Strengthening local government

Office of Local Government

Guidance to councils on transitioning to AASB 9, 16, 15 and 1058

There are a number of options available to entities on transition to the new Standards:

- AASB 9 *Financial Instruments*
- AASB 15 *Revenue from Contracts with Customers*
- AASB 16 *Leases*
- AASB 1058 *Income of Not-for-Profit Entities*

In order to achieve consistency and comparability (where possible) the Office of Local Government (OLG) has determined a position on AASB options, which all councils must adopt on transition to the new standards.

The new standards must be adopted on their respective mandatory effective dates, i.e. councils are not permitted to early adopt any of the standards.

This paper provides details of the AASB options and the policies adopted by OLG as the most appropriate for local government, and the rationale for this decision.

Financial reporting options elected on transition to new accounting Standards AASB 9, 16, 15 and 1058 (A600444)

AASB 9 *Financial Instruments*

Paragraph number	**AASB Accounting option**	**OLG position**	**Rationale**
7.2.15	Restatement of prior year information for classification and measurement of financial assets and liabilities	**Do not restate the prior year for classification and measurement – all changes on adoption of AASB 9 due to classification and measurement are taken to retained earnings at 1 July 2018.** **Disclosures required by AASB 7 paragraphs 42L – 42O are required**	Consistency with recommendation for AASB 15 and 16. Impact of AASB 9 not expected to be significant. Less onerous for Councils – limited benefit of retrospective application but potentially significant costs.

Note that the following are not mandated by OLG, as they will depend on the Council’s transactions and balances and relate more to judgements rather than accounting policy choices:

- Designation of any investments as fair value through other comprehensive income
- Determining whether financial assets meet the criteria to be held at amortised cost
- Determining whether there has been a significant increase in credit risk for receivables
- Determining impairment in accordance with the expected loss model.

Financial reporting options elected on transition to new accounting Standards AASB 9, 16, 15 and 1058 (A600444)

AASB 15 ***Revenue from Contracts with Customers***

Paragraph number	AASB Accounting option	OLG position	Rationale
Transition options			
C3	**We note that the same method has to be chosen for AASB 15 and AASB 1058** **Full retrospective adoption** – both current year (30 June 2020) and comparative year (30 June 2019) are prepared under AASB 15. Adjustments on adoption taken to retained earnings at 1 July 2018. Note – under the full retrospective approach, Councils would need to keep two sets of books for 30 June 2019 to allow reporting under the existing standards at 30 June 2019 and reporting under AASB 15 as comparatives in 30 June 2020. **Modified (cumulative catch up) adoption** – current year (30 June 2020) prepared under AASB 15 and prior year (30 June 2019) prepared under existing standards. Adjustments on adoption taken to retained earnings at 1 July 2019. Note – under the modified approach, Councils would be required to report numbers under the existing standards for 30 June 2020 to allow comparability under existing standards and therefore maintain two sets of books for the year-end 30 June 2020.	**Adopt AASB 15 using the modified (cumulative catch up) approach:** • **no restatement of comparatives** • **disclosure at 30 June 2020 of revenue under existing standards to allow comparability.**	Option allowed in AASB 15 to make transition to the standard easier. Councils will incur additional costs to restate with little perceived benefits. Requirement to disclose current year information under the old standard will provide some comparability. Disclosure of impact will be mandated in the Code.

