AASB Standard

AASB 2018-8
December 2018

Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities

[AASB 1, AASB 16, AASB 117, AASB 1049 & AASB 1058]

Australian Government

Australian Accounting Standards Board

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PREFACE

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AASB 2018-8 *AMENDMENTS TO AUSTRALIAN ACCOUNTING STANDARDS – RIGHT-OF-USE ASSETS OF NOT-FOR-PROFIT ENTITIES*

Australian Accounting Standard AASB 2018-8 *Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities* is set out on pages 5 – 9. All the paragraphs have equal authority.

Preface

Standards amended by AASB 2018-8

This Standard makes amendments to AASB 1 *First-time Adoption of Australian Accounting Standards* (July 2015), AASB 16 *Leases* (February 2016), AASB 117 *Leases* (August 2015), AASB 1049 *Whole of Government and General Government Sector Financial Reporting* (October 2007) and AASB 1058 *Income of Not-for-Profit Entities* (December 2016).

AASB 1058 made amendments to AASB 16 to require not-for-profit entities to measure right-of-use assets at initial recognition at fair value in respect of leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives.

However, the AASB has decided to provide a temporary option for not-for-profit entities to not measure a class or classes of such right-of-use assets at initial recognition at fair value, since further guidance is expected to be developed to assist not-for-profit entities in measuring right-of-use assets at fair value. The temporary option would also avoid requiring not-for-profit private sector entities at the lower level of the reporting thresholds to apply the fair value initial measurement requirements of AASB 16 when they might not be required to apply these requirements in the future as a result of recommendations of the ACNC Legislative Review.

Main features of this Standard

Main requirements

This Standard amends AASB 1, AASB 16, AASB 117, AASB 1049 and AASB 1058 to provide a temporary option for not-for-profit entities to not apply the fair value initial measurement requirements for right-of-use assets arising under leases with significantly below-market terms and conditions principally to enable the entity to further its objectives. The Standard requires an entity that elects to apply the option (i.e. measures a class or classes of such right-of-use assets at cost rather than fair value) to include additional disclosures in the financial statements to ensure users understand the effects on the financial position, financial performance and cash flows of the entity arising from these leases.

Application date

This Standard applies to annual periods beginning on or after 1 January 2019, with earlier application permitted, provided that AASB 1058 is also applied at the same time.

Accounting Standard AASB 2018-8

The Australian Accounting Standards Board makes Accounting Standard AASB 2018-8 *Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities* under section 334 of the *Corporations Act 2001*.

Kris Peach
Dated 24 December 2018 Chair – AASB

Accounting Standard AASB 2018-8
Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities

Objective

This Standard amends:

(a) AASB 1 *First-time Adoption of Australian Accounting Standards* (July 2015);

(b) AASB 16 *Leases* (February 2016);

(c) AASB 117 *Leases* (August 2015);

(d) AASB 1049 *Whole of Government and General Government Sector Financial Reporting* (October 2007); and

(e) AASB 1058 *Income of Not-for-Profit Entities* (December 2016);

to provide an option for not-for-profit entities to not apply the fair value initial measurement requirements to a class or classes of right-of-use assets arising under leases with significantly below-market terms and conditions principally to enable the entity to further its objectives. This Standard also adds additional disclosure requirements to AASB 16 for not-for-profit entities that elect to apply the option.

Application

The amendments set out in this Standard apply to entities and financial statements in accordance with the application of the other Standards set out in AASB 1057 *Application of Australian Accounting Standards* (as amended).

This Standard applies to annual periods beginning on or after 1 January 2019, except that the amendment to AASB 117 applies to periods beginning before 1 January 2019 if AASB 1058 is applied to such a period. Earlier application of this Standard is permitted, provided AASB 1058 is also applied to the period.

This Standard uses underlining, striking out and other typographical material to identify some of the amendments to a Standard, in order to make the amendments more understandable. However, the amendments made by this Standard do not include that underlining, striking out or other typographical material. Amended paragraphs are shown with deleted text struck through and new text underlined. Ellipses (…) are used to help provide the context within which amendments are made and also to indicate text that is not amended

Amendments to AASB 1 *First-time Adoption of Australian Accounting Standards* (July 2015)

Paragraphs AusD7.1, AusD9D.1 and AusD9D.2 are amended.

