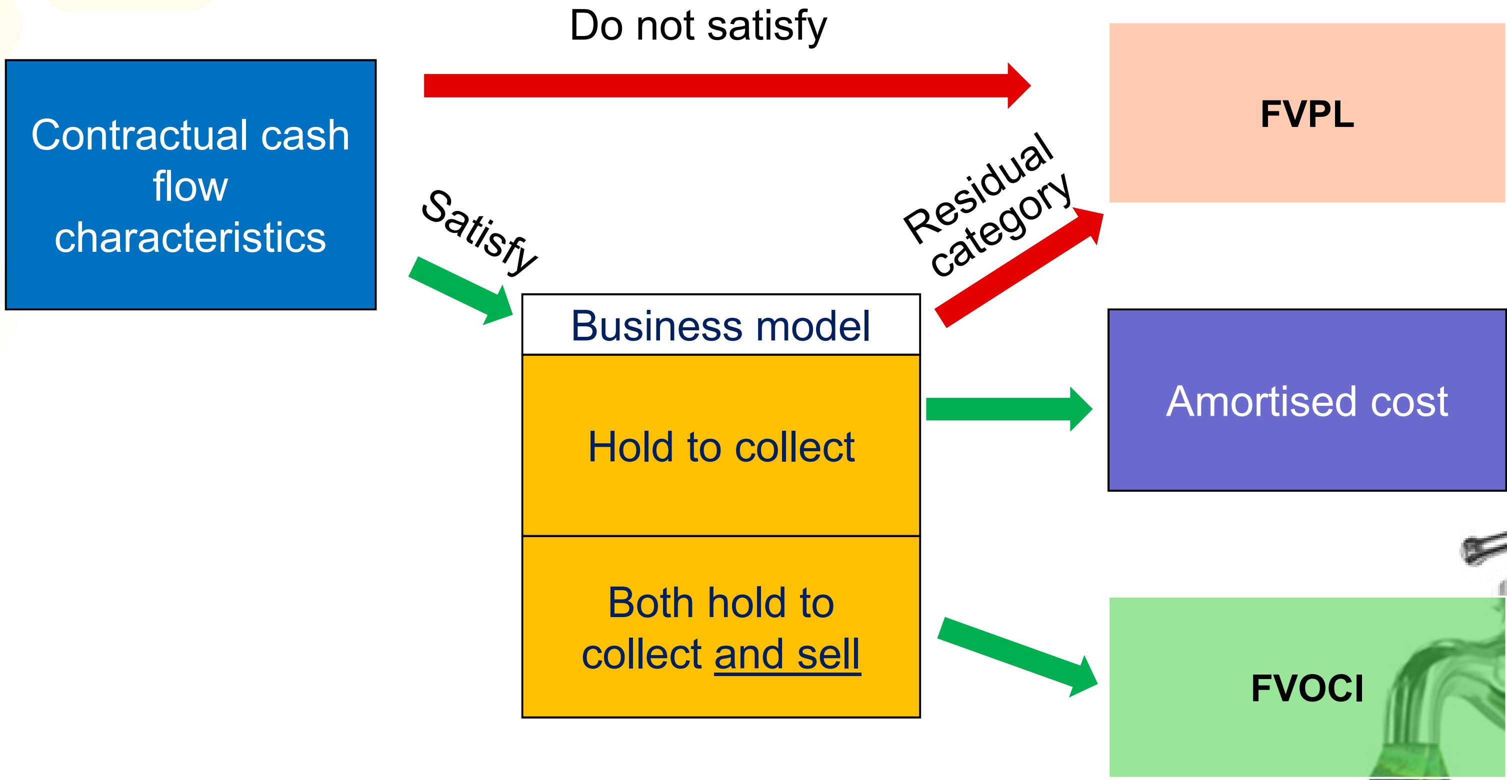
AASB 9 – Financial Assets
The Business Model



Reclassification applies to all business models

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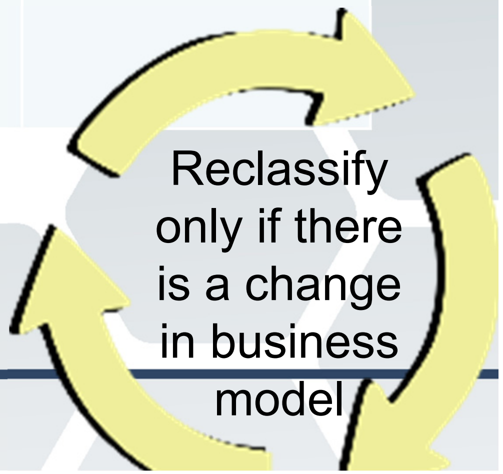
Types of Asset Business Models

An entity's business model is determined at a level that reflects how groups of financial assets are managed together to achieve a particular business objective.

Business Models	Key features	Measure at
Held-to-collect	• Entity holds assets to collect contractual cash flows • Sales are incidental to the objective (e.g. Trade Receivables, loans..)	Amortised cost
Held both to collect and for sale	• Both collecting contractual cash flows and sales are integral to achieving the objective of the business model (e.g. Debt instruments)	FVOCI
Others	• Assets are neither held-to-collect nor held to collect and for sale (e.g. Shares held for trading)	FVTPL



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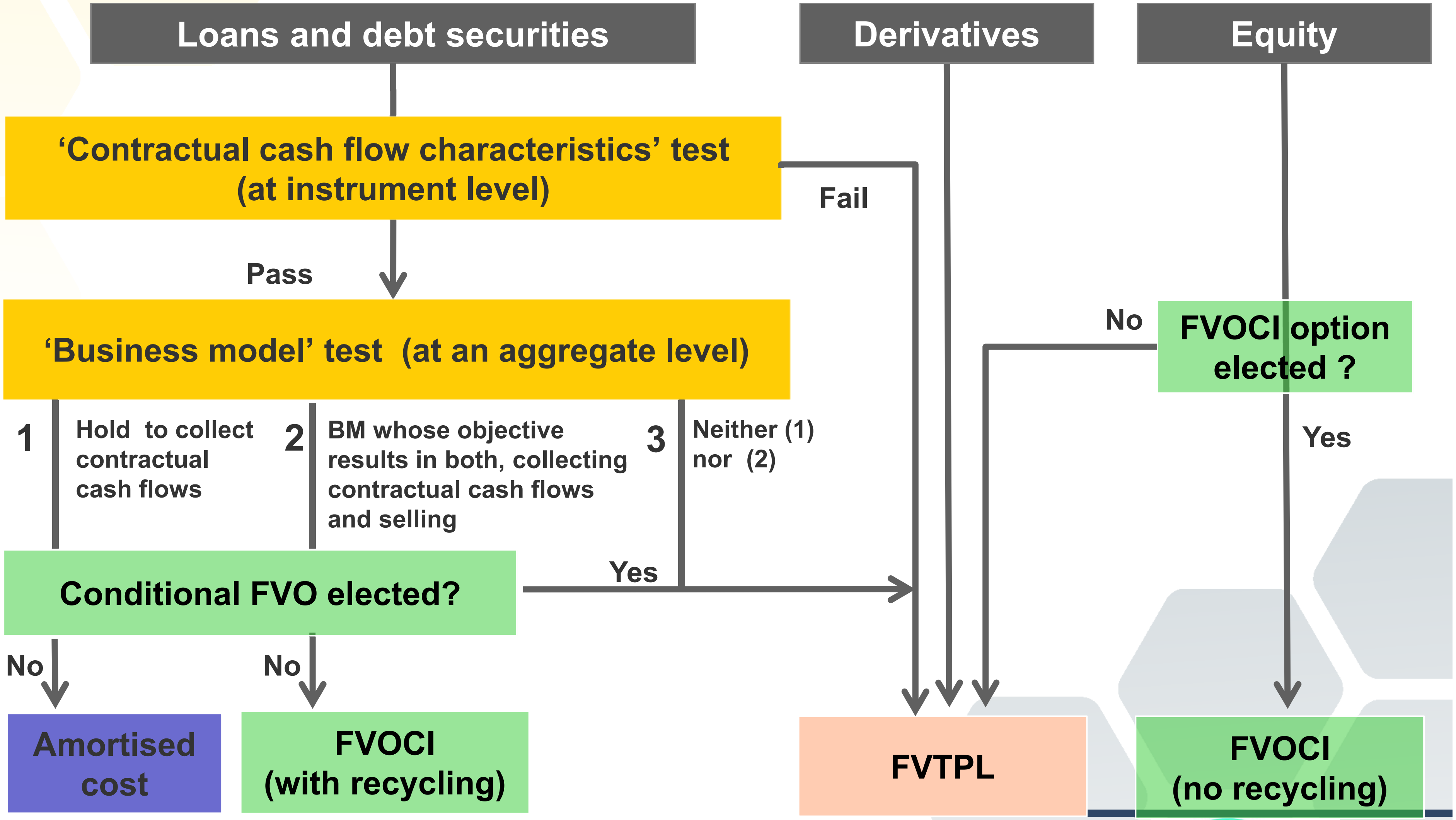
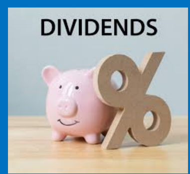
Criteria for classification and measurement



