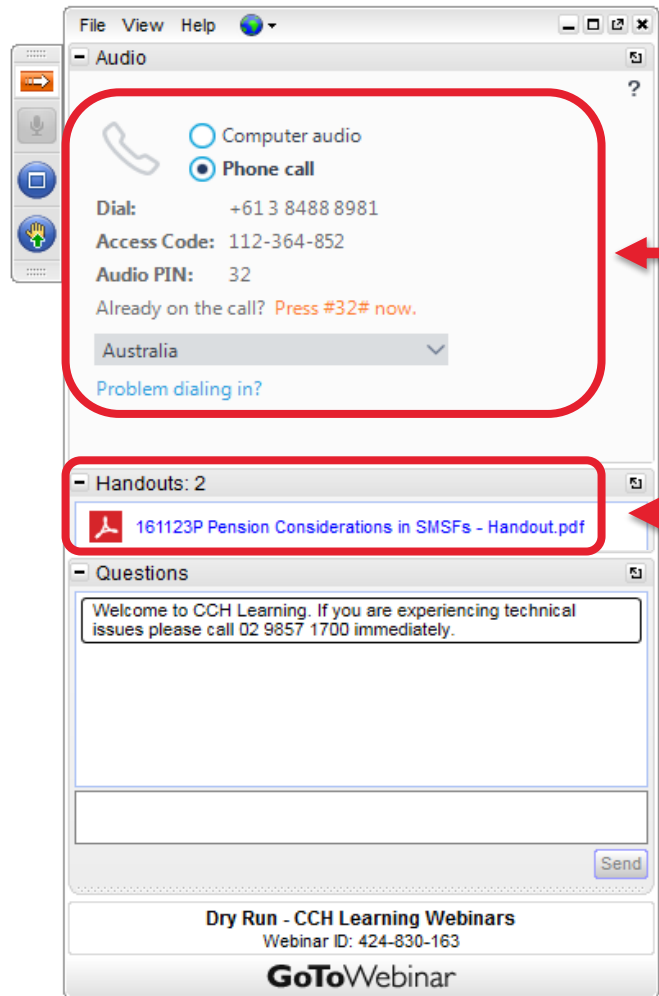

Latest Developments around Lease Accounting (IFRS 16)

Aletta Boshoff

Thursday 14 March 2024



How to Participate Today



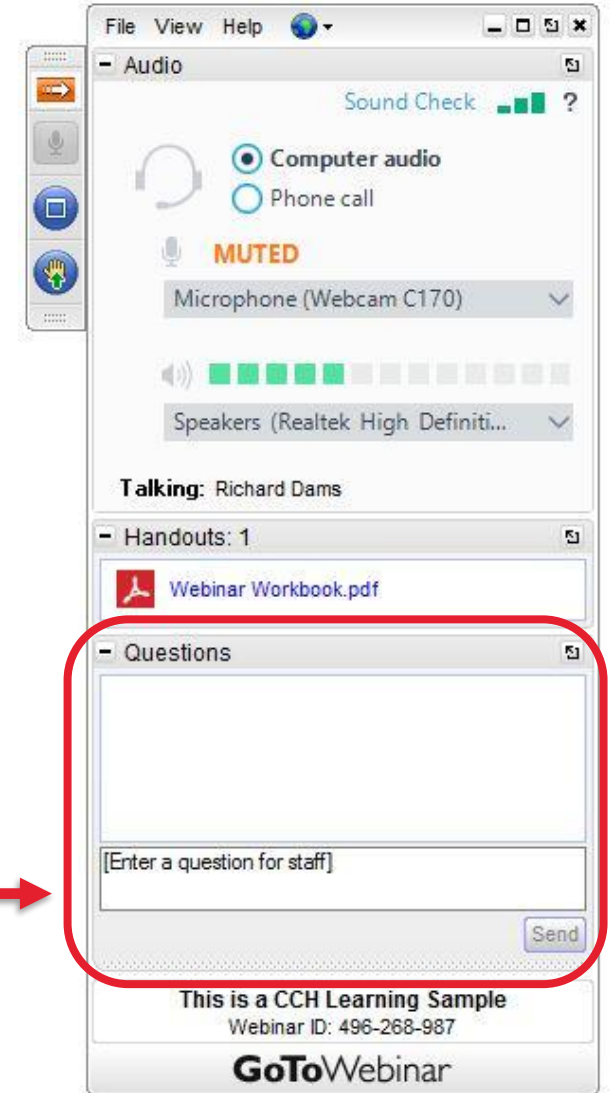
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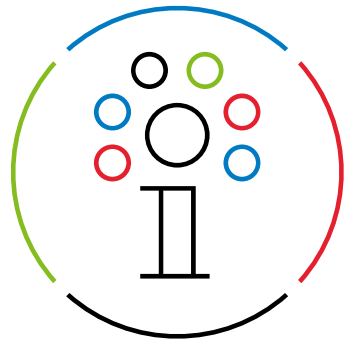
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Your Presenter