C7	**Practical expedients** Under the modified (cumulative catch up) method, entities may elect to apply AASB 15 only to contracts that are not completed contracts at the date of initial application (1 July 2019). Completed contracts are those: • where all goods / services have been transferred or • where revenue has previously all been recognised under AASB 1004 or in accordance with a AASB 137 provision.	**Prohibit Councils from using this practical expedient, i.e. require them to restate contracts at 1 July 2019 where the Council has transferred all of the goods or services at that date or the revenue has previously all been recognised.**	Incidences where all goods / services have been transferred but the revenue is not fully recognised is expected to be minimal for Councils. In considering the second element of the definition, i.e. where the revenue has been recognised but the goods / services have not been transferred – there would be benefit of this for long-term grants to show the revenue at the same time as the obligations are performed.
C7A	Entity can choose to reflect the aggregate effect of all contract modifications that occur before 1 July 2019 when: i. identifying the satisfied and unsatisfied performance obligations ii. determining the transaction price and iii. allocating the transaction price to the satisfied and unsatisfied This effectively allows Councils to use the benefit of hindsight where changes have previously occurred with the contracts.	**Mandate Councils to use this practical expedient for all contracts, where relevant.**	Given that this practical expedient allows the benefit of hindsight to be used – it will save costs for councils in not having to make adjustments for changes to contracts at numerous dates.
Ongoing options			
4	Entity can choose to apply AASB 15 to a portfolio of contracts (or *performance obligations*) with similar characteristics if the entity reasonably expects that the effects on the financial statements would not differ materially from applying this	**Allow, but not mandate Councils to use this expedient**	A portfolio basis can only be used if it is not materially different from apply the standard to individual contracts and therefore councils can choose whichever approach is more practical for them

	Standard to the individual contracts (or performance obligations) within that portfolio. When accounting for a portfolio, an entity shall use estimates and assumptions that reflect the size and composition of the portfolio.		
Aus 8.1 – Aus 8.3	A not-for-profit public sector licensor may elect not to apply the requirements in AASB 15 relating to licences to: (a)short-term licences; and (b) licences for which the transaction price is of low value. except where the licences have variable consideration. Where this election is made licensor shall recognise the revenue associated with those licences either at the point in time the licence is issued, or on a straight-line basis over the licence term or another systematic basis.	**Mandate that Councils make the election for applicable licences and recognise revenue from these licences on granting of the licence**	Use of this expedient will provide certainty for councils and therefore reduced costs since councils will not have to analyse licence requirements where they meet the short term or low value thresholds.
63	An entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between when the entity transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less.	**Mandate the use of this practical expedient**	Little benefit for councils to calculate significant financing component for less than one year.
94	As a practical expedient, an entity may recognise the incremental costs of obtaining a contract as an expense when incurred if the amortisation period of	**Mandate the use of this practical expedient**	Little benefit for councils to capitalise costs where the contract length is less than 12 months.

	the asset that the entity otherwise would have recognised is one year or less		
121	As a practical expedient, an entity need not disclose the information in paragraph 120 for a performance obligation if either of following conditions is met: a. the performance obligation is part of a contract that has an original expected duration of one year or less; or b. entity recognises revenue from the satisfaction of the performance obligation in accordance with paragraph B16	**Not mandate but allow the option to use this practical expedience – the Code will include the full disclosure with a guidance note**	Councils need to consider whether the disclosure will add value.
B16	As a practical expedient, if an entity has a right to consideration from a customer in an amount that corresponds directly with the value to the customer of the entity's performance completed to date (for example, a service contract in which an entity bills a fixed amount for each hour of service provided), the entity may recognise revenue in the amount to which the entity has a right to invoice	**Not mandate but allow the option to use this practical expedient**	Not considered relevant to councils but allow them to use this if applicable.
B43	If a customer has a material right to acquire future goods or services and those goods or services are similar to the original goods or services in the contract and are provided in accordance with the terms of the original contract, then an entity may, as a practical alternative to estimating the stand-alone selling price of the option, allocate the transaction price to the optional goods or services by reference to the goods or services expected to be provided and the corresponding expected	**Not mandate but allow the option to use this practical expedient**	Not considered relevant to councils but allow them to use this if applicable

	consideration. Typically, those types of options are for contract renewals.		

Note that the following are not mandated by OLG, as they will depend on the Council's transactions and balances and relate more to judgements rather than accounting policy choices:

- Which standard (AASB 15 or AASB 1058) is relevant for Councils revenue streams
- Whether Council is acting as an agent or principal
- How variable consideration should be calculated and the application of the constraint
- Whether multiple contracts with the same customer (or funding provider) should be aggregated
- What are the performance obligations in a contract
- When are performance obligations satisfied – at a point in time or over time
- Method for measuring progress where performance obligation is satisfied over time
- Allocation of the transaction price to performance obligations
- Whether costs meet the criteria for capitalisation.

