

A photograph of a modern, multi-level architectural interior. The space is characterized by white, curved walkways and railings. A long, straight staircase with wooden steps and metal railings leads upwards from the bottom center. The ceiling features a series of curved, teal-colored light fixtures. The overall atmosphere is bright and clean, with a focus on geometric forms and light. A semi-transparent white banner is overlaid across the middle of the image, containing text.

TRANSITION TO AASB/IFRS 16

September 2018

ALETTA BOSHOFF
PARTNER & NATIONAL LEADER, IFRS ADVISORY



INTRODUCTION

OUTLINE OF THIS WEBINAR

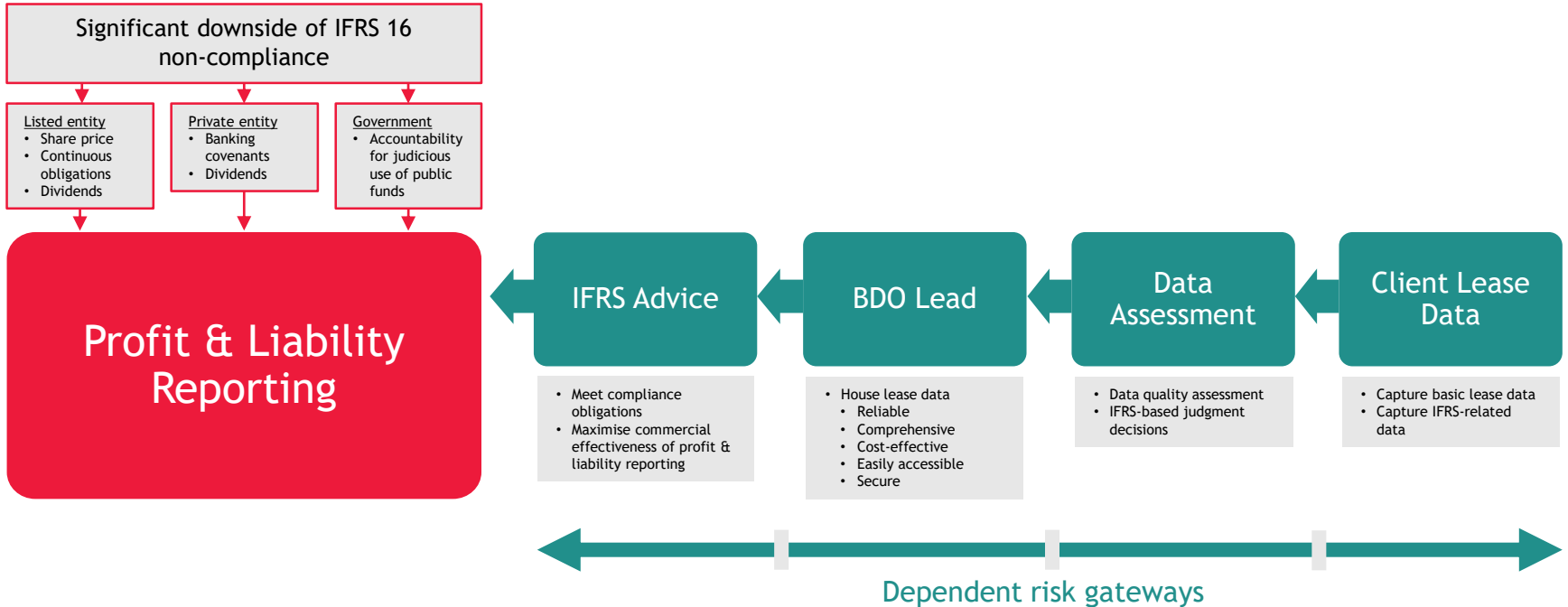
- ▶ What is the business problem?
- ▶ 1 January 2019 - The Clock is Ticking Down!
- ▶ Retrospective Application Options for Lessees
- ▶ Practical Expedients - Modified Retrospective Approach
- ▶ Definition of a Lease
- ▶ Illustration and Comparison of Transition Approaches
- ▶ Peppercorn Leases
- ▶ Next Steps
- ▶ Do you need assistance?



WHAT IS THE BUSINESS PROBLEM?

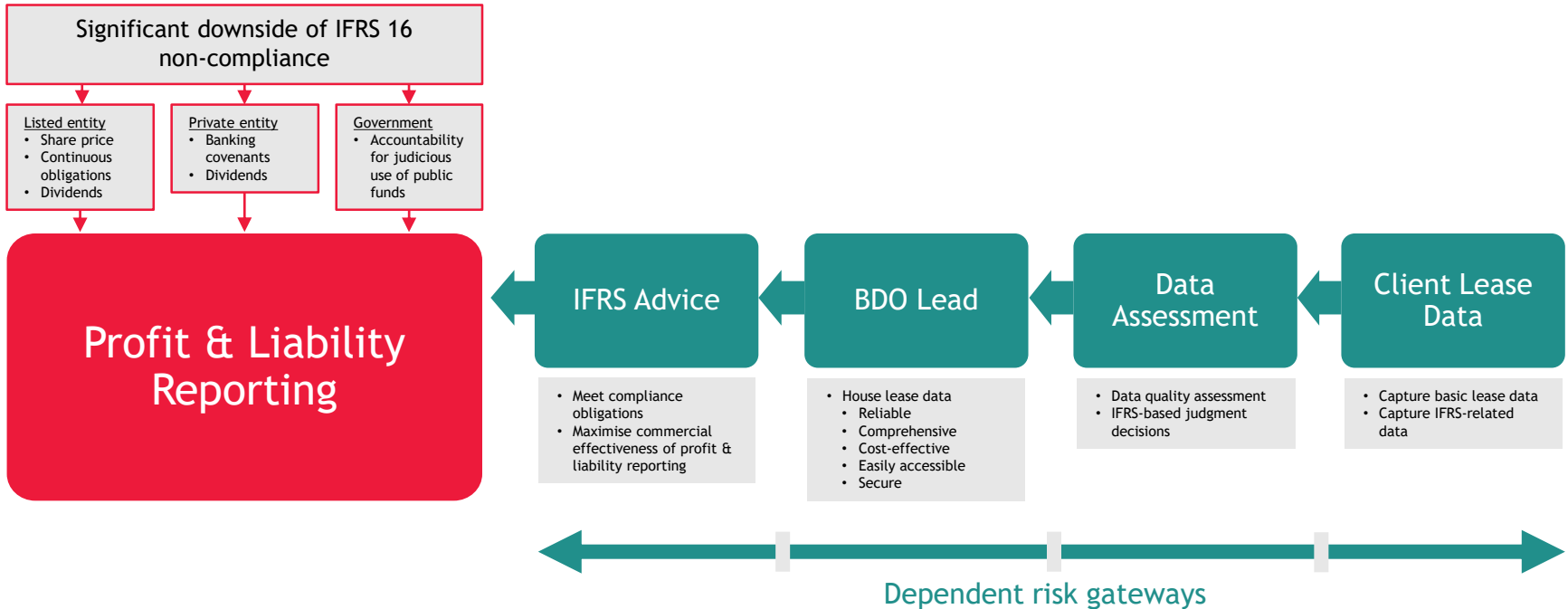
Private Sector Entities - Preserve Shareholder Value