Subsequent measurement of *investments in equity instruments at Fair value through OCI*

Statement of financial position	Profit or loss	Other Comprehensive Income
Fair Value	Dividends 	Changes in fair value and foreign exchange component Amounts accumulated never reclassified to P&L

Classification & Measurement – Debt Instrument Illustrative Example

An entity purchases a 5 year corporate bond with a fixed interest rate of 3%. The bond was purchased with funds set aside to finance the construction of a new road in 5 years. It intends to hold the instrument to maturity and collect on the cash flows.

The instrument was previously held as part of a held to maturity portfolio.

1. SPPI Test: 
2. Business Model: *Hold to Collect*

AASB 9 Classification = Amortised Cost

Classification & Measurement – Debt Instrument Illustrative Example

An entity purchases a 5 year corporate bond, with a variable interest rate based on market rates as part of a social fund. The entity intends to hold the instrument to maturity and collect on the cash flows, but may sell as part of periodic rebalancing of the portfolio to better match the estimated timing and amount of future social fund payments.

The instrument was previously classified as AFS.

1. SPPI Test: 
2. Business Model: *Hold to Collect and Sell*

AASB 9 Classification = FVOCI (Debt)

AASB 9 – Financial Liabilities

- All financial liabilities to be measured at amortised cost using the effective interest method

except for:

- Financial liabilities at fair value through profit of loss
  - Held for trading
  - designated

Only change for financial liabilities designated at FVTP&L

- fair value changes attributable to the entity's own credit risk are presented in OCI (unless mismatch)

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AASB 9 - Impairment

At each reporting date assess:

- Whether credit risk has increased significantly since initial recognition
- Must consider reasonable and supportable information that is available without undue cost or effort.
- When information not available, entity may use past due information.
- Rebuttable presumption
  - There is a rebuttable presumption that credit risk has increased significantly if 30 days past due.

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AASB 9 – Impairment General rule

An entity shall recognise a Loss Allowance for Expected Credit losses on:

- Financial Assets at amortised cost
- Financial assets at FVOCI (meeting both the contractual CF test and business model test)

Debt securities. Receivables, Loans

- Leases receivable
- Contract assets
- Loan commitments
- Financial guarantee contracts

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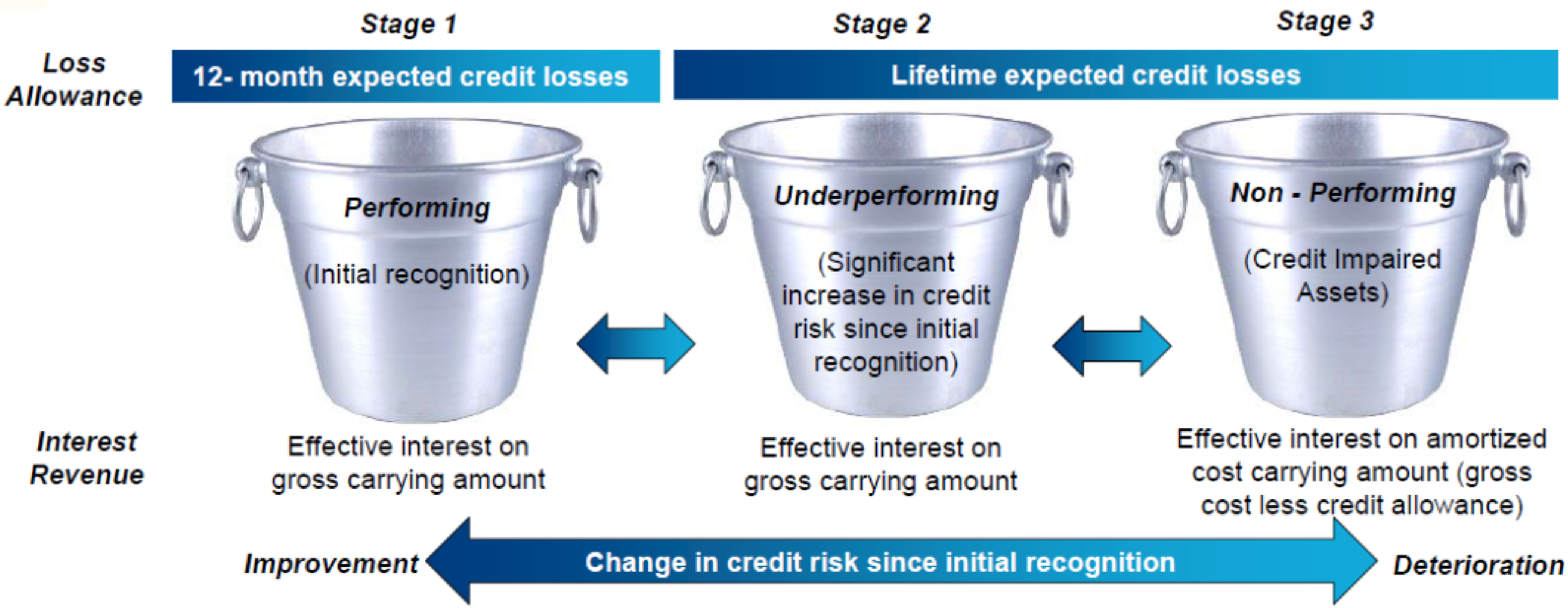
Summary of Expected Credit Loss Model
(General Approach)



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AASB 9 – Simplified Impairment

- Simplified approach available for:
  - Trade receivables and contract assets that result from transactions within scope of AASB 15 *Revenue from Contracts with Customers*, and
  - Lease receivables within scope of AASB 117 *Leases*.
- Entity to measure expected credit loss allowance at an amount equal to lifetime expected credit losses
- Practical expedient – can use provision matrix to estimate expected lifetime expected credit losses

AASB 9 – Simplified Impairment

Example provision matrix:

	Current	1–30 days past due	31–60 days past due	61–90 days past due	More than 90 days past due
Historic default rate	0.2%	1.3%	3.0%	5.7%	9.6%
Forward-looking estimate	0.1%	0.3%	0.6%	0.9%	1.0%
Total default rate	0.3%	1.6%	3.6%	6.6%	10.6%

Historical & Forward - looking

	Trade receivables	**Expected credit loss**	**Impairment allowance**
	A	B	AxB
Current	15,000	0.3%	45
1–30 days past due	7,500	1.6%	120
31–60 days past due	4,000	3.6%	144
61–90 days past due	2,500	6.6%	165
More than 90 days past due	1,000	10.6%	106
	30,000		**580**

AASB 9 – Write-offs

- Directly reduce carrying amount where no reasonable expectation of recovering a financial asset (entirety or proportion).
- There is a rebuttable presumption that entities should not set a default greater than 90 days without reasonable and supportable evidence for the alternative.