- **Aletta Boshoff**
- Partner, BDO
- National Leader IFRS & Corporate Reporting
- National Leader ESG & Sustainability

Today's session will cover



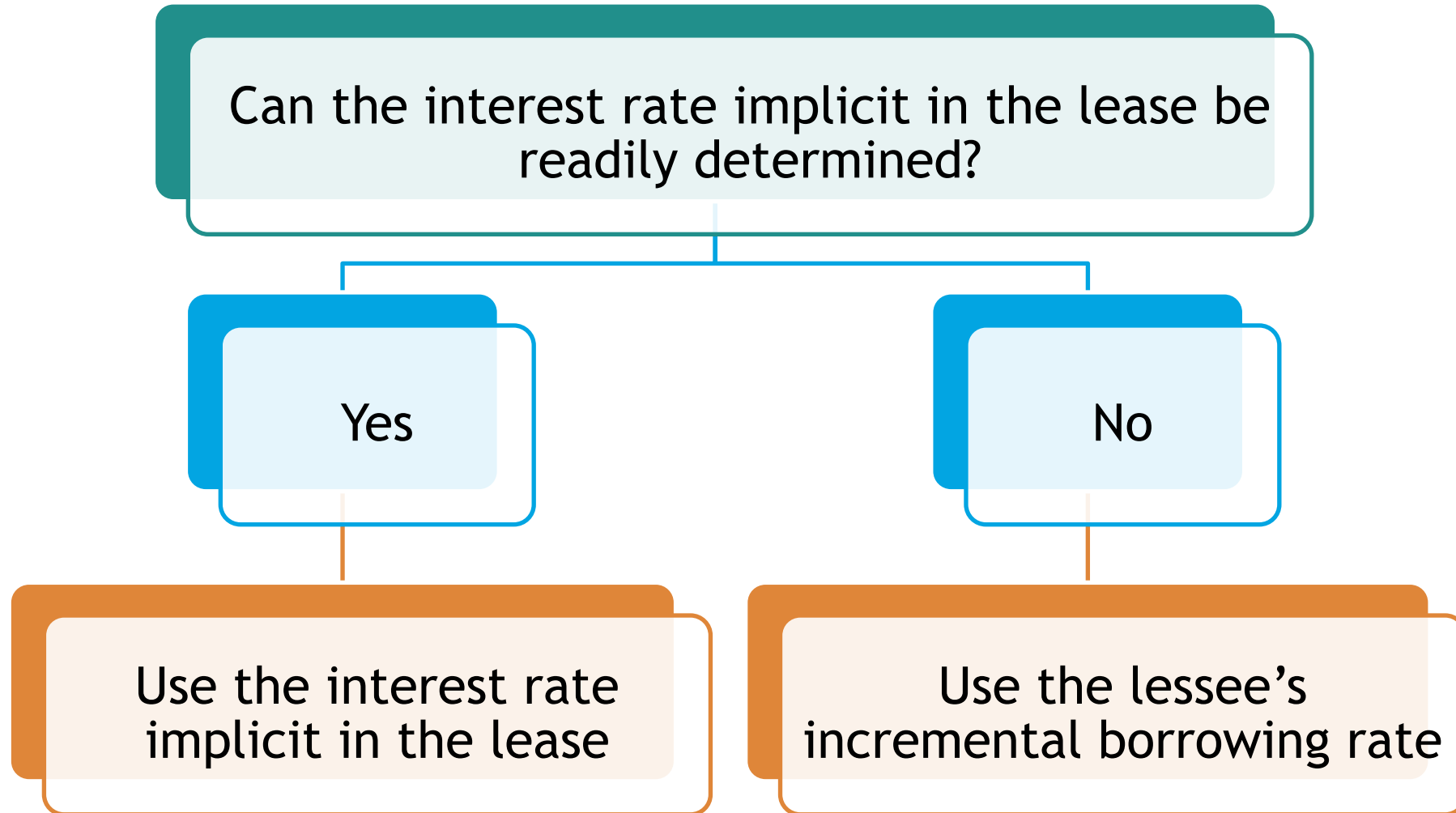
Top 10 lease accounting challenges in 2024