IFRS 16 will create winners and losers for organisations with multiple leases, depending on how effectively they control the risk at each point in the lease management lifecycle.



Public Sector Entities & NFP Entities - Maintain Public Support

IFRS 16 will create winners and losers for organisations with multiple leases, depending on how effectively they control the risk at each point in the lease management lifecycle.





AFR, 5 SEPTEMBER 2018

<https://www.afr.com/business/retail/myer-woolworths-hardest-hit-by-new-lease-accounting-standard-20180905-h14yqo>

Myer, Woolworths hardest hit by new lease accounting standard



AFR, 9 JULY 2017

<https://www.afr.com/business/retail/wesfarmers-woolworths-among-retailers-bracing-for-new-lease-accounting-rules-20170706-gx69ij>

Wesfarmers, Woolworths liabilities to double under lease accounting change

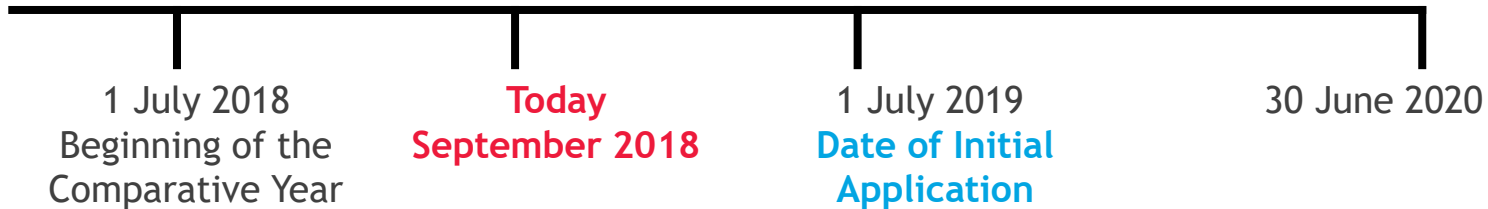
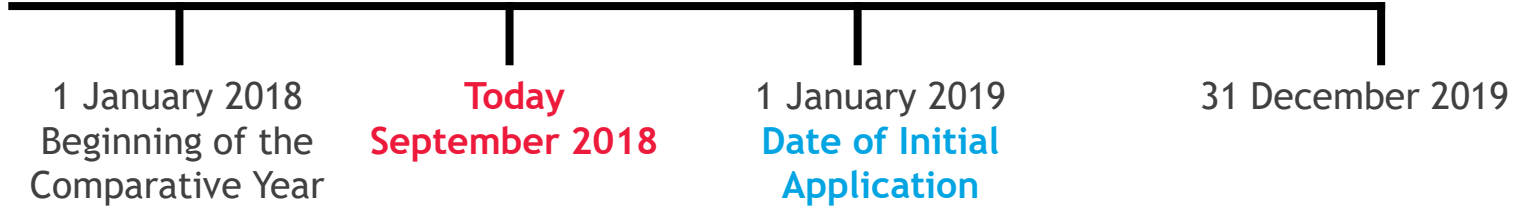


1 JANUARY 2019 - THE CLOCK IS TICKING DOWN!

EFFECTIVE DATE OF IFRS 16

Accounting Standard	Effective Date - Years Beginning on or after ...	31 December Year-ends	30 June Year-ends
AASB/IFRS 16 <i>Leases</i>	1 January 2019	31 December 2019	30 June 2020

WHY NOW?





RETROSPECTIVE APPLICATION OPTIONS FOR LESSEES

RETROSPECTIVE APPLICATION OPTIONS FOR LESSEES

<u>Full Retrospective Method</u>	<u>Modified Retrospective Method</u>
<ul style="list-style-type: none">• Comparatives restated• Cumulative effect recognised as adjustment to opening equity at the <u>start of the earliest comparative period presented</u>• Third statement of financial position presented at start of preceding period• n/a• Limited transitional relief	<ul style="list-style-type: none">• Comparatives not restated• Cumulative effect recognised as adjustment to opening equity at the <u>start of the current period</u> ('date of initial application')• Third statement of financial position not required• Two approaches for calculating RoU asset on a lease by lease basis• More extensive transitional relief



FULL RETROSPECTIVE APPROACH

- ▶ Comparative figures are restated as if IFRS 16 had always been in effect
- ▶ Disclosure
 - Current year per IFRS 16
 - Comparative year per IFRS 16
 - Restate retained earnings at the beginning of the comparative year