Deemed cost

…

AusD7.1 Notwithstanding paragraphs D5–D7, where a lessee is a not-for-profit entity ~~and the lease had at inception significantly below-market terms and conditions principally to enable the entity to further its objectives~~, the entity ~~shall~~ <u>may elect to</u> measure <u>a class of</u> ~~the~~ right-of-use ~~asset~~ <u>assets arising under leases that had at inception significantly below-market terms and conditions principally to enable the entity to further its objectives</u> at fair value at the beginning of the current period presented in the entity's first

Australian-Accounting-Standards financial statements or at the previous GAAP valuation if that valuation broadly reflects that fair value.

…

Leases

…

AusD9D.1 Notwithstanding paragraphs D9B–D9D, where a lessee is a not-for-profit entity and the lease had at inception significantly below-market terms and conditions principally to enable the entity to further its objectives, all references in those paragraphs to the date of transition to Australian Accounting Standards shall be read as referring to the beginning of the current period presented in the entity's first Australian-Accounting-Standards financial statements. Consequently, the entity shall measure the lease liability and the right-of-use asset at that date. ~~The right-of-use asset shall be measured in accordance with paragraph AusD7.1.~~

AusD9D.2 Where a lessee is a not-for-profit entity and ~~the lease~~ elects to measure at fair value in accordance with paragraph AusD7.1 a class of right-of-use assets arising under leases that had at inception significantly below-market terms and conditions principally to enable the entity to further its objectives, the entity shall also recognise any related items in accordance with paragraph 9 of AASB 1058 *Income of Not-for-Profit Entities*. Any income arising shall be recognised as an adjustment to the opening balance of retained earnings (or another component of equity, as appropriate) at the beginning of the current period presented in the entity's first Australian-Accounting-Standards financial statements.

Amendments to AASB 16 *Leases* (February 2016)

Paragraphs Aus25.1, AusC5.1, AusC8.1 and AusC11.1 are amended and paragraphs Aus59.1 and Aus59.2 are added. Paragraph AusC5.2 has not been amended but has been included for ease of reference.

Aus25.1 Notwithstanding paragraphs 23–25, where the lessee is a not-for-profit entity, ~~and the lease has significantly below-market terms and conditions principally to enable the entity to further its objectives, the right-of-use asset shall initially be measured~~ the lessee may elect to measure right-of-use assets on a class-by-class basis at initial recognition at fair value in accordance with AASB 13 *Fair Value Measurement* for leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives. AASB 1058 *Income of Not-for-Profit Entities* addresses the recognition of related amounts.

…

Aus59.1 In addition to the disclosures required in paragraphs 53–59, where a lessee is a not-for-profit entity and elects to measure a class or classes of right-of-use assets at initial recognition at cost in accordance with paragraphs 23–25 for leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives, the lessee shall disclose additional qualitative and quantitative information about those leases necessary to meet the disclosure objective in paragraph 51. This additional information shall include, but is not limited to, information that helps users of financial statements to assess:

(a) the entity's dependence on leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives; and

(b) the nature and terms of the leases, including:

(i) the lease payments;

(ii) the lease term;

(iii) a description of the underlying assets; and

(iv) restrictions on the use of the underlying assets specific to the entity.

Aus59.2 The disclosures provided by a not-for-profit entity in accordance with paragraph Aus59.1 shall be provided individually for each material lease that has significantly below-market terms and conditions principally to enable the entity to further its objectives or in aggregate for leases involving right-of-use assets of a similar nature. An entity shall consider the level of detail necessary to satisfy the disclosure objective and how much emphasis to place on each of the various requirements. An entity shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have substantially different characteristics.

…

AusC5.1 Not-for-profit entities electing to measure a class of right-of-use assets at initial recognition at fair value and applying this Standard retrospectively in accordance with paragraph C5(a) to leases that at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives shall:

(a) measure ~~the~~ each right-of-use asset in the class at fair value;

(b) measure the lease liability in accordance with this Standard; and

(c) recognise any related items in accordance with paragraph 9 of AASB 1058 *Income of Not-for-Profit Entities*.

Any income arising shall be recognised as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the beginning of the earliest prior period presented.

AusC5.2 Notwithstanding paragraph AusC5.1, not-for-profit entities that adopted AASB 1058 in an earlier reporting period are not required to remeasure the fair value of the right-of-use asset arising from leases that (1) at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives and (2) were previously classified as finance leases applying AASB 117. Instead, the entity shall transition those leases in accordance with paragraph C11, regardless of which transition option in paragraph C5 is applied.