1. Incremental borrowing rate
2. Hold over leases
3. Renegotiation of holdover leases
4. Managing on-going changes to lease portfolio
5. CPI adjustments
6. New leases which are actually modifications
7. Expired leases
8. Early terminated leases
9. Make good provisions
10. Sub leases



**#1 - INCREMENTAL
BORROWING RATE**

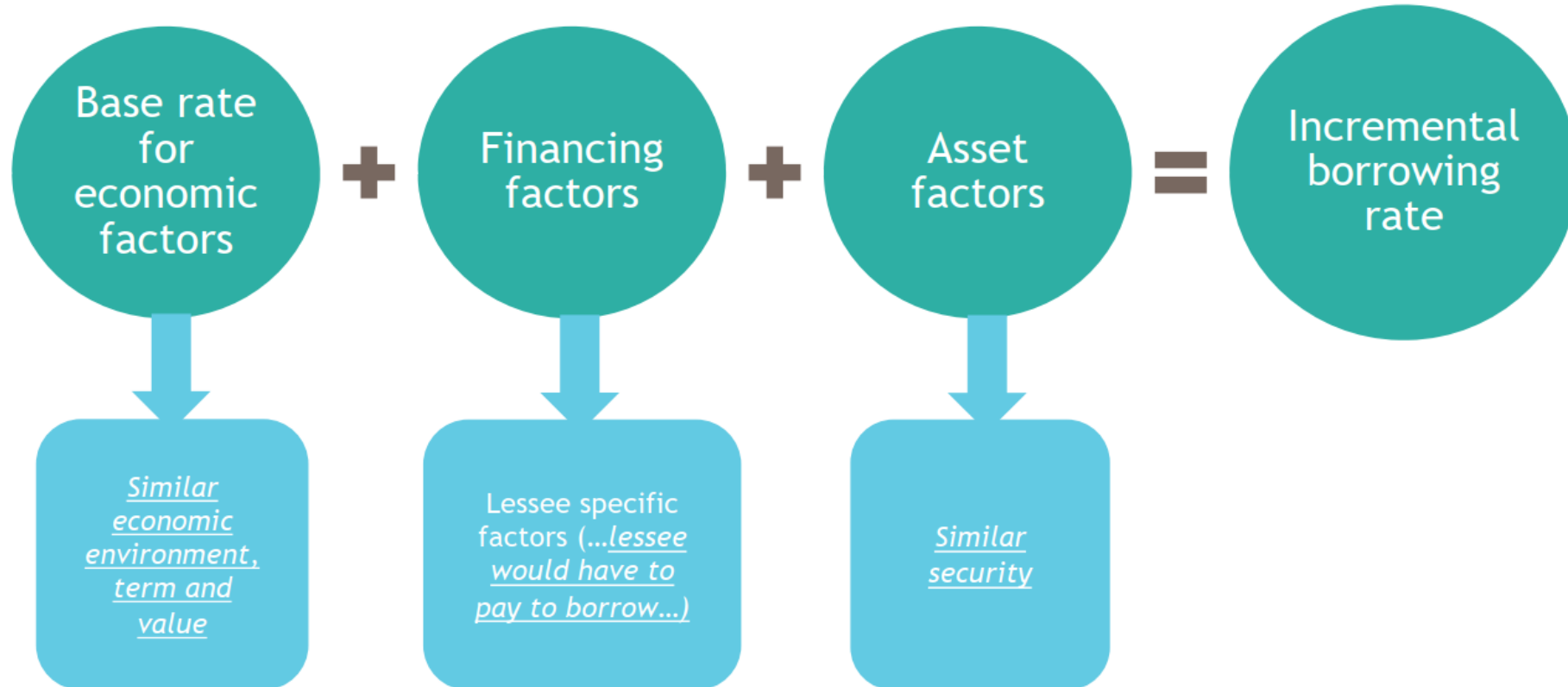
APPROPRIATE DISCOUNT RATE



LESSEE'S INCREMENTAL BORROWING RATE

- ▶ The rate of interest that a lessee would **have to pay** to borrow
 - Over a similar term, and
 - With a similar security
- ▶ The funds necessary to **obtain an asset**
 - Of a similar value to the right-of-use asset
 - In a similar economic environment