MODIFIED RETROSPECTIVE APPROACH #1

- ▶ The lease liability is net present value of the remaining (i.e. future) lease payments using the incremental borrowing rate at the date of initial application
- ▶ The right-of-use (RoU) asset is recognized at the date of initial application as an amount equal to the lease liability, using the prevailing incremental borrowing rate at the date of initial application
- ▶ Adjusted for any prepaid or accrued lease payments relating to that lease that were recognised in the statement of financial position immediately before the date of initial application

MODIFIED RETROSPECTIVE APPROACH #2

- ▶ Lease liability calculated in the same way as under the modified retrospective approach #1
- ▶ That is, the lease liability is net present value of the remaining (i.e. future) lease payments using the incremental borrowing rate at the date of initial application
- ▶ The RoU asset is recognized as at the date of initial application as if IFRS 16 had always been applied
- ▶ BUT calculated as if the prevailing incremental borrowing rate as at the date of initial application also applied at lease commencement

Retrospective Application Options for Lessees

Full Retrospective Approach

Modified Retrospective Approach

Modified Retrospective Approach #1

RoU Asset = Lease Liability -
Accrual/Prepayment ito old AASB
117

Modified Retrospective Approach #2

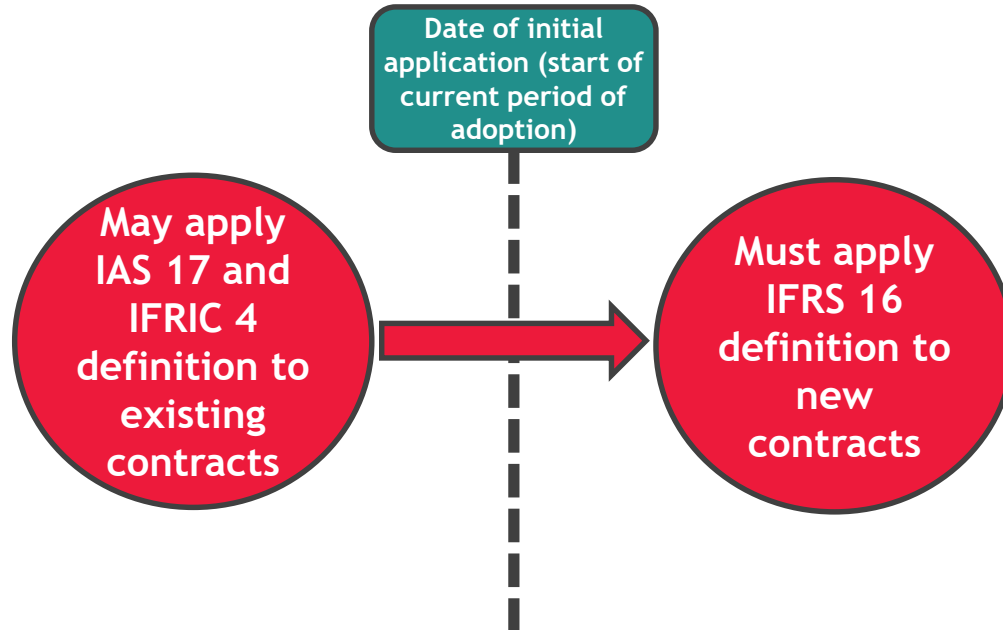
RoU Asset is calculated on a retrospective basis & practical expedients available in its calculation AND the prevailing incremental borrowing rate at the date of initial application is used

HAVE YOU DECIDED ON A TRANSITIONAL APPROACH?

- ▶ Preparers should consult with the relevant financial statement users and those charged with governance (the Board and/or Audit Committee) to assist them in determining which approach to transition is most suitable for their needs
- ▶ Benefits of the full retrospective method
 - Comparable information
- ▶ Benefits of the two modified retrospective approaches
 - Simpler due to more practical expedients

DEFINITION OF A LEASE

PRACTICAL EXPEDIENT #1 - DEFINITION OF A LEASE





PRACTICAL EXPEDIENTS - MODIFIED RETROSPECTIVE APPROACH

MODIFIED RETROSPECTIVE - OTHER PRACTICAL EXPEDIENTS

#2: Apply a single discount rate to a portfolio of leases with reasonably similar characteristics

#3: Use onerous lease assessment and any provision recognised immediately before date of application instead of an IAS 36 impairment test

#4: Exclude initial direct costs from the measurement of right-of-use assets at the date of initial application

#5: No requirement to recognise leases when the term ends within 12 months of the date of initial application

#6: Use hindsight, such as in determining the lease term, if the contract contains options to extend or terminate the lease

OPTIONAL TRANSITIONAL RELIEFS

Summary

	PE #1 Definition	PE #2 Portfolio discount rate	PE #3 Relief from IAS 36	PE #4 Direct Costs	PE #5 Remaining term < 12 months	PE #6 Hindsight
Full Retrospective Method	✓	✗	✗	✗	✗	✗
Modified Retrospective Method (RoU measurement approach #1)	✓	✓	✓	n/a	✓	n/a
Modified Retrospective Method (RoU measurement approach #2)	✓	✓	✓	✓	✓	✓