AASB 1058 ***Income of Not-for-Profit entities***

Paragraph number	AASB Accounting option	OLG position	Rationale
Transition options			
C3	**We note that the same method has to be chosen for AASB 15 and AASB 1058** **Full retrospective adoption** – both current year (30 June 2020) and comparative year (30 June 2019) are prepared under AASB 1058. Adjustments on adoption taken to retained earnings at 1 July 2018. Note – under the full retrospective approach, Councils would need to keep two sets of books for 30 June 2019 to allow reporting under the existing standards at 30 June 2019 and reporting under AASB 1058 as comparatives in 30 June 2020. **Modified (cumulative catch up) adoption** – current year (30 June 2020) prepared under AASB 1058 and prior year (30 June 2019) prepared under existing standards. Adjustments on adoption taken to retained earnings at 1 July 2019. Note – under the modified approach, Councils would be required to report numbers under the existing standards for 30 June 2020 to allow comparability under	**Adopt AASB 1058 using the modified (cumulative catch up) approach:** • **no restatement of comparatives** • **disclosure at 30 June 2020 of revenue under existing standards to allow comparability.**	Option allowed in AASB 1058 to make transition to the standard easier. Councils will incur additional costs to restate with little perceived benefits. Requirement to disclose current year information under the old standard will provide some comparability. Disclosure of impact will be mandated in the Code.

	existing standards and therefore maintain two sets of books for the year-end 30 June 2020.		
C6	An entity may elect to apply AASB 1058 retrospectively only to contracts and transactions that are not completed contracts at the date of initial application.	**Prohibit Councils from using this practical expedient, i.e. require them to restate contracts at 1 July 2019 where the Council has transferred all of the goods or services at that date or the revenue has previously all been recognised.**	Incidences where all goods / services have been transferred but the revenue is not fully recognised is expected to be minimal for Councils. In considering the second element of the definition, i.e. where the revenue has been recognised but the goods / services have not been transferred – there would be benefit of this for long-term grants to show the revenue at the same time as the obligations are performed.
C8	Councils may have acquired an asset at significantly less than fair value but at a value greater than nil or nominal consideration in prior years and recorded the asset at its cost. Option not to restate the value on transition.	Mandate the use of this practical expedient where the asset is recorded in the statement of financial position at its cost.	Cost of obtaining the fair value at the acquisition date is considered onerous with little associated benefit.
Ongoing options			
19	Recognise volunteer services if the fair value can be measured reliably but the services would not have been purchased if they weren’t donated.	Prohibit the recognition of volunteer services unless they meet the mandatory recognition criteria in paragraph 18.	The valuation of volunteer services is a judgemental process and results in recognition of income and expenses with a nil net result in the income statement. If councils want to acknowledge the level of volunteer services, which would not have

			been purchased if they were not donated, then we encourage councils to include this information in the unaudited section of the annual report rather than in the financial statements.

Note that the following are not mandated by OLG, as they will depend on the Council's transactions and balances and relate more to judgements rather than accounting policy choices:

- Which standard (AASB 15 or AASB 1058) is relevant for councils revenue streams.
- Which classes of volunteer services have fair value, which can be measured reliably.
- Whether volunteer services would have been purchased if they had not been donated.

AASB 16 *Leases*

Paragraph number	AASB Accounting option	OLG position	Rationale
Transition options			
C3	An entity (lessor or lessee) is not required to reassess whether a contract is, or contains a lease at the date of initial application. The entity is permitted to: - Apply AASB 16 to contracts previously identified as leases under AASB 117 / Interpretation 4 - Not to apply AASB 16 to contracts that were not previously identified as containing a lease applying AASB 117 / Interpretation 4.	**Mandate the use of this practical expedient – where agreements were previously assessed at inception as not containing leases under AASB 117 and associated interpretations. Supporting documentation for the previous assessment will need to be provided.** **However, we encourage councils to identify agreements (including service agreements) which could meet the definition of a lease under AASB 16 since on renewal date of those contracts; they will need to be accounted for under AASB 16.**	The cost of applying AASB 16 is significant and given the number of leases in place at councils, the preference would be to focus on putting time and effort into ensuring that existing leases are accounted for correctly under AASB 16. Once the service / management agreements are renewed, councils will have to assess whether they meet the definition of a lease and apply the appropriate accounting from that date.
C5	A lessee shall apply AASB 16 to its leases either: **Full retrospective adoption** – both current year (30 June 2020) and comparative year (30 June 2019) are prepared under AASB 16. Adjustments on adoption taken to retained earnings at 1 July 2018. Note – under the full retrospective approach, Councils would need to keep two sets of books for 30 June 2019 to allow reporting under the existing standards at 30 June 2019 and reporting under AASB 16 as comparatives in 30 June 2020.	**Mandate modified (cumulative catch up) method of adoption for councils**	Consistent with proposed revenue treatment and allows councils to take advantage of a number of practical expedients in AASB 16 which are only available where modified (cumulative catch up method) is used.