LESSEE'S INCREMENTAL BORROWING RATE





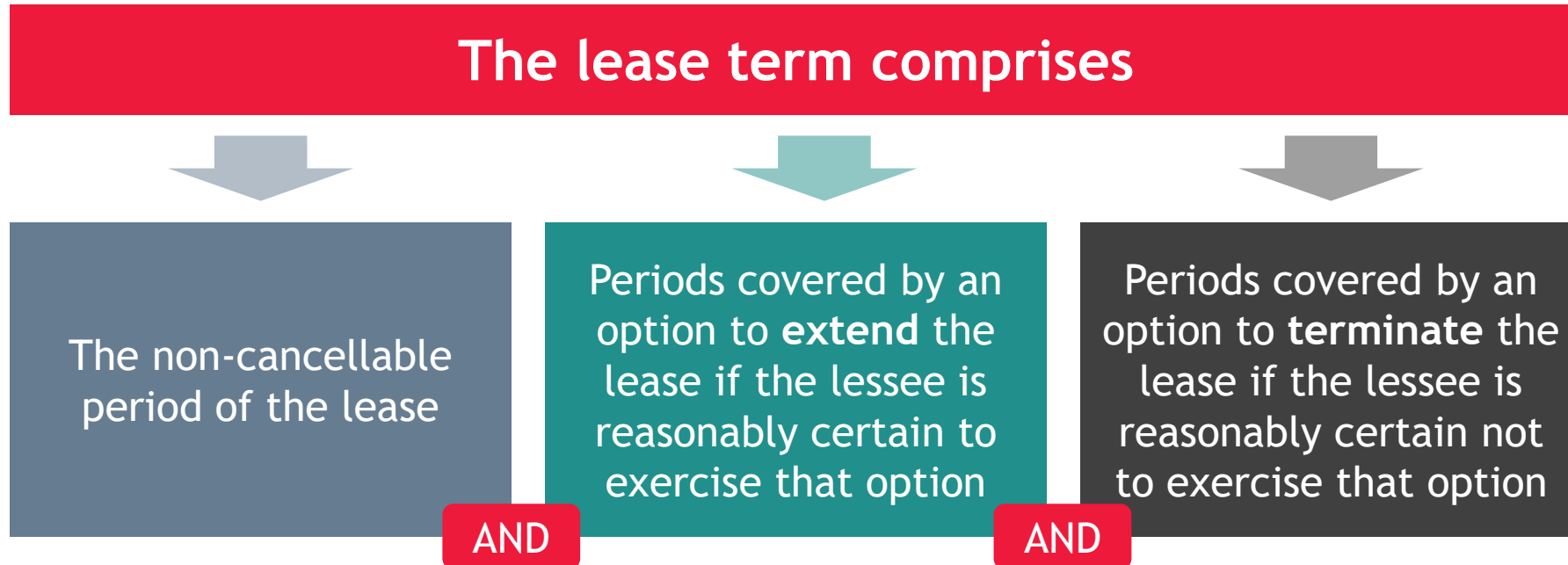
LESSEE'S INCREMENTAL BORROWING RATE

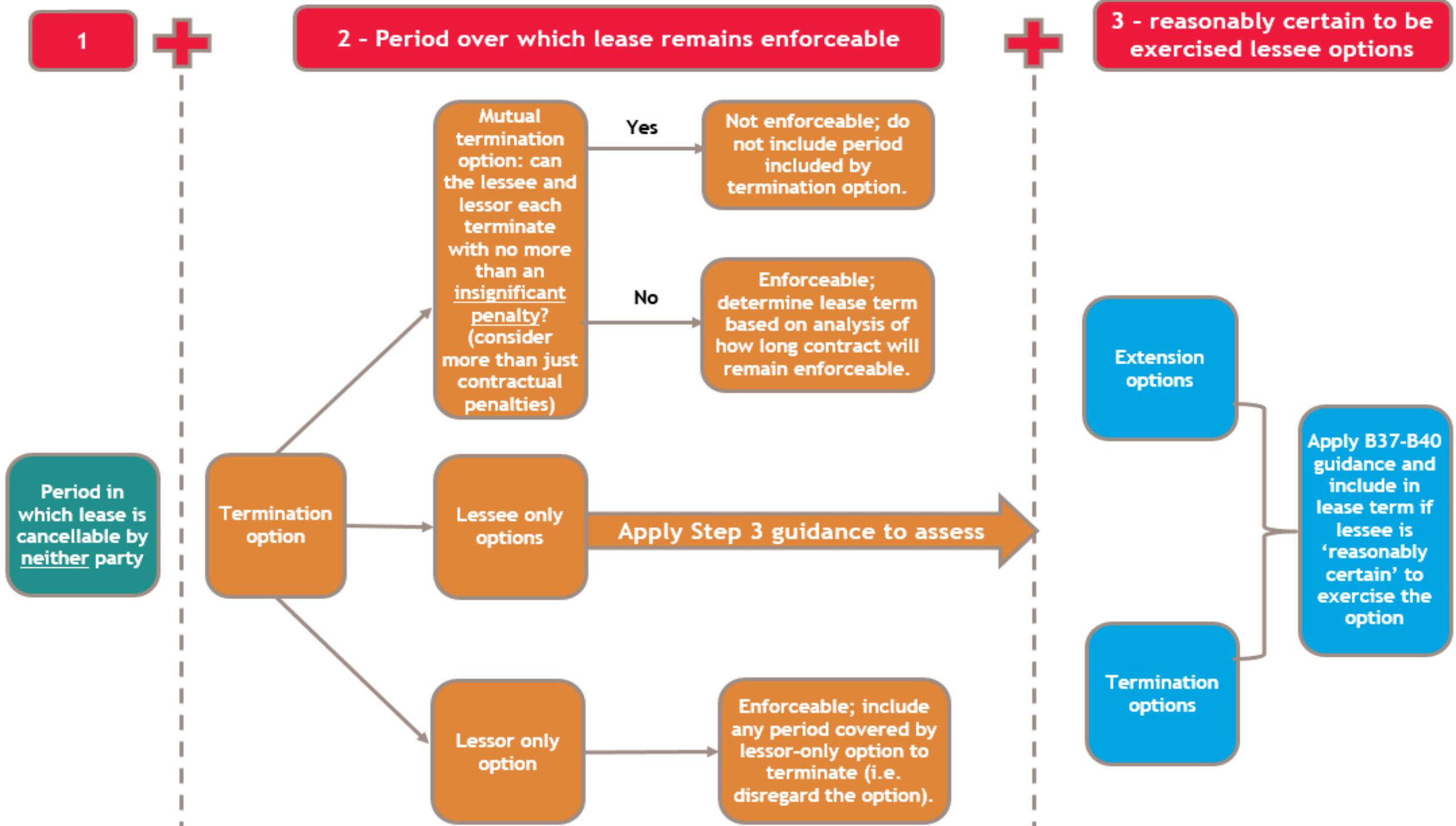
- ▶ When do entities need to update the IBR?
- ▶ Impact of the current interest rate environment on IBR

A photograph of two women walking through a modern office hallway. The woman on the left has curly hair, is wearing a white button-down shirt and a dark skirt, and is holding a black folder. The woman on the right has straight hair with bangs, is wearing a white sleeveless top and dark trousers, and is holding a smartphone. They are both looking at each other and appear to be in conversation. The hallway has a carpeted floor, glass railings, and office desks in the background.