ILLUSTRATION AND COMPARISON OF TRANSITION APPROACHES

EXAMPLE

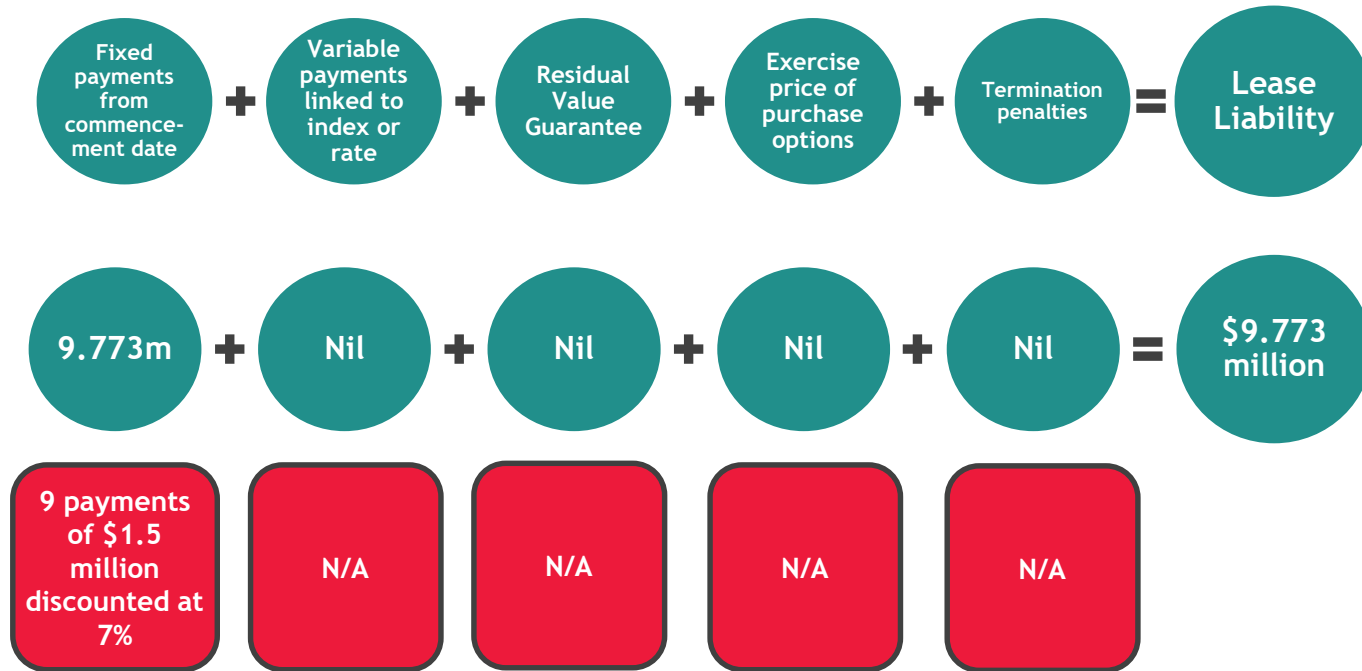
- ▶ Entity A enters into a 10 year lease for a piece of equipment on 1 January 2017 and in the process, incurs \$500 of initial direct costs in the form of commissions, which were expensed under IAS 17
- ▶ Entity A will pay the lessor \$1,500 per annum on 1 January of each year
- ▶ The lease does not contain any termination, extension or purchase options
- ▶ The rate implicit in the lease is 7%.
- ▶ Entity A's incremental borrowing rate as at 1 January 2019 is 5%.

EXAMPLE

- ▶ The lease was previously classified as an operating lease under IAS 17
- ▶ The following additional assumptions are made:
 - The contract meets the definition of a lease under both IAS 17 and IFRS 16
 - The lease does not meet the low value or short-term lease exemptions under IFRS 16
 - Entity A has a calendar year-end, so IFRS 16 is effective as of 1 January 2019
 - Entity A will use the cost model to amortise the RoU asset