	Modified (cumulative catch up) adoption – current year (30 June 2020) prepared under AASB 16 and prior year (30 June 2019) prepared under existing standards. Adjustments on adoption taken to retained earnings at 1 July 2019.		
C8b	Right of use for each lease is measured at either: - its carrying amount as if AASB 16 had been applied since the commencement of the lease but discounted at the lessee's incremental borrowing rate at the date of initial application or - an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.	**Mandate the second option for determining right of use asset on initial recognition, i.e. recognise right-of-use at amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.**	Whilst the right to use asset will be overstated using this approach – the cost of calculating the balance on commencement of lease for each lease in place in 1 July 2019 will be significant with limited benefit.
C10a	A lessee may apply a single discount rate to a portfolio of leases with reasonably similar characteristics (such as leases with a similar remaining lease term for a similar class of underlying asset in a similar economic environment	**Allow councils to use this expedient but not mandate it.**	Not mandated as councils will be using different discount rates and therefore it is not a consistent issue.
C10b	A lessee may rely on its assessment of whether leases are onerous applying AASB 137 immediately before the date of initial application as an alternative to performing an impairment review. If a lessee chooses this practical expedient, the lessee shall adjust the right-of-use asset at the	**Mandate the use of this exemption**	Councils are not expected to have onerous leases, however for consistency and ease this is mandated as the AASB 137 provision would be a reasonable proxy for the impairment of the right-of-use asset.

	date of initial application by the amount of any provision for onerous leases recognised in the statement of financial position immediately before the date of initial application		
C10c	A lessee may elect not to apply the requirements in AASB 16 to leases for which the lease term ends within 12 months of the date of initial application. In this case, a lessee shall: i. account for those leases in the same way as short-term leases; and ii. include the cost associated with those leases within the disclosure of short-term lease expense in the annual reporting period that includes the date of initial application.	**Mandate the use of this exemption**	When leases expire within 12 months from 1 July 2019, the cost to restate them would be significant compared to the benefit to the users of the financial statements. Preference would be to focus on the leases which extend beyond 30 June 2020 rather than those which will have expired by 30 June 2020.
C10d	A lessee may exclude initial direct costs from the measurement of the right-of-use asset at the date of initial application.	**Do not allow the use of this practical exemption.**	Given that the expedient in C8b is recommended to be mandated, this expedient is not relevant and therefore if its use is prohibited then it will avoid confusion.
C10e	A lessee may use hindsight, such as in determining the lease term if the contract contains options to extend or terminate the lease.	**Mandate the use of this practical expedient.**	This expedient will allow councils to apply known factors to the lease accounting rather than trying to determine what the answer would have been at the time of the lease commencement and will provide information that is more meaningful to the users.
C11	For leases which were previously classified as finance leases , the carrying amount of the right of use asset and the lease liability at the date of initial adoption is the carrying amount of the lease asset	**Whilst not strictly a choice, included for completeness.**	Existing balances for finance lease at 30 June 2019 will be opening balances for AASB 16 at 1 July 2019. These balances will