#2 - HOLD OVER LEASES

DETERMINING THE LEASE TERM





DETERMINING THE LEASE TERM

In circumstances in which only the lessee has a termination option, to estimate the lease term a lessee must assess the likelihood of it either exercising or failing to exercise that option. Factors that would be considered in this assessment include, but are not limited to:

- (a) Contractual terms and conditions for the optional periods compared with market rates, such as:
 - i. The amount of payments for the lease in any optional period;
 - ii. The amount of any variable payments for the lease or other contingent payments;
 - iii. The terms and conditions of any options that are exercisable after periods covered by another option (or other options), e.g. a purchase option that is exercisable at the end of one or more extension periods at a rate that is currently below market rates;
- (b) Significant leasehold improvements or other improvements made to underlying assets that are expected to have a significant residual benefit to the lessee when options become exercisable;
- (c) Costs relating to the termination of the lease (e.g. negotiation, relocation, and search costs, installation and setup costs for new assets, termination penalties or costs to return an underlying asset at the end of the lease term);
- (d) The importance of an underlying asset to the lessee's operations (e.g. whether the underlying asset is highly specialised, the location of the asset and the availability of suitable alternatives); and
- (e) Conditionality associated with the exercise option (i.e. if an option can be exercised only if one or more conditions are met) and the likelihood that those conditions will be met.

A photograph of two women in a modern office setting. The woman on the left is wearing a dark blazer over a white top and is pointing at a tablet held by the woman on the right. The woman on the right is wearing a black top and is looking at the tablet. The background is a blurred office with desks and other people. There are red vertical bars on the left and right sides of the image.

#3 - RENEGOTIATION OF HOLD OVER LEASES

IDEAS | PEOPLE | TRUST



RENEGOTIATION OF HOLD OVER LEASES

What if...?

- ▶ A 10 year lease of a building expires in May 2023
- ▶ From 1 June 2023 the lease is in holdover and the entity is busy negotiating a new lease
 - Expected new lease term 3 years
 - Expected lease payments of \$8,000 per month
- ▶ On 1 August 2023, the entity enters into a brand new lease agreement for 5 years at \$10,000 per month

