



**Australian Government**  
**Department of Finance**



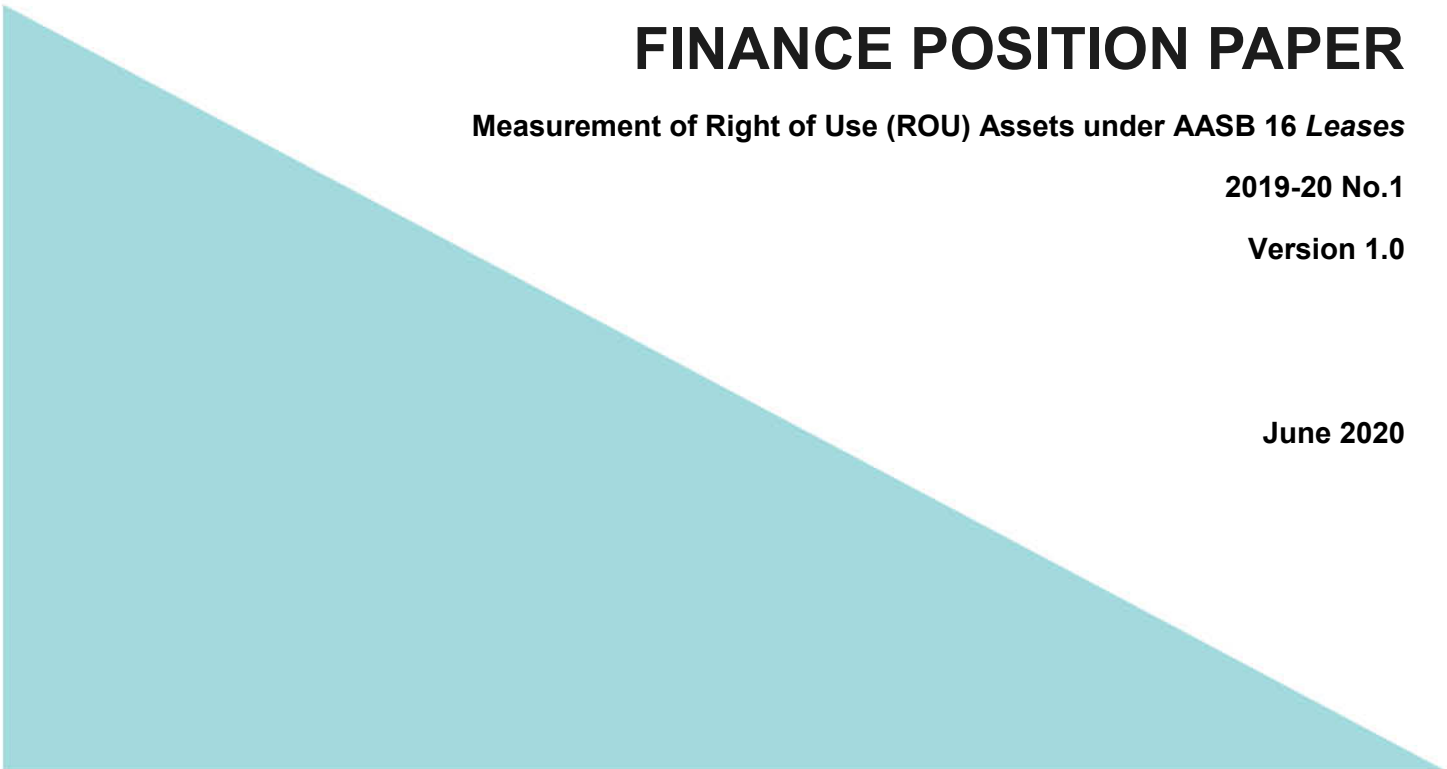
# **FINANCE POSITION PAPER**

**Measurement of Right of Use (ROU) Assets under AASB 16 Leases**

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## Purpose

This paper provides the Department of Finance's (Finance's) position on whether Right of Use (ROU) lease assets are required to be measured at fair value under AASB 16 *Leases* and related Australian Accounting Standards.

## Background

AASB 16 *Leases* applies to the 2019-20 financial year and brings leases that were previously recognised as operating expenses onto balance sheets as ROU assets and lease liabilities. Paragraphs 29 and 35 of AASB 16 require lessees to measure ROU assets at cost, unless the ROU assets related to a class of property, plant and equipment (PPE) measured at fair value under AASB 116 *Property, Plant & Equipment*<sup>1</sup>.

The *Public Governance, Performance and Accountability (Financial Reporting) Rule 2015* (FRR) generally requires Commonwealth entities' non financial assets to be measured at fair value. This accounting policy maintains consistency with Government Finance Statistics (GFS) in the Commonwealth's Whole of Government and General Government Sector (GGS) financial statements, as required by AASB 1049 *Whole of Government and General Government Sector Financial Reporting*<sup>2 3</sup>.