…

AusC8.1 Not-for-profit entities electing to measure a class of right-of-use assets at initial recognition at fair value and applying this Standard retrospectively in accordance with paragraph C5(b) to leases that (1) at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives and (2) were previously classified as operating leases applying AASB 117 shall:

(a) notwithstanding paragraph C8(b), measure ~~the~~ each right-of-use asset in the class at fair value at the date of initial application of this Standard;

(b) measure the lease liability in accordance with paragraph C8(a); and

(c) recognise any related items in accordance with paragraph 9 of AASB 1058.

Any income arising shall be recognised as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the date of initial application of this Standard.

…

AusC11.1 Subject to paragraph AusC5.2 and notwithstanding paragraph C11, not-for-profit entities electing to measure a class of right-of-use assets at initial recognition at fair value and applying this Standard retrospectively in accordance with paragraph C5(b) to leases that (1) at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives and (2) were previously classified as finance leases applying AASB 117 shall:

(a) measure ~~the~~ each right-of-use asset in the class at fair value at the date of initial application of this Standard;

(b) measure the lease liability in accordance with this Standard; and

(c) recognise any related items in accordance with paragraph 9 of AASB 1058.

Any income arising shall be recognised as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the date of initial application of this Standard.

Amendments to AASB 117 *Leases* (August 2015)

The amendment to AASB 117 applies to periods beginning before 1 January 2019. This means that the amendment applies only if AASB 1058 is applied to an earlier period.

Paragraph Aus20.1 is amended.

Finance Leases

Initial recognition

…

Aus20.1 Notwithstanding paragraph 20, a not-for-profit entity may elect to measure a class of ~~the~~ leased assets ~~asset shall initially be measured~~ at initial recognition at fair value in accordance with AASB 13 *Fair Value Measurement* for leases where:

(a) at inception the lease has significantly below-market terms and conditions principally to enable the lessee to further its objectives; and

(b) the lessee applies AASB 1058 *Income of Not-for-Profit Entities* to the period.

AASB 1058 addresses the recognition of related amounts.

Amendments to AASB 1049 *Whole of Government and General Government Sector Financial Reporting* (October 2007)

Paragraph 13D is added.

Compliance with Australian Accounting Standards and the ABS GFS Manual

…

13D Notwithstanding paragraph 13, a government may elect to measure a class of right-of-use assets at initial recognition at cost or at fair value in accordance with AASB 16 *Leases* for leases that had at inception significantly below-market terms and conditions principally to enable the entity to further its objectives.

Amendments to AASB 1058 *Income of Not-for-Profit Entities* (December 2016)

Paragraphs C10 and C11 are amended and paragraph C10A is added.

Leases with significantly below-market terms and conditions

…

Leases classified as finance leases

C10 If an entity elects to measure a class of right-of-use assets at initial recognition at fair value and applies this Standard before applying AASB 16, for leases that (1) at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives and (2) were classified as finance leases in accordance with AASB 117, and if an entity elects to apply this Standard in accordance with:

(a) paragraph C3(a) – the entity shall:

(i) measure ~~the~~ each leased asset in the class at fair value at the beginning of the earliest period presented;

(ii) measure the lease liability in accordance with AASB 117;

(iii) recognise any related items in accordance with paragraph 9; and

(iv) recognise any income arising as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the beginning of the earliest period presented; or

(b) paragraph C3(b) – the entity shall:

(i) measure ~~the~~ each leased asset in the class at fair value at the date of initial application of this Standard;

(ii) measure the lease liability in accordance with AASB 117;

(iii) recognise any related items in accordance with paragraph 9; and

(iv) recognise any income arising as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the date of initial application of this Standard.

C10A If an entity elects not to measure a class of right-of-use assets at initial recognition at fair value and applies this Standard before applying AASB 16, for leases that (1) at inception had significantly below-market terms and conditions principally to enable the entity to further its objectives and (2) were classified as finance leases in accordance with AASB 117, the entity shall continue to apply its accounting policy under AASB 117 to those finance leases. On transition to AASB 16, the entity shall apply the transition requirements of that Standard to leases classified as finance leases in accordance with AASB 117.