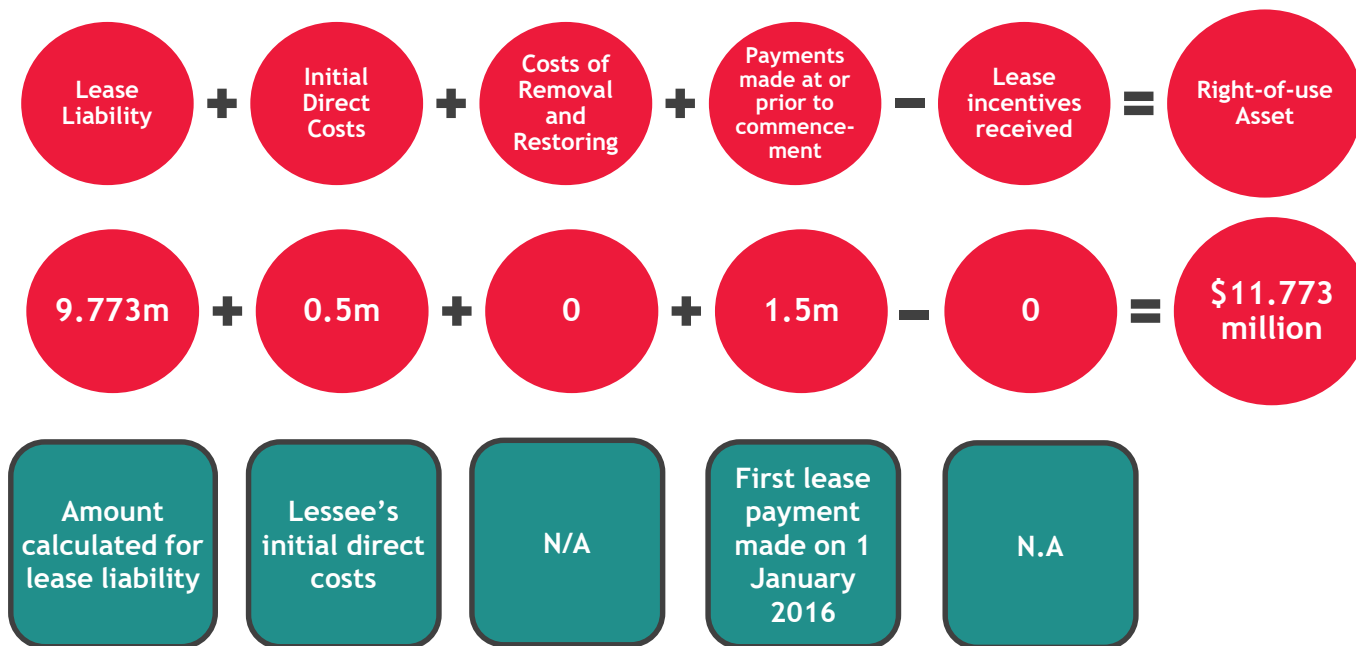
EXAMPLE - FULL RETROSPECTIVE APPROACH

Calculate the Lease Liability at 1 January 2016



EXAMPLE - FULL RETROSPECTIVE APPROACH

Calculate the RoU Asset at 1 January 2016



EXAMPLE - FULL RETROSPECTIVE APPROACH

Calculate the Lease Liability at 1 January 2018 and 1 January 2019

Year Ended	Opening Balance (A)	Payment (B)	Interest (C) (A - B) * 7%	Closing Balance (A - B + C)
31 December 2016	\$9,773	-	\$684	\$10,457
31 December 2017	\$10,457	\$1,500	\$627	\$9,584
31 December 2018	\$9,584	\$1,500	\$566	\$8,650

EXAMPLE - FULL RETROSPECTIVE APPROACH

Calculate the RoU Asset at 1 January 2018 and 1 January 2019

Year Ended	Opening Balance	Amortisation Charge	Closing Balance
31 December 2016	\$11,773	\$1,173	\$10,596
31 December 2017	\$10,596	\$1,173	\$9,419
31 December 2018	\$9,419	\$1,173	\$8,242

EXAMPLE - FULL RETROSPECTIVE APPROACH

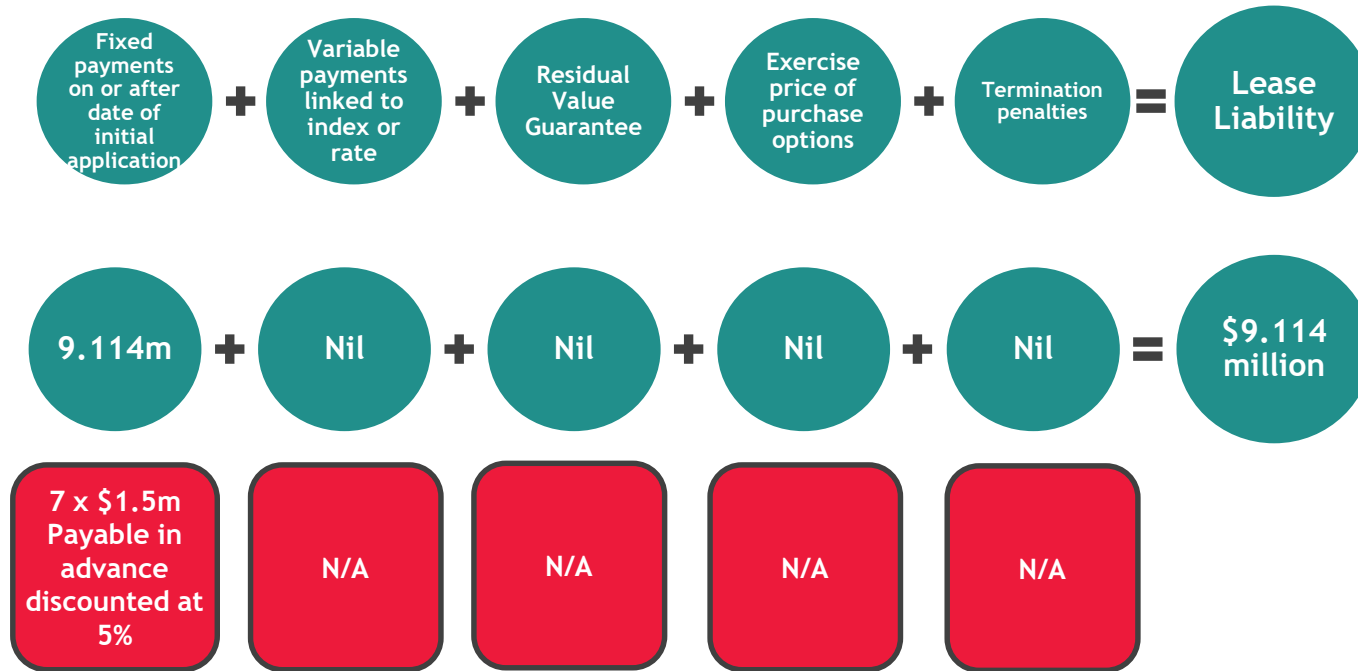
Summary

	31 December 2018 (1 January 2019)	31 December 2017 (1 January 2018)
RoU Asset	\$8,242	\$9,419
Lease Liability	\$8,650	\$9,584
Adjustment to Equity	(\$408)	(\$165)

Dr RoU Asset	\$8,242	
Cr Lease Liability		\$8,650
Dr Opening retained earnings (1 January 2019)	\$408	

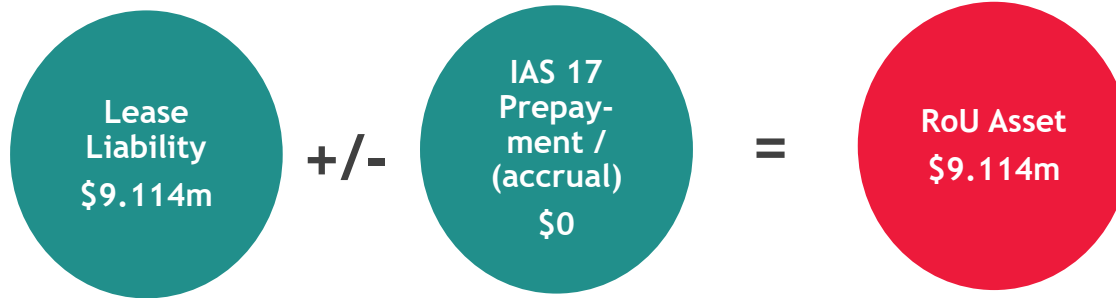
EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #1