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Classification & measurement: overview

	AASB 139			AASB 9
	Categories	Measurement		Measurement categories
ASSETS	Held-to-Maturity (bonds) Loans & receivables	**Amortised cost** *(with split accounting)*	New classification criteria	**Amortised cost**
	Available-For-Sale (Equites & bonds)	**Fair Value / OCI recyclable** *(with split accounting)*		**Fair Value / OCI recyclable** (loans & bonds) **Fair Value / OCI non-recyclable** (measurement option for equities)
	Fair Value Option Trading	**Fair Value / P&L**		**Fair Value / P&L**
LIABILITIES	Fair Value Option Trading	**Fair Value / P&L**		**Fair Value / P&L** *(FVO: own credit-risk in non-recyclable OCI)*
	Amortised cost			**Amortised cost**

AASB 9 – Transition

- Full retrospective classification – restatement of comparative periods
  - Not applied to items already de-recognised at the date of initial application
  - Must reclassify all financial instruments (retrospective)
  - Must revoke previous designations that don't meet designation provisions for AASB 9
  - May designate if meet provisions of AASB 9
- Pragmatic - comparatives not required to be restated (reconciliation required)

New disclosure requirements

- Ongoing
  - Classification and measurement policies (incl' Bus Model)
  - Impairment (Policies, quantitative info' on loss calc's and a reconciliation of the loss allowance)
  - Hedging (policies and narrative and quantitative info' about strategies, objectives, instruments, reserves and ineffectiveness)
- On adoption
  - Narrations (explaining choices, designations, reasons and how classifications applied for each instrument)
  - Reconciliations of quantitative information in a tabular form

(Remember – AASB 7 *Financial Instruments: Disclosures* applies)

Reconciliation of financial instruments on adoption of AASB 9

On the date of initial application, 1 January 2018, the financial instruments of the Group were reclassified as follows:

		Measurement Category		Carrying Amount		
	Notes	Original AASB 139 category	New AASB 9 category	Closing balance 31 December 2017 (AASB 139)	Adoption of AASB 9	Opening balance 1 January 2018 (AASB 9)
		$'000	$'000	$'000	$'000	$'000
Assets						
Current financial assets						
Trade and other receivables	12	Amortised cost	Amortised cost	23,441	(22)	23,419
Derivative instruments (not used for hedge accounting)	13.7	FVPL	FVPL	212	-	212
Derivatives - Hedge accounting applied	13.7	Fair value with effective movements included in cash flow hedge reserve	Fair value with effective movements included in cash flow hedge reserve	230	-	230

AASB 7.42I (a),(b)
AASB 108.8.28(f)

Reconciliation of the statement of financial position balances from AASB 139 to AASB 9 at 1 January 2018:

	AASB 139 carrying amount 2017 $'000	Re-classification $'000	Re-measurement $'000	AASB 9 carrying amount 2018 $'000
~~Held to maturity~~				
Closing balance 31 December 2017	1,189			
To amortised cost		(1,189)		
Opening balance 1 January 2018 - AASB 9	**1,189**	**(1,189)**	**-**	**-**
Amortised cost				
Closing balance 31 December 2017 - AASB 139	34,638			
From Available for sale (AFS) - government bonds		1,189		
Impairment - receivables			(22)	
Impairment - government bond			(30)	
Opening balance 1 January 2018 - AASB 9	**34,638**	**1,189**	**(52)**	**35,775**

Reconciliation of equity for the impact of AASB 9 at 1 January 2018:

Impacted area	AFS financial assets reserve	FVOCI reserve	Retained earnings
	$'000	$'000	$'000
Closing balance 31 December 2017 - AASB 139	(22)	-	37,282
Reclassify listed equities from AFS to FVPL	22	-	(22)
Remeasurement - unlisted equities XY Ltd	-	-	27
Impairment - receivables	-	-	(22)
Impairment - government bonds	-	-	(30)
Opening balance 1 January 2018 - AASB 9	-	-	37,235

AASB 108.28 (f)(i)
AASB 7.42L

Policies for current year and comparative

E.g. Receivables recognition and Impairment…

Recognition and Measurement

All 'regular way' purchases or sales of financial asset are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Receivables are initially recognised at fair value plus any directly attributable transaction costs. Trade receivables that do not contain a significant financing component are measured at the transaction price.

Subsequent measurement under AASB 9 (from 1 July 2018)

The entity holds receivables with the objective to collect the contractual cash flows and therefore measures them at amortised cost using the effective interest method, less any impairment. Changes are recognised in the net result for the year when impaired, derecognised or through the amortisation process.

Subsequent measurement under AASB 139 (for comparative period ended 30 June 2018)

Subsequent measurement is at amortised cost using the effective interest method, less any impairment. Changes are recognised in the net result for the year when impaired, derecognised or through the amortisation process.

Impairment under AASB 9 (from 1 July 2018)

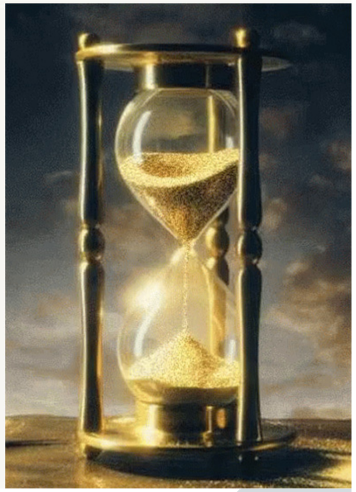
The entity recognises an allowance for expected credit losses (ECLs) for all debt financial assets not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows and the cash flows that the entity expects to receive, discounted at the original effective interest rate.

For trade receivables, the entity applies a simplified approach in calculating ECLs. The entity recognises a loss allowance based on lifetime ECLs at each reporting date. The entity has established a provision matrix based on its historical credit loss experience for trade receivables, adjusted for forward-looking factors specific to the receivable.

Impairment under AASB 139 (for comparative period ended 30 June 2018)

Receivables are subject to an annual review for impairment. These are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows have been affected.

The entity first assesses whether impairment exists individually for receivables that are individually significant, or collectively for those that are not individually significant. Further, receivables are assessed for impairment on a collective basis if they were assessed not to be impaired individually.



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Disclosure Update

Template updated by Advisory Panel

2019 Executive Remuneration

Name	Position	Period	Base Salary[1] $'000	Short-Term Incentive Payments[2] $'000	Superannuation[3] $'000	Vehicles[4] $'000	Other Monetary Benefits[5] $'000	Other Non-Monetary Benefits[6] $'000	Total Remuneration ~~Package~~ $'000	Termination Benefits[7] $'000	Other Long-Term Benefits[8] $'000	Total $'000
Mr J Napier	*Chief Executive Officer*	*Full year*	*270*	*25*	*44*	*25*	*2*	*2*	*368*	*0*	*5*	*373*
Mr O C Cobblepot	*General Manager Safety*	*Full year*	*130*	*0*	*20*	*8*	*0*	*1*	*159*	*0*	*14*	*173*
Prof. J Crane	*General Manager Research*	*Full year*	*175*	*12*	*28*	*6*	*0*	*0*	*221*	*0*	*1*	*222*
Mr H Dent	*Director Project Delivery*	*Full year*	*165*	*0*	*25*	*16*	*0*	*0*	*206*	*0*	*(14)*	*192*
Mr V Fries	*General Manager Cold Storage*	*To 28/2/2019*	*145*	*0*	*34*	*5*	*0*	*0*	*184*	*81*	*(55)*	*210*
Dr. P Isley	*Director - Distribution*	*Full year*	*145*	*12*	*24*	*12*	*2*	*0*	*195*	*0*	*(11)*	*184*

- “Other Non-Monetary Benefits” now part of “Total Remuneration ~~Package~~”
- Only termination benefits & leave movements outside “Total Remuneration”
- Definition Updates - “Other Monetary Benefits” & “Other Non-Monetary Benefits”
- Applies this year
- Revised template available on TAO Website
- Comparatives to be presented into new layout.
  ($ remain unchanged)

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AASB 15 – Revenue
AASB 1058 – Revenue for Not-for-Profit

Core Principle:

- The recognition of revenue for the transfer of goods and services, at a value that reflects the consideration to which the entity expects to be entitled, in return for meeting performance obligations

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AASB 15
The 5 Revenue Steps

Step 1
Identify the Contract

Step 2
Identify the separate performance obligations

Step 3
Determine the transaction price

Step 4
Allocate transaction price to performance obligations

Step 5
Recognise revenue when each performance obligation is satisfied

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Step 1 – Identify the contract
Contract criteria (AASB 15:9)

Step 1
Identify the Contract

The contract is approved and the parties are committed to their obligations

The entity can identify each party's rights and payment terms

Contracts with customers must meet ALL of these criteria

The contract has commercial substance

Collection of consideration is probable

If each party has the unilateral enforceable right to terminate a wholly unperformed contract without compensating the other party (or parties) → no contract for the purposes of AASB 15