C11 An entity applying paragraph C10 may, as a practical expedient, apply the paragraph ~~C10~~ to a portfolio of leases with similar characteristics if the entity reasonably expects that the effects on the financial statements of this approach would not differ materially from applying paragraph C10 to the individual leases within that portfolio. If accounting for a portfolio, an entity shall use estimates and assumptions that reflect the size and composition of the portfolio.

Commencement of the legislative instrument

For legal purposes, this legislative instrument commences on 31 December 2018.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, AASB 2018-8 Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities.

Introduction

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's considerations in reaching the conclusions in this Standard. It sets out the reasons why the Board developed the Standard, the approach taken to developing the Standard and the key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.

Reasons for issuing this Standard

BC2 AASB 1058 *Income of Not-for-Profit Entities* and AASB 16 *Leases* are effective for annual reporting periods beginning on or after 1 January 2019. These Standards require not-for-profit entities to measure right-of-use assets at initial recognition at fair value for leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives.

BC3 For ease of reference in this Basis for Conclusions, leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives are referred to as 'concessionary leases'.

BC4 The Board considered comments from stakeholders in the not-for-profit sector preparing for the implementation of AASB 16 and AASB 1058, some of whom expressed difficulties in applying the principles in AASB 13 *Fair Value Measurement* in determining the fair value of right-of-use assets arising under concessionary leases. The difficulties noted included how often-significant restrictions on the right of use of the underlying assets and the specialised nature of the underlying assets should be incorporated in the valuation of right-of-use assets arising from concessionary leases.

BC5 Whilst other assets required by other Standards to be fair valued might also be subject to restrictions on use or specialised in nature, the Board noted that the issues related to right-of-use assets for lessees might be different to the issues for owners of the assets, making it difficult to determine the fair value of right-of-use assets simply by reference to the fair value of the underlying assets. Since the principles in AASB 13 are based on market participants buying and selling assets, further guidance appears to be needed to assist not-for-profit entities in applying the principles to right-of-use assets in concessionary lease arrangements.

BC6 The Board considered the prevalence and magnitude of concessionary leases in the not-for-profit sector, and the significance of restrictions on rights of use of the underlying assets in many cases. The Board also noted that a temporary option for not-for-profit lessees to not measure a class (or classes) of right-of-use assets at initial recognition at fair value for concessionary leases would avoid undue cost and effort being incurred by preparers in applying AASB 13 in the absence of additional guidance. The Board assessed these factors with reference to *The AASB's Not-for-Profit Entity Standard-Setting Framework* and decided to propose the temporary option. The interpretative issues arising from fair valuing right-of-use assets arising under concessionary leases will be addressed in the AASB's Fair Value Measurement for Public Sector Entities project.

BC7 The Board also noted that the financial reporting thresholds for not-for-profit private sector entities may be revised as a result of the ACNC Legislative Review recommendations. It is possible that entities at the lower level of the reporting thresholds might not be required in future to apply the requirements of AASB 16 and AASB 1058. The temporary option would avoid such smaller entities incurring costs in measuring right-of-use assets at initial recognition at fair value when they might be exempted from this requirement in future by not being required to prepare financial statements that comply with Accounting Standards.

BC8 However, as some not-for-profit entities had already commenced the process of determining the fair value of right-of-use assets in concessionary leases, the Board decided to make the temporary relief optional. This allows these entities to continue their work on fair valuing concessionary leases and applying the fair value initial recognition measurement requirements to measure right-of-use assets.

BC9 Entities electing not to measure the right-of-use assets in concessionary leases at fair value will recognise the assets at cost in accordance with AASB 16 (paragraphs 23–25), which incorporates the amount of the initial measurement of the lease liability.

BC10 The optional relief will be reassessed when further guidance has been developed to assist not-for-profit entities in fair valuing right-of-use assets and the financial reporting requirements for private sector not-for-profit entities have been finalised. The Board will consider whether to provide a permanent option for not-for-profit entities to measure a class of right-of-use assets at initial recognition either at cost or at fair value for those concessionary leases entered into prior to the application date of AASB 16 or for all concessionary leases.

Issue of ED 286 *Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities*

BC11 The Board's proposals were exposed for public comment in November 2018 through Exposure Draft ED 286 *Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities*.