Calculate the Lease Liability at 1 January 2019



EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #1

Calculate the RoU Asset at 1 January 2019



EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #1

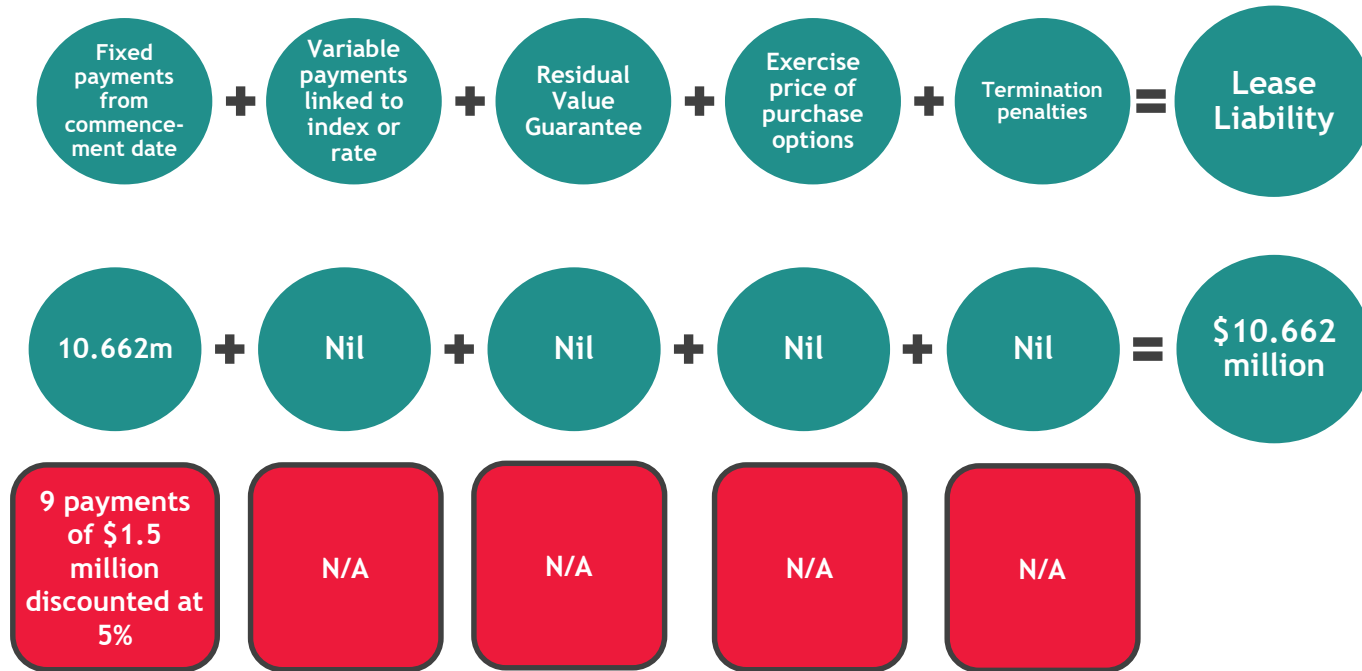
Summary

	1 January 2019	31 December 2018	1 January 2018
RoU Asset	\$9,114	-	-
Lease Liability	\$9,114	-	-
Adjustment to Equity	\$0	-	-

Dr RoU Asset	\$9,114	
Cr Lease Liability		\$9,114
Dr Opening retained earnings (1 January 2019)	\$0	

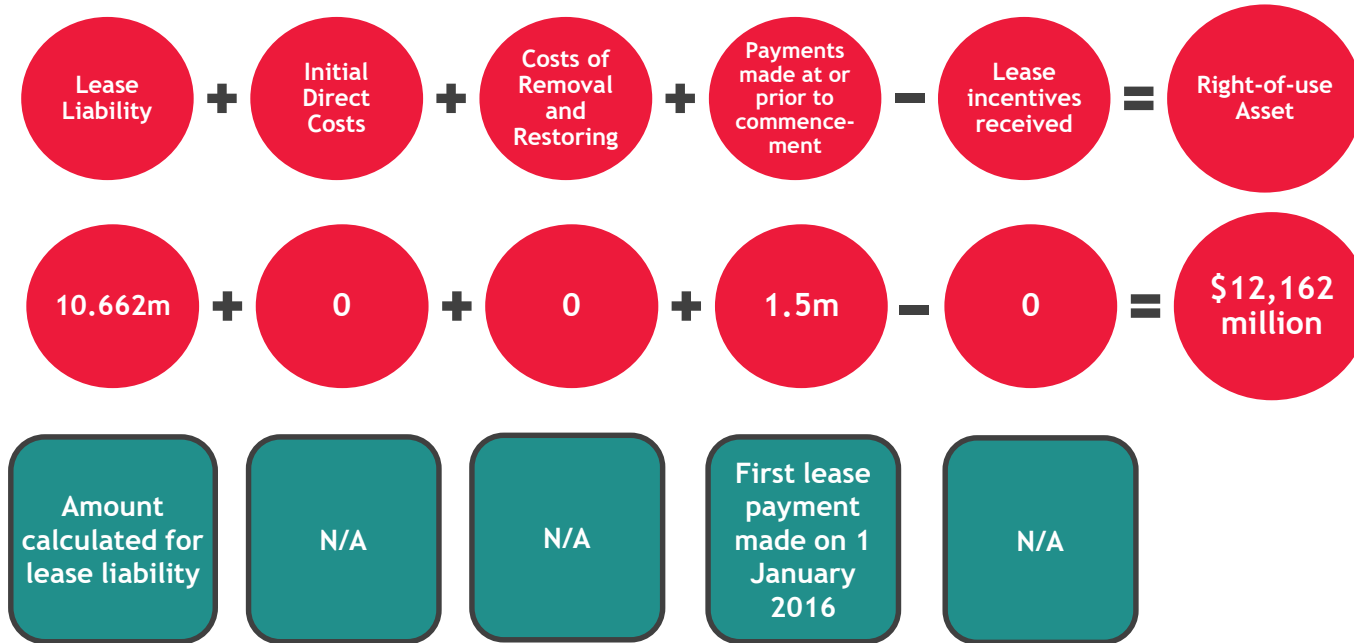
EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #2