Step 2 – Identify the performance obligations

Step 1
Identify the Contract

Step 2
Identify the separate performance obligations

A **performance obligation** is a promise in a contract with a customer to transfer a **distinct** good or service (or bundle of goods or services), or a series of substantially similar distinct goods or services with the same pattern of transfer to the customer

Some examples of promised goods or services:

- sale of goods produced by an entity (eg inventory)
- resale of goods purchased by an entity (eg merchandise or product)
- resale of rights to goods or services purchased by an entity (eg electricity)
- performing a contractually agreed-upon task for the customer (eg cleaning services)
- granting a licence

Step 2 – Identify the performance obligations

Distinct good or service

Step 1
Identify the Contract

Step 2
Identify the separate performance obligations

1. Customer can benefit from good or service
(ie capable of being distinct)

- On its own; (para 27a)or
- Together with other readily available goods or services (including goods or services previously acquired from entity)

And

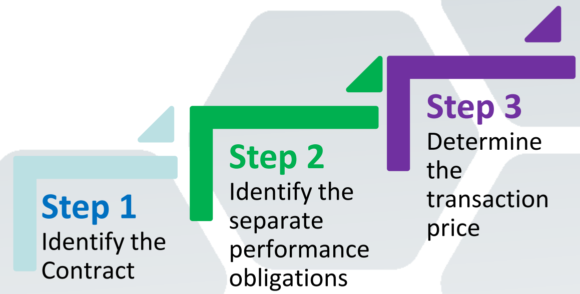
2. Promised good or service is separable from other promises
(ie distinct in the context of the contract) (para 29)

- No significant service of integrating the good or service
- Good or service does not significantly modify or customise another good or service in the contract
- Good or service is not highly dependent on or highly interrelated with other goods or services

Step 3 - Determine the Transaction Price

The amount of consideration to which an entity <u>expects</u> to be entitled in exchange for transferring the promised goods or services to a customer

- Relative stand-alone selling price
- Non-cash consideration measured at fair value
- Adjust for significant financing benefit to customer
- Estimate of variable consideration.



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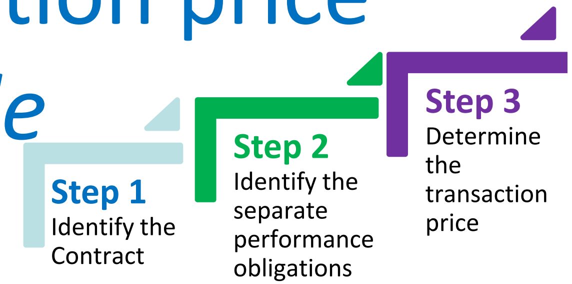
Step 3 – Determining the transaction price

Constraining estimates of variable consideration



Include estimate of variable consideration in the transaction price only to extent it is *highly probable a significant reversal of revenue will not occur* when uncertainty is resolved (para 56)

Entity's expectations of revenue reversal assessed using indicators, e.g.: Para 57

– Factors outside entity's influence (market, 3rd-party actions etc)

– Length of time before uncertainty resolved

– Entity's level of experience with similar types of contracts

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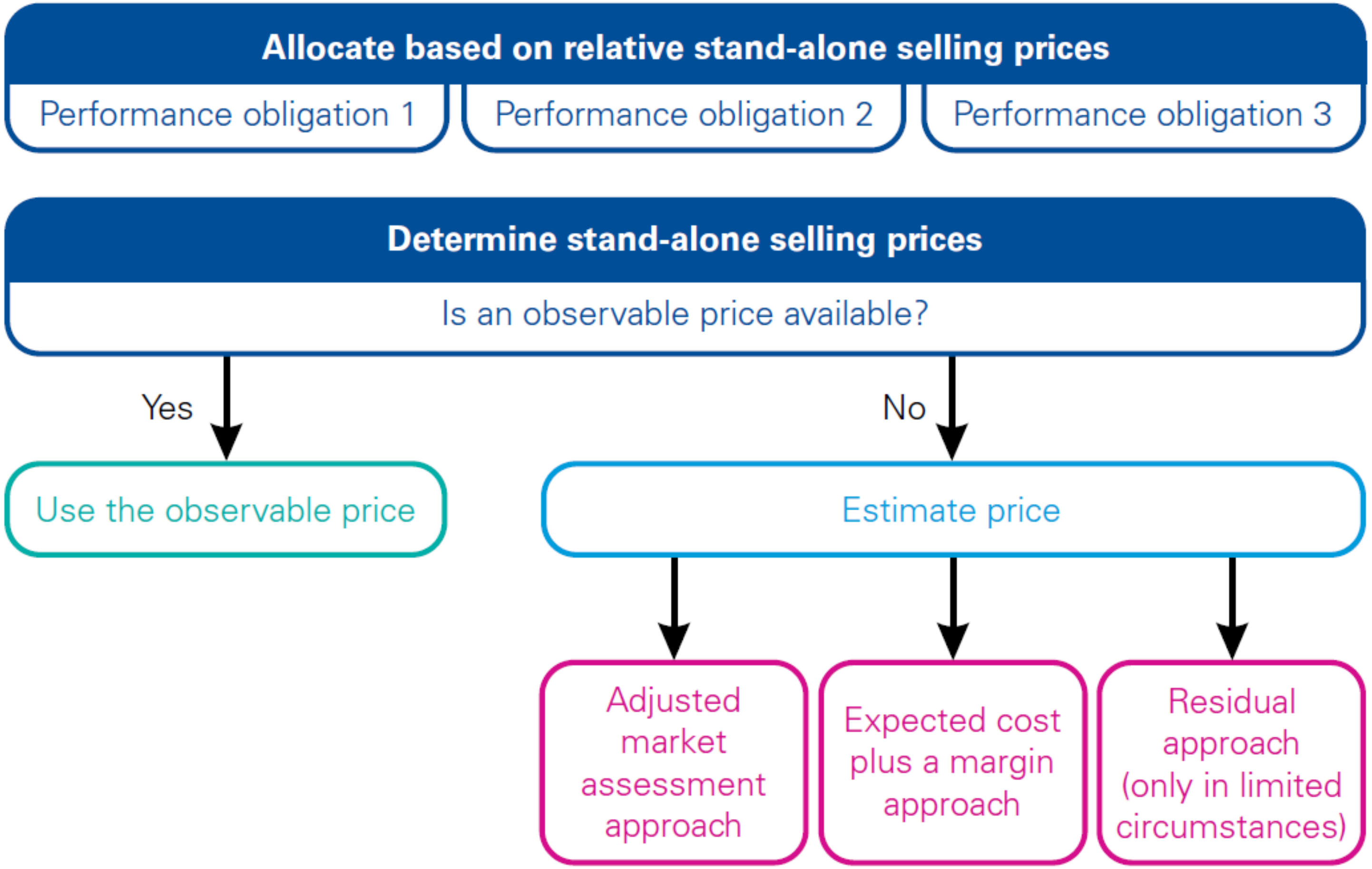
Step 4 - Allocating performance obligations based on stand alone selling prices

Step 4
Allocate transaction price to performance obligations

- Transaction price is allocated to each performance obligation in proportion to stand-alone price.