BC12 The Board received feedback on its proposals through 20 submissions on ED 286. The responses to ED 286 indicated that:

(a) all respondents agreed that not-for-profit entities should be given some form of relief to not measure right-of-use assets for concessionary leases at initial recognition at fair value. Some respondents agreed that the relief should only be given on a temporary basis until further guidance has been developed to assist not-for-profit entities in fair valuing right-of-use assets and the financial reporting requirements for not-for-profit private sector entities have been finalised. However, other respondents were of the view that the option to elect either cost or fair value measurement should be made available on a permanent basis for all concessionary leases and for not-for-profit entities in both the private sector and the public sector; and

(b) most respondents agreed that the proposed additional disclosure requirements in AASB 16 would provide adequate information for users of the financial statements to understand the effects on the financial position, financial performance and cash flows of the entity arising from concessionary leases in the absence of fair value information. However, some respondents suggested providing further clarification to ensure not-for-profit entities understand the disclosure requirements.

BC13 The Board considered the feedback and in December 2018 decided to finalise its decisions to provide a temporary option for not-for-profit entities to elect to measure a class of right-of-use assets arising under concessionary leases at cost or at fair value at initial recognition. At a later time, when fair value measurement guidance has been developed and the not-for-profit private sector financial reporting requirements have been finalised, the Board will consider whether the temporary option should be made permanent.

Election of measurement basis

BC14 Some ED 286 respondents noted that there might be instances where an entity may wish to apply the option of not fair valuing right-of-use assets for concessionary leases only to some, but not all, of the right-of-use assets. This may be the case for example where the not-for-profit entity has elected to apply the revaluation model under AASB 116 *Property, Plant and Equipment* to a class of property, plant and equipment and would therefore likely elect to measure right-of-use assets that relate to that class also at fair value, as permitted by AASB 16, paragraph 35. However, this should not force the entity to also measure all other right-of-use assets arising from concessionary leases on initial recognition at fair value.

BC15 Consequently, the Board decided that the election of the measurement basis for initial recognition of right-of-use assets of concessionary leases should be made by class of right-of-use assets. As specified in other Standards, a class is a grouping of assets of a similar nature and use in an entity's operations.

Disclosures

BC16 In the absence of fair value information, the Board decided that entities electing to measure a class of right-of-use assets at initial recognition at cost rather than at fair value would need to make additional disclosures. This will ensure adequate information is disclosed for users of financial statements to understand the effects on the financial position, financial performance and cash flows of the entity arising from concessionary leases.

BC17 A number of ED 286 respondents expressed concerns that, without reference to fair value information, it might be difficult to assess whether a concessionary lease is material and therefore requires individual disclosures under AASB 16, paragraph Aus59.2.

BC18 AASB 101 paragraph 7 defines when information is material and AASB Practice Statement 2 *Making Materiality Judgements* provides further guidance, including in relation to disclosure requirements. When

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making materiality judgements, an entity needs to take into account how information could reasonably be expected to influence the primary users of its financial statements when they make decisions on the basis of those statements. In respect of not-for-profit entities, primary users of financial statements are concerned with the ability of the entity to achieve its objectives. Therefore, when assessing whether a concessionary lease is material to the financial statements, the entity could consider factors such as the significance of the concessionary lease to the entity's operations in fulfilling its objectives.

BC19 Some respondents recommended the Board consider clarifying the extent of disclosures required in AASB 16 paragraphs Aus59.1 and Aus59.2. Consistent with AASB Practice Statement 2, an entity applies judgement in determining the level of detail necessary to satisfy the disclosure objective, including the level of aggregation or disaggregation of disclosures so that useful information is not obscured. The Board notes that AASB 16 paragraph Aus59.2 requires disclosures to be made individually for each material lease and permits aggregated disclosures for other concessionary leases involving right-of-use assets of a similar nature.

GAAP/GFS convergence

BC20 Several respondents commented that measuring right-of-use assets at either cost or fair value could result in Government Finance Statistics (GFS) convergence differences. As the ABS GFS Manual continues to distinguish operating leases and finance leases, some of these convergence differences relate to the underlying principles of AASB 16. However, a new convergence difference would arise if right-of-use assets under concessionary leases that would previously have been classified as finance leases are measured at cost under the temporary option, rather than at fair value. On balance, the Board considered that it was appropriate to provide not-for-profit entities with the temporary option in respect of such concessionary leases.

BC21 Consequently, the Board added an exception to AASB 1049 (paragraph 13D) to permit public sector entities to measure right-of-use assets arising under concessionary leases at initial recognition at cost, rather than fair value.

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