Calculate the Lease Liability at 1 January 2016



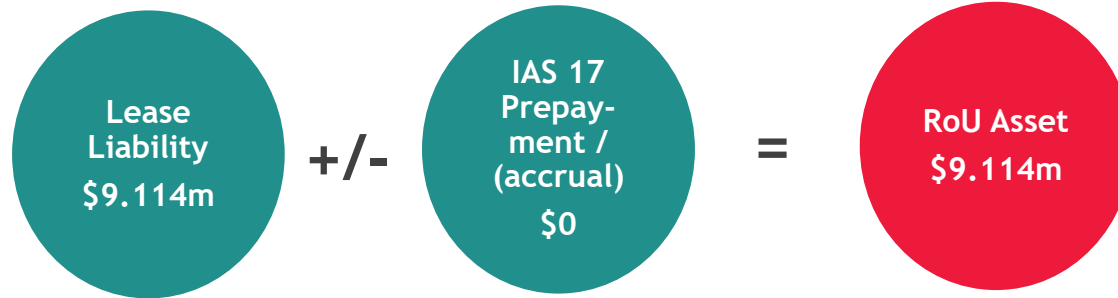
EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #2

Calculate the RoU Asset at 1 January 2016



EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #2

Calculate the RoU Asset at 1 January 2019



EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #2

Calculate the RoU Asset at 1 January 2018 and 1 January 2019

Year Ended	Opening Balance	Amortisation Charge	Closing Balance
31 December 2016	\$12,162	\$1,216	\$10,946
31 December 2017	\$10,946	\$1,216	\$9,730
31 December 2018	\$9,730	\$1,216	\$8,514

EXAMPLE - MODIFIED RETROSPECTIVE APPROACH #2

Summary

	1 January 2019	31 December 2018	1 January 2018
RoU Asset	\$8,514	-	-
Lease Liability	\$9,114	-	-
Adjustment to Equity	(\$600)	-	-

Dr RoU Asset	\$8,514	
Cr Lease Liability		\$9,114
Dr Opening retained earnings (1 January 2019)	\$600	



COMPARISON

- ▶ Only with the modified retrospective approach #1 is there no impact to equity on first time application to IFRS
- ▶ The two versions of the modified retrospective approach can be adopted on a lease-by-lease basis



PEPPERCORN LEASES

PEPPERCORN LEASES

Amendment to new AASB 16 *Leases*

- Where the lessee is a NFP entity and the lease has 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 the lease payments that are not paid at that date; and
 - Recognise any related items in accordance with AASB 1058 (potentially income?)

EXAMPLE

- School A enters a 30 year lease with a lessor for the use of a building
- The lease contract specifies lease payments of \$100 per annum
- At the inception of the lease, the entity assesses the terms and conditions of the lease, including restrictions, and determines the fair value of the right to use the facility for 30 years is \$360,000
- The leased premises must be used to provide education services, or else School A will no longer be able to use the facility
- There are no other conditions specified in the lease contract
- Assume the NPV of the future lease payments discounted at School A's incremental borrowing rate of 5% per annum is \$1,537

EXAMPLE

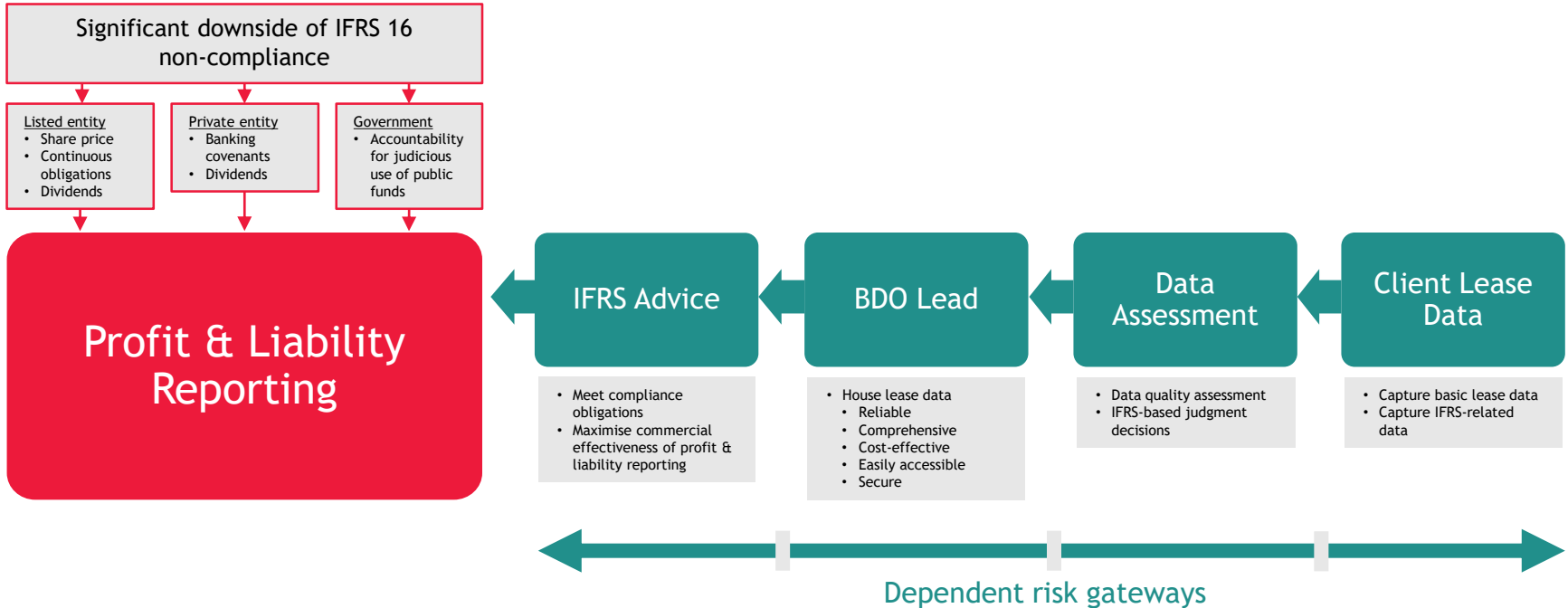
- The journal entry on initial recognition is:
 - DrRight-of-use asset \$360,000
 - CrLease liability \$1,537
 - CrIncome \$358,463