Step 4 – Allocating the transaction price to performance obligations

Step 4
Allocate transaction price to performance obligations

- Where stand-alone selling price is not directly observable: estimate the amount using one of the following approaches: (para 79)

Adjusted market assessment approach	• Evaluate the market in which goods or services are sold and estimate the price that customers in the market would be willing to pay
Expected cost plus a margin approach	• Forecast the expected costs of satisfying a performance obligation and then add an appropriate margin for that good or service
Residual approach (limited applicability)	• The total transaction price less the sum of the observable stand-alone selling prices of other goods or services promised in the contract

Step 4 – Allocating the transaction price to performance obligations

Allocation discount

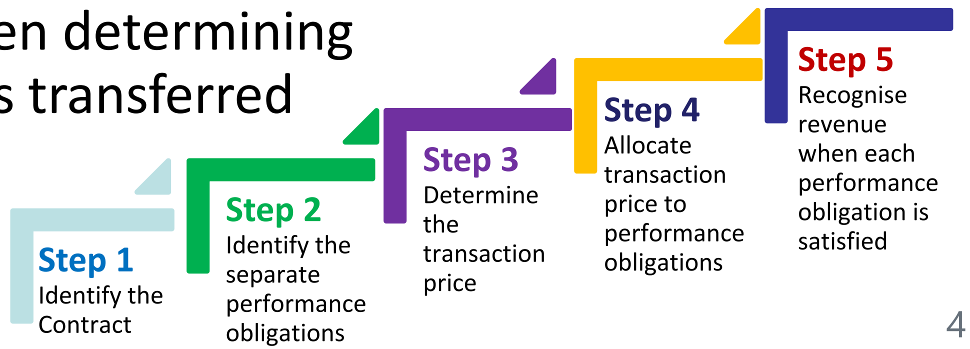
- A discount is where the price for the bundle is less than the sum of the stand-alone price of individual performance obligations
- Allocate discount proportionately to all performance obligations in the contract, (except when they relate to one or more but not all)

Allocate variable considerations

- Allocation can be to entire contract or specific parts
- Allocate variable consideration to a performance obligation if :
  - The terms of the variable payment relate specifically to satisfying the performance obligation
  - This allocation would faithfully depict the consideration entity expects for transferring the goods or services to the customer

Step 5- Recognise revenue when (or as) the entity satisfies a performance obligation

- When the customer obtains control of the good or service
- Control transfers 'over time' or at a 'point in time'
  - First, determine if control transfers over time
    - If control transfers over time, select a single input or output method to measure progress for a particular performance obligation
    - Apply consistent method for all similar arrangements
  - If control does not transfer over time, default is point in time
    - Indicators provided to assist when determining the point in time when control is transferred



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Step 5 - *Continued..*

➢ Revenue is recognised **over time** when: (para 35)

- Customer simultaneously receives and consumes all of the benefits as the entity performs obligations (traditional service arrangements e.g. cleaning and security services).
- Performance creates or enhances an asset that the customer controls (e.g. construction contracts where the customer controls the work-in-progress throughout the arrangement).
- Performance does not create an asset with an alternate use and entity has enforceable right to payment for performance to date (e.g. legal services – payment reflects work performed including a reasonable profit margin).

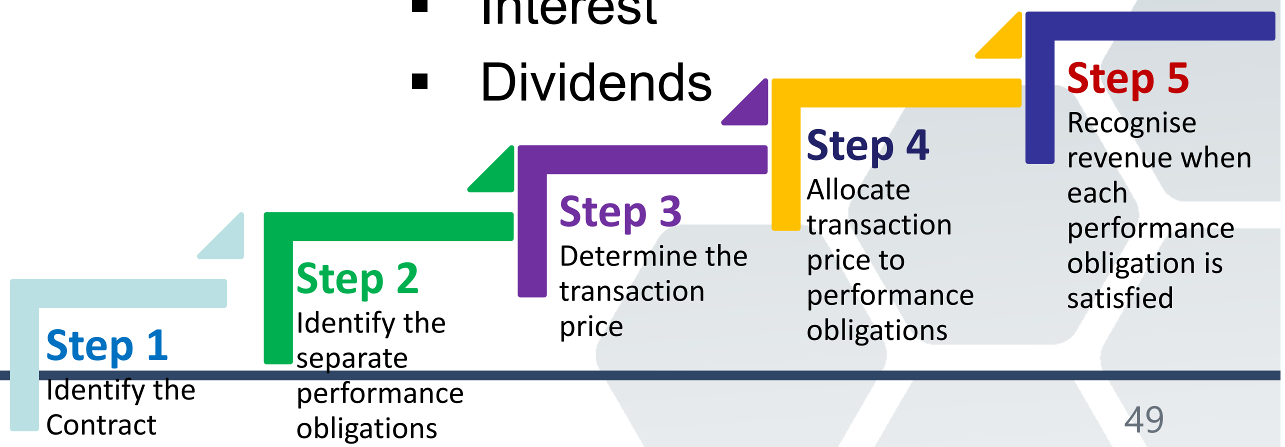
Step 5 – Recognition of revenue *(continued)*

- If not over time, then **point in** time…. (para 38)
- Recognise revenue when control transfers
- Indicators of the transfer of control of a good or service *include*:

- The entity has a present right to payment
- The customer has legal title
- The entity has transferred physical possession
- The customer has the significant risks and rewards of ownership
- The customer has accepted the asset

Revenue and Income Sources

- Appropriations
- Grants – Recurrent
- Grants – Special purpose
- Grants – Capital
- Fees
- Levies
- User charges
- Fees for service
- Sale of goods
- Licences
  - Right of Use
  - Right of access
- Royalties
- Performance management fees
- Contributed services
- Capital contributions / contributed assets
- Sponsorship
- Taxes
- Interest
- Dividends



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Allocation based on a stand-alone selling price

Example

- An entity has a contract to sell equipment, provide training and operate a helpdesk.
- Each of these has been assessed to be separate performance obligations.
- The total transaction price is $1,200,000.

The stand-alone selling price for each distinct good or service is:

Equipment	$750,000	50%
Training	$150,000	10%
Helpdesk	$600,000	40%
Total of stand-alone prices	**$1,500,000**	

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Allocation based on a stand-alone selling price

Example

- The total transaction price is allocated to each service performance obligation as follows:

Equipment	Point in time	600,000	1,200,000 x 50%
Training	Over time	120,000	1,200,000 x 10%
Helpdesk		480,000	1,200,000 x 40%
Total transaction price		**$1,200,000**	

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AASB 15 – Transition is Retrospective

Two approaches allowed:

1. Fully Retrospectively application, *with some relief*
   - Need not restate completed contracts that begin and end within the same period
   - Hindsight allowed for variable consideration of completed contracts
   - Prior to application, need not disclose information on remaining performance obligations in comparatives.
2. Retrospectively with <u>cumulative effect</u> at date of initial application:
   - Apply the Standard to all existing contracts as of effective date and to contracts entered into subsequently
   - Recognise the cumulative effect as an adjustment to the opening balance of retained earnings

AASB 15 – Disclosures

- Key qualitative and quantitative disclosures:
  - Contract balances
  - Disaggregation of revenue
  - Costs to obtain or fulfil contracts
  - Remaining performance obligations
  - Significant judgements and changes in judgements

AASB 1058 Income of Not-for-profit Entities

Process:

1. Determine if AASB 15 applies and if it does the NFP applies AASB 15
2. If AASB 15 does not apply then the NFP considers if AASB 1058 applies:

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AASB 1058 *Income of Not-for-Profit Entities* – Objective

Establishes principles that apply to:

(a) transactions where the consideration to acquire an asset is significantly less than fair value principally to enable the NFP to further its objectives

(b) the receipt of volunteer services.

AASB 1058 – Key Areas

1. Assets received below fair value
2. Transfers received to acquire or construct non-financial assets
3. Grants
4. Non-contractual statutory income
5. Peppercorn leases
6. Volunteer services

Consideration for asset significantly less than fair value + furthers NFP objectives

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AASB 1058 – Grants

Example

Example:

A NFP receives a Gov't grant of $2.4m on 31 May 20X8, which is refundable if the money is not spent in the period 1 July 20X8 to 30 June 20X9.

- It's charter is to provide counselling to victims of violence and emergency accommodation to the homeless; and
- It has an agreement that specifies the grant must be spent providing crisis counselling services for a given number of hours per week for the entire year ending 30 June 20X9. The entity expects to fulfil its promise.