This paper considers whether Commonwealth ROU assets should be measured at fair value under AASB 16. Commonwealth agencies have advised that revaluing ROU assets would be a resource intensive process which will present a range of practical difficulties, including finance system limitations in reconciling movements in ROU asset values to lease payments.

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<sup>1</sup> Paragraph 29 of AASB 116 allows measurement of PPE assets after initial recognition at cost or fair value, by class of PPE asset.

<sup>2</sup> Paragraph 13 of AASB 1049 states: "where compliance with the ABS GFS Manual would not conflict with Australian Accounting Standards, the principles and rules in the ABS GFS Manual shall be applied. In particular, certain Australian Accounting Standards allow optional treatments within their scope. Those optional treatments in Australian Accounting Standards aligned with the principles or rules in the ABS GFS Manual shall be applied".

<sup>3</sup> Paragraph 14(a) of AASB 1049 states: "Examples of particular optional treatments in Australian Accounting Standards that paragraph 13 of this Standard has the effect of limiting, include: (a) assets within the scope of AASB 116 Property, Plant and Equipment, AASB 138 Intangible Assets or AASB 140 Investment Property that may be measured at cost or at fair value. Those assets that are assets under the ABS GFS Manual that are within the scope of those Standards are required to be measured at fair value because the ABS GFS Manual requires those assets to be measured at market value".

# Relevant Accounting Pronouncements

The following accounting standards are relevant:

- AASB 13 *Fair Value Measurement*;
- AASB 16 *Leases*;
- AASB 116 *Property, Plant & Equipment*; and
- AASB 1049 *Whole of Government and General Government Sector Financial Reporting*.

## Finance Positions

### Asset Classes

Paragraph 37 of AASB 116 defines a class of property, plant and equipment (PPE) assets as “A class of property, plant and equipment is a grouping of assets of a similar nature and use in an entity’s operations. The following are examples of separate classes: (a) land; (b) land and buildings; (c) machinery; (d) ships; (e) aircraft; (f) motor vehicles; (g) furniture and fixtures; (h) office equipment; and (i) bearer plants”.

The rights and obligations and risks and benefits of assets under lease contracts may differ substantially from corresponding assets owned outright. Lease ROU assets can therefore be considered to be a distinct ‘grouping of assets of a similar nature’ to corresponding assets owned outright and will be separately disclosed in Commonwealth entity financial statements.

Where ROU assets were previously recognised by Commonwealth lessees under AASB 117 *Leases* as finance lease assets, reclassifying those ROU assets into separate ROU specific asset classes under AASB 16 would be a change in accounting policy under AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. Paragraph 19(a) of AASB 108 states that entities should “account for a change in accounting policy resulting from the initial application of an Australian Accounting Standard in accordance with the specific transitional provisions, if any, in that Australian Accounting Standard;”. The Commonwealth Government has elected to apply paragraph C5(b) of AASB 16, which is to apply AASB 16 *Leases* “retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application”.

The date of initial application of AASB 16 for Commonwealth entities which report on a financial year basis is 1 July 2019. Therefore, the new ROU asset classes would only apply for these entities from the 2019-20 year.

**FINANCE POSITION 1:** Lease ROU assets should be classified by Commonwealth lessees as separate asset classes to corresponding assets owned outright from 2019-20 onwards.

## Ongoing Measurement of ROU Assets under AASB 16

Paragraph 35 of AASB 16 provides entities with the option to measure ROU assets at fair value where the ROU assets relate to a class of PPE assets already measured at fair value under AASB 116. All other ROU assets should be at cost.

Because ROU assets do not relate to a class of PPE to which Commonwealth agencies already apply the revaluation model, ROU assets should not be measured at fair value under paragraph 35 of AASB 16. Therefore, this approach is consistent with GFS practices under AASB 1049.

ROU asset classes may include some existing leases which were previously accounted for as finance lease ROU assets under AASB 117 *Leases*. Prior to 2019-20, these ROU assets were included in PPE asset classes which were required to be measured at fair value under clause 17 of the FRR. Paragraph C11 of AASB 16 requires, where implementation option C5(b) is applied, that ROU assets previously classified as finance leases under AASB 117 be initially recognised on AASB 16 transition date at their carrying amount under AASB 117 immediately prior to transition.

**FINANCE POSITION 2:** Lease ROU assets should be measured at cost after initial recognition in Commonwealth entity, GGS and Whole of Government financial statements. Existing AASB 117 finance lease ROU assets on transition date should be transferred into the new asset classes at their carrying values on 1 July 2019.

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