NEXT STEPS

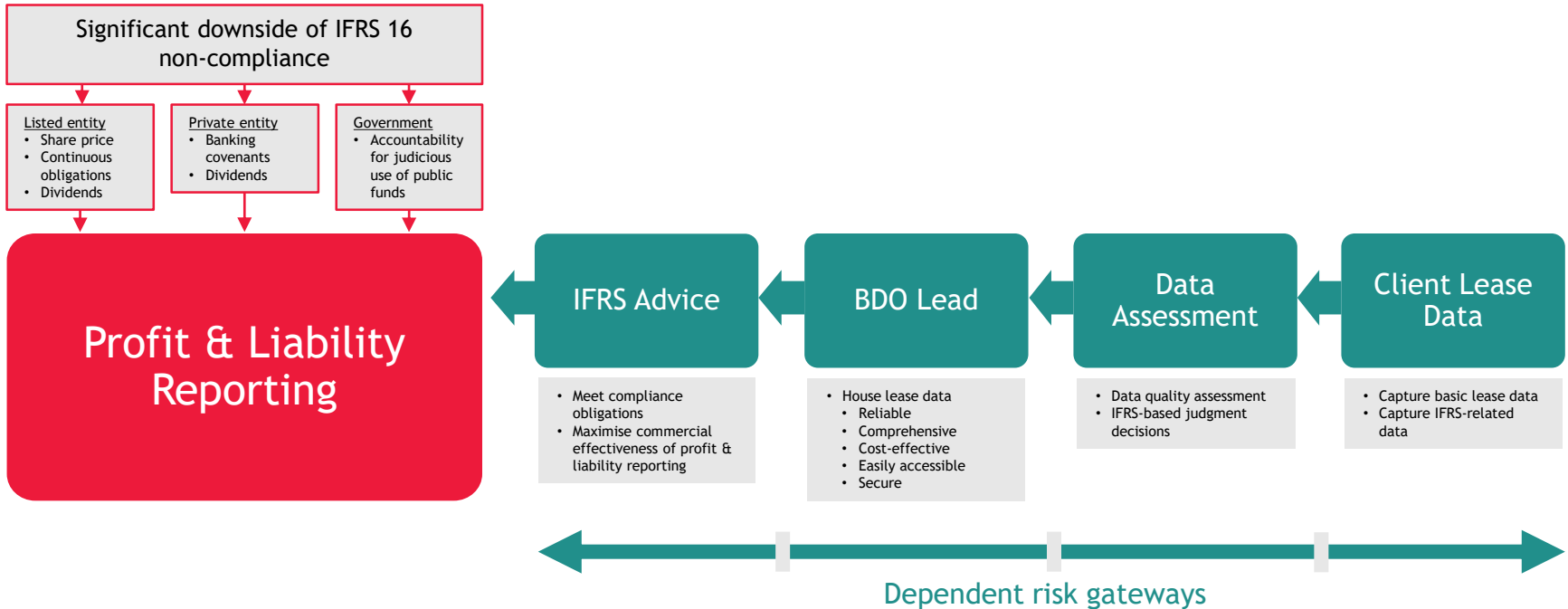
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BDO LEAD - OUR VERY OWN BDO AASB 16 TECHNOLOGY SOLUTION

<https://www.bdo.com.au/en-au/services/audit-assurance/ifrs-advisory-services/aasb-16/lease-management-ifrs-16-tool>



NEXT STEPS

- ▶ Do you have copies of all your operating & finance leases?
- ▶ Have you decided on a transitional approach?
- ▶ Do you have all the data necessary to implement IFRS 16?
- ▶ Do you have a technology solution?
- ▶ Can you maintain your leases on an ongoing basis?



NEXT STEPS

- ▶ Have you educated yourself and your team re the technical requirements of IFRS 16?
- ▶ Have you done a risk assessment re IFRS 16?
- ▶ Have you designed an appropriate response to the completed risk assessment re IFRS 16?
- ▶ Have you designed a **project plan** re the implementation of IFRS 16?
- ▶ Have you decided on an appropriate **transitional approach** re IFRS 16?
- ▶ Have you changed and improved your systems and processes to deal with the new IFRS 16?



DO YOU NEED ASSISTANCE?

MONTHLY FINANCIAL REPORTING WEBINARS

- ▶ <https://www.bdo.com.au/en-au/insights/audit-assurance/webinars/2018-financial-reporting-accounting-standards>
- ▶ Upcoming IFRS 16 Webinars
 - IFRS 16 - Risk Assessment (24 October 2018)
 - IFRS 16 - Problem Areas (12 December 2018)
- ▶ Previously recorded IFRS 16 Webinars
 - 22 February 2017 - Overview of IFRS 16
 - 20 September 2017
 - 18 October 2017

NEWSLETTERS & OTHER PUBLICATIONS

- ▶ <https://www.bdo.com.au/en-au/accounting-news/accounting-news-august-2018>
- ▶ <https://www.bdo.com.au/en-au/services/audit-assurance/ifrs-advisory-services/ifrs-technical-resources>

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QUESTIONS



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