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AASB 1058 – Grants

Example

Example - journal entries:

Initial recognition - 31 May X8	**Debit**	**Credit**
Cash	2,400,000	
Contract Liability		2,400,000
Year 2 – 20X9		
Contract Liability	2,400,000	
Expenses	2,400,000	
Cash		2,400,000
Income		2,400,000

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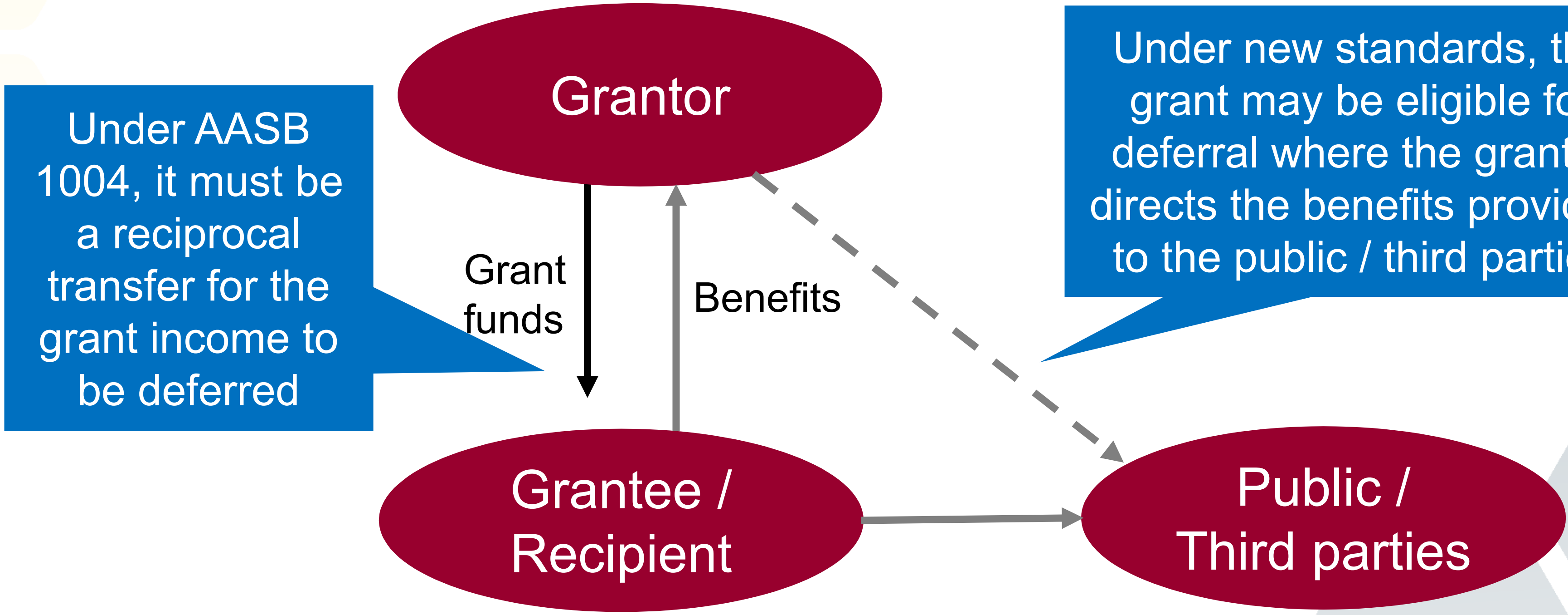
Revenue Recognition Changes
Accounting for Grant Income



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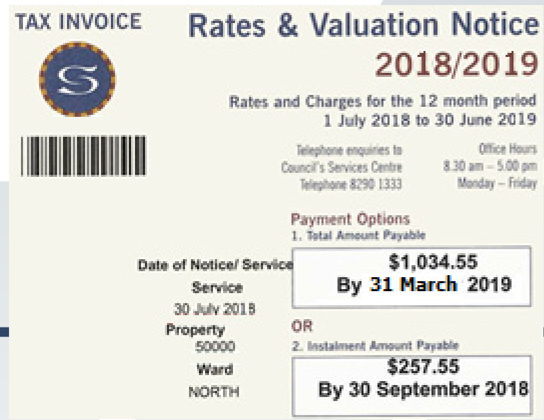
AASB 1058 – Non-contractual Income arising from Statutory Requirements

- Disclose statutory income (rates, taxes & fines)
- Disaggregated into categories that reflect how the nature and amount of income are affected by economic factors
- Statutory receivables initial recognition to be part of AASB 9 *(AASB 2016-8)*
- Can be a receivable or a liability
- Example:
  - prepaid taxes or rates for which the *taxable event* has yet to occur


TAX INVOICE
Rates & Valuation Notice
2018/2019
Rates and Charges for the 12 month period
1 July 2018 to 30 June 2019
Telephone enquiries to
Council's Services Centre
Telephone 8290 1333
Office Hours
8.30 am – 5.00 pm
Monday – Friday
Payment Options
1. Total Amount Payable
Date of Notice/ Service
Service
30 July 2018
Property
50000
Ward
NORTH
$1,034.55
By 31 March 2019
OR
2. Instalment Amount Payable
$257.55
By 30 September 2018

AASB 1058 – Peppercorn Leases

- Where a NFP lessee has a lease that at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives, the NFP entity shall :
  - Measure the right-of-use asset at fair value
  - Measure the lease liability at the present value of lease payments not paid at that date
  - Recognise any related items in accordance with AASB 1058 (i.e. the difference)

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Example

AASB 1058 – Peppercorn Leases

Example:

- An entity built on land leased to it for $20pa for 99 years
- Present value of remaining lease payments is $200
- Fair value of the right of use land is $1m
- The entity had not previously recognised the right-of-use asset for land or a lease liability.

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Example

AASB 1058 – Peppercorn Leases

Example:

- The entity is reporting for the period ending 30 June 2020.

Treatment on transition:

Journal entry 1 July 2019	**Debit**	**Credit**
Right-of-use asset - land	1,000,000	
Lease Liability		200
Opening retained earnings		999,800

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Amending Standard AASB 2018 – 8: *Right-of-use Assets of Not-for-Profit Entities*

- temporary option not to measure ROU assets arising from leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives

  NFPs lessees to elect:

  - FV per *AASB 13 Fair Value Measurement*; **or**
  - Cost in accordance with AASB 16

- option applies **both** on transition and new leases

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Amending Standard AASB 2018–8: *Right-of-use Assets of Not-for-Profit Entities*

Additional qualitative and quantitative disclosures:

- the entity’s dependence on leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives; and
- the nature and terms of the leases, including:
  - the lease payments;
  - the lease term;
  - a description of the underlying assets; and
  - restrictions on the use of the underlying assets specific to the entity.

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AASB 1058 – Volunteer Services

- Local governments, government departments, general government sectors and whole of governments must recognise an inflow of resources where:
  - they would have been purchased if they had not been donated; and
  - the fair value of those services can be measured reliably.
- Any other NFP can elect
- Disclosure of additional qualitative information is encouraged

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AASB 16 Leases

Stephen Morrison
Assistant Auditor-General Financial Audit

Definition

A Lease - is a 'contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration'

All contracts create rights and obligations

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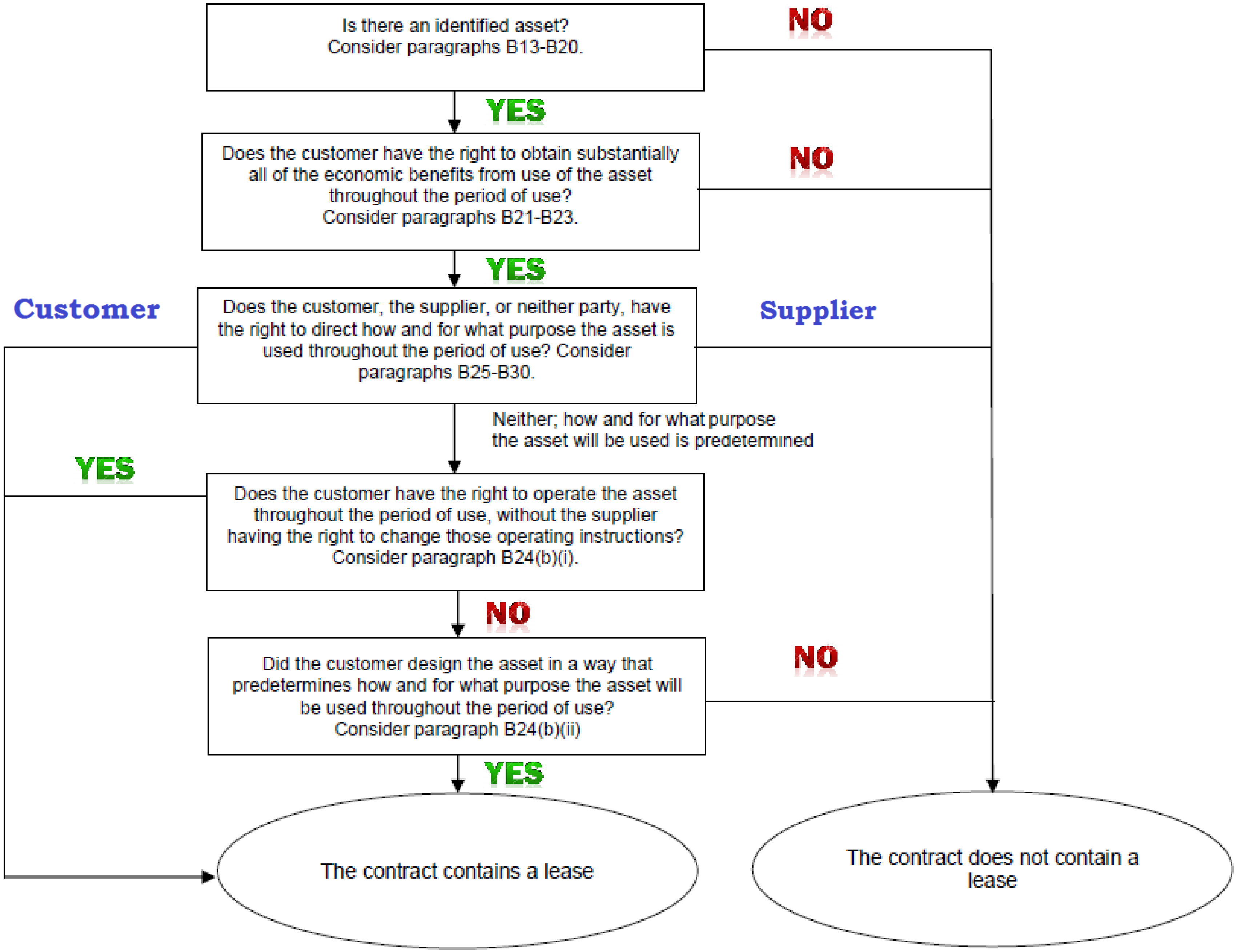
So what does this mean?