	and lease liability immediately prior to the date of adoption under AASB 117.		then be subject to AASB 16 on an ongoing basis.
Aus 25.1	Where the lessee is a not-for-profit entity, , 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 AASB13 Fair Value Measurement for leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives.	**Recommend but not mandate that Councils do not measure right of use assets at fair value for leases in place at transition date (being 1 July 2019).**	Measuring the fair value of the right of use assets on 1 July 2019 for existing peppercorn (and other leases below market value) is challenging due to the lack of guidance on this subject. OLG recommend council choose to hold these assets at cost until such time that the AASB release guidance and lift the temporary deferral. Any Council who has previously recognised right of use asset at fair value is able to continue to recognise the asset on this basis.
Ongoing options			
4	A lessee may, but is not required to, apply this Standard to leases of intangible assets other than those described in paragraph 3(e)	**Mandate that councils do not apply AASB 16 to leases of intangible assets**	Councils will not have to spend time determining whether agreements in place over the use of an intangible asset meets the definition of a lease.
5	A lessee may elect not to apply the requirements of AASB 16 to short-term leases	**Mandate that councils make this election for all leases, which qualify as short-term.**	The cost of applying AASB 16 is significant and given the short nature of these leases (less than 12 months) – the cost of the accounting is considered to exceed the benefits.
5	A lessee may elect not to apply the requirements of AASB 16 to leases for which the underlying asset is of low value	**Mandate that councils make this election for all leases where the underlying asset is of low value.**	The cost of applying AASB 16 is significant and given the number of leases in place at councils, the preference would be to focus

		OLG will provide guidance on the threshold for low value assets to be in the region of $7,000 - $10,000 but no higher than $10,000.	on putting time and effort into getting the non-low value asset leases correct and take advantage of the exemption in the standard for the low-value assets. Note that low-value threshold will be consistent across all councils, as it is not related to materiality.
15	A lessee may elect, by class of underlying asset, not to separate non-lease components from lease components and instead account for each lease component and any associated non-lease component as a single lease component. [E.g. cleaning / security services on a building lease]	**Permit councils to use this practical expedient but not mandate its use.** **We note that where expenses are based on sales or usage, such as utilities charges on a building, then this would be accounted for on an as incurred basis and therefore not be included as part of the lease liability.**	Whilst this practical expedient may result in an overstated right to use and lease liability, given that it is an option permitted in the standard – the cost of separating the lease and non-lease components is considered to exceed the benefit to the users. However, Councils are permitted to choose to separate the lease and non-lease components where the non-lease component is significant – this choice is made on a class of underlying asset basis.
29	Subsequent to initial recognition, a lessee shall measure the right-of-use asset applying cost or fair value under AASB 116 or AASB 140.	**Mandate that the right-of-use asset is exempt from the fair value requirement and allow councils to carry this asset at cost.**	The right-of-use asset is in substance an intangible asset and the revaluation exercise would be costly and comprise of significant estimation. Whilst the tangible assets of councils are required to be held at fair value, there is no reason to apply the same requirement to right-of-use assets. The right of use would be presented as a separate class of asset and therefore it would not affect any other assets.

47	Lessee shall present in the statement of financial position or in the notes - Right of use assets separately from other assets - Lease liabilities separately from other liabilities.	**Present right-of-use assets and lease liabilities as a separate line item on the face of the statement of financial position.**	These line items are likely to be material and therefore the information is more meaningful to the users if they are presented separately rather than being lost in the notes to the financial statements.
50	Lessee should classify cash payments for the interest portion of the lease liability applying the requirements of AASB 107, i.e. as operating, financing or investing.	**Continue to mandate interest paid to be shown as operating cash flows.** **Note the IASB has a project to mandate the presentation of interest and if a standard is issued then this may affect the presentation prior to adoption of AASB 16.**	Consistency with existing AASB 107 OLG mandate.

Note that the following are not mandated by OLG, as they will depend on the Council's transactions and balances and relate more to judgements rather than accounting policy choices:

- Identifying whether a contract meets the definition of a lease.
- Where it is reasonably certain that an option included in a lease will be exercised.
- Whether a lease modification is a separate lease or a modification to the existing lease
- Whether a lessor classifies a lease as operating or finance.
- Whether a lessor recognises rental income on a straight-line basis or other systematic basis – although likely to recommend straight-line unless evidence of another basis provides information that is more useful to the users.