- Need to review contracts to identify potential leases
- Determine rights and obligations
- Does the contract:
  - Have an identifiable asset (there may be more than one)
  - Provide the right for the customer to obtain all of the economic benefits from using the asset over the period of the contract
  - Provide the customer with the right to direct how and what purpose the asset is used for
- If yes – generally considered to be a lease
- If no – contract unlikely to be a lease


Is there an identified asset?
Consider paragraphs B13-B20.
NO
YES
Does the customer have the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use?
Consider paragraphs B21-B23.
NO
YES
Customer
Does the customer, the supplier, or neither party, have the right to direct how and for what purpose the asset is used throughout the period of use? Consider paragraphs B25-B30.
Supplier
Neither; how and for what purpose the asset will be used is predetermined
YES
Does the customer have the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions?
Consider paragraph B24(b)(i).
NO
Did the customer design the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use?
Consider paragraph B24(b)(ii)
NO
YES
The contract contains a lease
The contract does not contain a lease

Exclusions

Not required to be included in lease liabilities

- Leases of low-value assets (approx. $10,000)
- Short-term assets (<12 months)

Excluded from lease liabilities

- Variable lease payments
- Optional payments (not reasonably certain)

- Disclosure requirements apply (p53)

Lessee Model

- Assets & liabilities on the balance sheet, initially measured at the present value of unavoidable lease payments
- Amortisation of lease assets and interest on lease liabilities over the lease term

  (Assets – typically straight-line basis)
- Separate the total amount of cash paid into:
  - Principal portion (presented within financing activities)
  - Interest (either operating or financing activities).

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Presentation Impacts

Statement of Financial Position		
• Right-of-use asset • Lease liability	Either by:	➢ Separate line items, or ➢ In the relevant Notes and link

Income Statement
• Interest expense on the lease liability • Depreciation charge on right-of-use assets

Statement of Cash Flows	
• Cash payment on the principal	➢ Financing Activity
• Short-term, low-value and variable lease payments not included in liability measurement	➢ Operating Activity
• Interest portion	➢ Apply AASB 107 *St' of Cash Flows*

Recognition – Lease Liability

- Initial recognition at commencement date:

Present value of:

the lease payments not paid

+

Residual value guarantees

-

Lease incentives receivable

+

Exercisable Options (reasonably certain)

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Recognition – Right to Use Asset

- Initial recognition:

Lease liability as calculated previously

\+

Lease payments made before commencement date

\-

Lease incentives received

\+

Initial direct costs of Lessee

\+

PV Cost of removal and make-good at end of the lease

Example 1 - Recognition

- Information available
  - Office accommodation – Commencing 1 July 2020
  - Term 5 years with a 5 year option expected to be exercised
  - Rent $48,000 per annum
  - Outgoings $12,000 per annum
  - Financing rate 6%
  - Lease incentive (fit-out) $20,000
    - Received $15,000
    - Receivable $5,000
  - Legal costs for lease $2,000
  - Lease payment made 1 June 2020 - $4,000
  - Residual value guarantee $Nil
  - Make Good $20,000

Example 1 - Recognition

- Liability

  + Rent $236,000 ($48,000 x 5 years less $4,000 paid)

  + Option $240,000 ($48,000 x 5 years)

  + Residual value $0

  - Lease Incentive Receivable ($5,000)

  Total $471,000 (to be discounted to Present Value)

- Asset

  + Lease liability $471,000 (to be discounted to Present Value)

  + Lease paid before commencement $4,000

  - Lease Incentive Received ($15,000)

  + Legal Fees $2,000

  + Make Good $20,000 (to be calculated and discounted under AASB 137)

  Total $482,000

Example

Example 2

- Assumptions:
  - 3 year lease.
  - Lease payments $50,000 p.a.
  - Effective interest rate 6%.
  - Lease payments made at end of period.

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Example

Example 2

- At start - RoUA and lease liability $133,651.
- At the end of each period - RoUA amortisation $44,550
- For each lease payment - cash $50,000 and:
  - Year 1; Interest expense $8,019 & principal repayment $41,981
  - Year 2; Interest expense $5,500 & principal repayment $44,500
  - Year 3; Interest expense $2,830 & principal repayment $47,170

Totals **$16,349** **$133,651**

$150,000

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Example 2

	Year 1		Year 2		Year 3	
Opening Journal						
DR Right-of-use-asset	133,651					
CR Lease Liability		133,651				
Yearly Journal	**Year 1**		**Year 2**		**Year 3**	
DR Interest Expense	8,019		5,500		2,830	
DR Lease Liability	41,981		44,500		47,170	
CR Bank		- 50,000		- 50,000		- 50,000
Dr Amortisation Expense	44,550		44,550		44,550	
Cr Accumulated Amortisation		- 44,550		- 44,550		- 44,550
Statement of Financial Position						
DR Right-of-Use-Asset	133,651		133,651		133,651	
Cr Accumulated Amortisation	- 44,550		- 89,101		- 133,651	
($133,651/ 3 years = $44,550)	89,101		44,550		-	
CR Lease Liability		- 133,651		- 91,670		- 47,170
DR Lease Liability		41,981		44,500		47,170
		- 91,670		- 47,170		-

Example

Example 2

Statement of Comprehensive Income	Year 1	Year 2	Year 3
Interest Expense	8,019	5,500	2,830
Amortisation Expense	44,550	44,550	44,550
	52,569	50,050	47,380

Statement of Cash Flows			
Interest Expense	8,019	5,550	2,830
Financing Cash Flow *(Principal Repayment)*	41,981	44,500	47,170
	50,000	50,000	50,000

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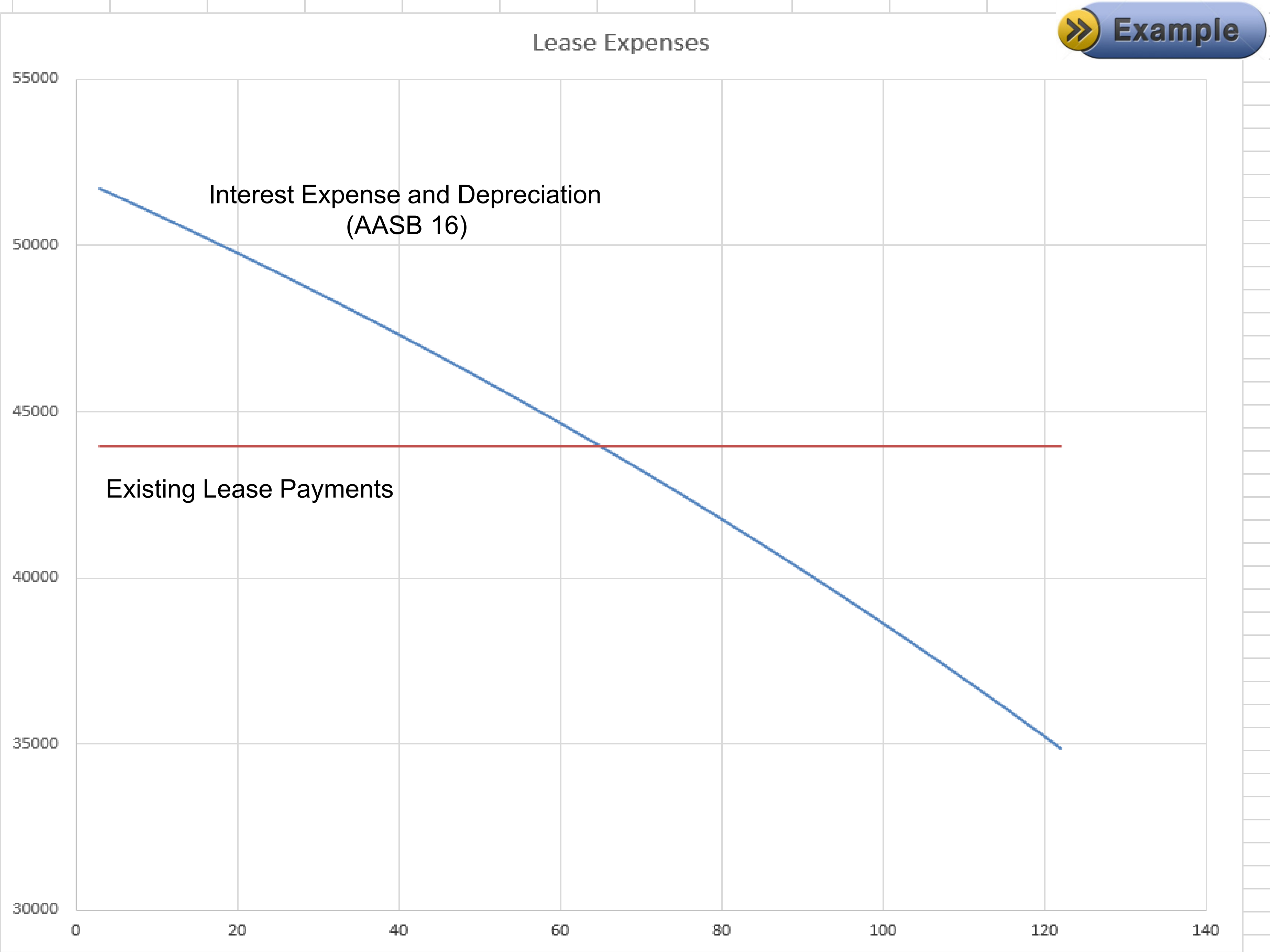

Example
Lease Expenses
55000
50000
45000
40000
35000
30000
0
20
40
60
80
100
120
140
Interest Expense and Depreciation
(AASB 16)
Existing Lease Payments

Other Considerations

- CPI and other rate increases
- Changes to leases during lease period (modifications)
- Present value calculations - determine effective interest rate (may differ between leases for similar or like assets)
- Review disclosure requirements

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Example

Example 3 Lease re-measurement

(for example, CPI rent increase)

		1-Jul-10			1-Jul-11	
	1-Jul-10	1,000,000				
	1-Jul-11	1,000,000		1-Jul-11	1,020,000	Changed rent
	1-Jul-12	1,000,000		1-Jul-12	1,020,000	
	1-Jul-13	1,000,000		1-Jul-13	1,020,000	
	1-Jul-14	1,000,000		1-Jul-14	1,020,000	
	1-Jul-15	1,000,000		1-Jul-15	1,020,000	
	1-Jul-16	1,000,000		1-Jul-16	1,020,000	
	1-Jul-17	1,000,000		1-Jul-17	1,020,000	
	1-Jul-18	1,000,000		1-Jul-18	1,020,000	
	1-Jul-19	1,000,000		1-Jul-19	1,020,000	
NPV 5%	1-Jul-10	7,848,186				
NPV 5%	30-Jun-11	7,231,114	$144,623		7,375,737	

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Example

Example 3 Lease re-measurement

(for example, CPI rent increase)

		Asset	Liability		Asset	Liability
Opening balance	**1-Jul-10**	0	0	**1-Jul-11**	7,063,797	7,231,114
Adjustment		7,848,186	7,848,186		144,623	144,623
Adjusted opening balance	1-Jul-10	7,848,186	7,848,186		7,208,419	7,375,737
Interest			382,928			357,619
Repayments			-1,000,000			-1,020,000
Depreciation		-784,389			-802,641	
Closing balance	**30-Jun-11**	7,063,797	7,231,114	**30-Jun-12**	6,405,778	6,713,355

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Example

Lease Modifications

Eg: Lessee has 10yr lease for 2 floors office space. In year 6 an additional floor becomes available in the market.

A separate lease if both: *(Para 44)*

(a) the modification increases the scope of the lease by adding the right to use one or more underlying assets; and

(b) Increase in consideration for the lease is commensurate with the stand-alone price of the additional RoUA to reflect the circumstances of the particular contract.

Example

Lease Modifications

Eg. *Lessee has 10 year lease for office space.*
At the end of year 6 the lessee and lessor agree to amend the original lease and extend it by 4 years.

Lessee remeasures the lease liability:

- *On an 8 year remaining lease term*
- *Recognises the difference between carrying amounts of the lease (before and after), as an adjustment to the right-of-use asset*

Example

Lease Modifications

Eg. *Lessee has 10 year lease for office space.*
At the end of year 6 the lessee and lessor agree to amend the original lease to reduce the office space from 2 floors to 1 floor.

Lessee remeasures the lease liability:

- *Decreasing carrying amount of RoUA to reflect partial or full termination of the lease*
- *Recognise any gain or loss in the profit or loss*

Disclosures

a) amortisation charge for right-of-use assets by class of underlying asset

b) interest expense on lease liabilities

c) the expense relating to short-term leases accounted for applying exemption. (This expense need not include the expense relating to leases with a lease term of one month or less)

d) the expense relating to leases of low-value assets accounted for applying exemption. (excluding short-term leases of low-value assets included in (c))

(Para 53)

Disclosures (Cont.)

e) the expense relating to variable lease payments not included in the measurement of lease liabilities

f) income from subleasing right-of-use assets

g) total cash outflow for leases

h) additions to right-of-use assets

i) gains or losses arising from sale and leaseback transactions

j) the carrying amount of right-of-use assets at the end of the reporting period by class of underlying asset.

AASB 16 – *Transition*

Full Retrospective OR **Cumulative Catch-up**

Full Retrospective

how?

Apply AASB 8
- Prepare statements as if AASB 16 had always been applied
- Restate comparative information
- Disclose effect on each line item

Benefits?

Better quality of reported information in transition year

Cumulative Catch-up

how?

- Recognise cumulative effect on initial application in opening balance of retained earnings
- Do not restate comparative information
- Consider additional reliefs
- Disclose effect of applying cumulative catch-up approach

Benefits?

Significant cost relief on transition

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Draft Treasurer's Instruction FC 19 Leases

- Outlines approval, accounting and reporting
- Provides for delegated approvals
- Requires compliance with AASB 16
- Provides for Secretary of Treasury and Finance to determine accounting and reporting treatment in certain circumstances
  - Short term leases > $1 million

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Draft Treasurer’s Instruction FC 19 Leases

- Sets $10,000 as the low value threshold
- Determines accounting requirements for lease of:
  - Fleet vehicles
  - Office accommodation
  - Other individual assets
  - Group of underlying assets

Draft Treasurer's Instruction FC 19 Leases

- Transitional provisions
  - Low value and leases with remaining term <12 months to continue to be expensed
  - Lease with remaining term >12 months to be recognised on the balance sheet using partial retrospective recognition in accordance with paragraphs C7 to C13 of AASB 16
  - Deemed approval for existing leases