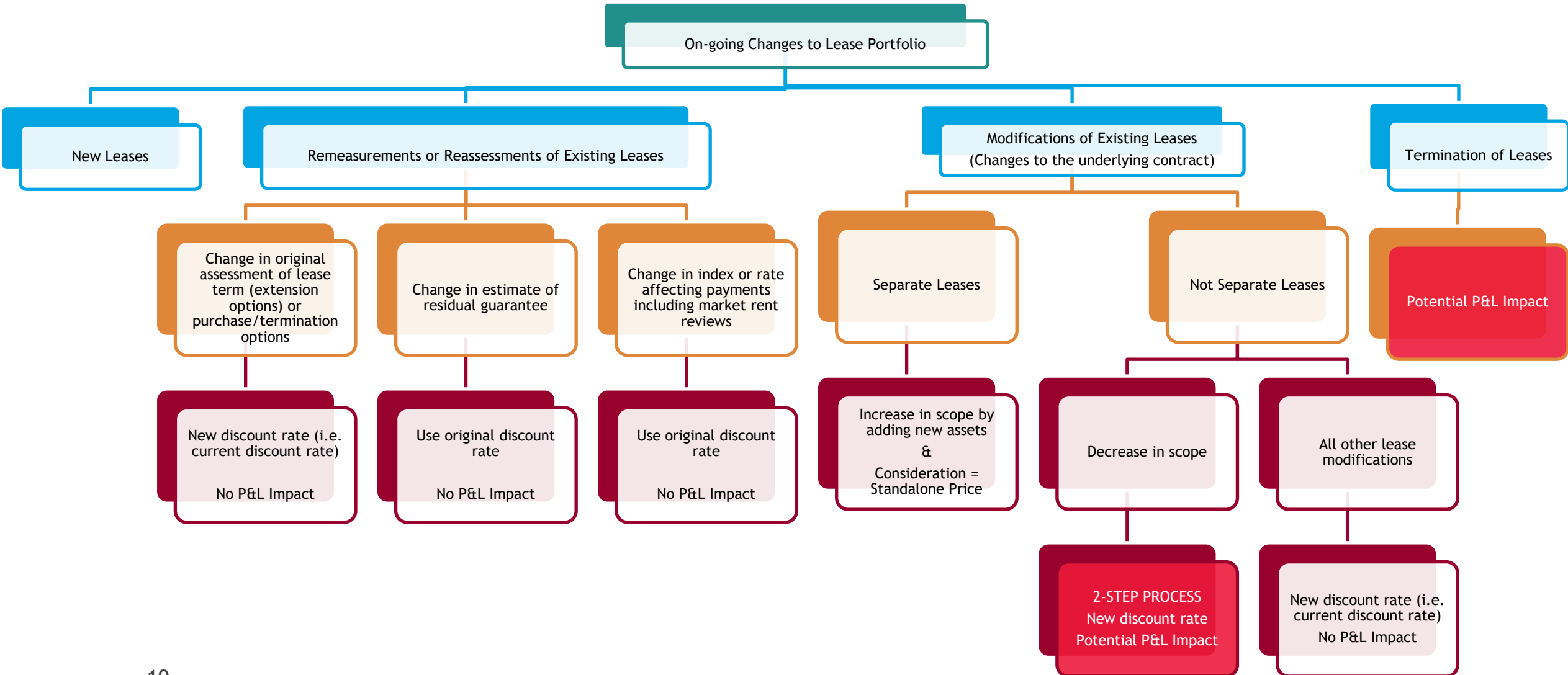


#4 - MANAGING ON-GOING CHANGES TO LEASE PORTFOLIO

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MANAGING ON-GOING CHANGES TO LEASE PORTFOLIO





#5 - CPI ADJUSTMENTS

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CPI ADJUSTMENTS

Variable payments that depend on an index or a rate

- Include in the initial measurement of the lease using the index or rate as at the commencement date
- Remeasure lease in the period the rate or index changes



#6 - NEW LEASES WHICH ARE ACTUALLY MODIFICATIONS

NEW LEASES WHICH ARE ACTUALLY MODIFICATIONS

- ▶ New legal lease agreements
- ▶ BUT
- ▶ Continuing to use the same asset
- ▶ EQUALS
- ▶ A lease modification

- ▶ NOT a new lease for lease accounting purposes!

A photograph of two men sitting at a table in a meeting. The man on the left is wearing glasses and a plaid shirt, looking towards the man on the right. The man on the right is wearing a white sweater and is gesturing with his hands while speaking. A laptop and a glass of water are on the table. The background shows a window with a view of a building.

#7 - EXPIRED LEASES



EXPIRED LEASES

- ▶ End of lease term
- ▶ The entity no longer uses the asset (i.e. the asset is returned to the lessor)
- ▶ No RoU asset and no lease liability - should we just do nothing...?
- ▶ Remove the original cost of the RoU asset and remove the accumulated depreciation of the RoU asset

A photograph of two men in a modern office setting. The man on the left is wearing a dark suit jacket over a grey t-shirt and glasses, holding a tablet. The man on the right is wearing a light blue button-down shirt and brown trousers. They are standing in a glass-walled office space with a desk and chair visible in the background. A red vertical bar is on the left side of the image.

#8 - EARLY TERMINATED LEASES

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EARLY TERMINATED LEASES

- ▶ Expect a P&L impact
- ▶ Remove RoU asset and lease liability with balance being an P&L impact



#9 - MAKE GOOD PROVISIONS

MAKE GOOD PROVISIONS

- ▶ Debit entry
 - Included in RoU asset ito IFRS
 - Subject to depreciation

- ▶ Credit entry
 - Not part of the lease liability
 - Separate make good provision ito IAS 37
 - Unwinding of discount per IAS 37

A man with glasses and a black shirt is holding a tablet, looking at it intently. A woman with dark hair in a ponytail, wearing a white polka-dot shirt, is sitting next to him, looking at the tablet and holding a pen to her chin in a thoughtful pose. They are in a modern office setting with blurred desks and lights in the background. A red vertical bar is on the left side of the image.

#10 - SUB LEASES

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SUBLEASES

- ▶ Assess whether the sublease is a finance lease or an operating lease
- ▶ Compare lease terms of head lease and sublease

SUBLEASES - FINANCE LEASES

- ▶ Derecognise the RoU asset, i.e. the cost and the accumulated depreciation of the RoU asset
- ▶ Recognise a lease receivable
 - Recognise interest income in future
- ▶ Keep the lease liability



SUBLEASES - OPERATING LEASES

- ▶ Keep the RoU asset
- ▶ Keep the lease liability



**DO YOU HAVE AN EFFICIENT AND
EFFECTIVE LEASE SOLUTION?**

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LEASE ACCOUNTING ... YOUR TIME IS VALUABLE

BDO Lead SaaS

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



BDO Lease Management Services (Outsourcing your lease accounting to us)

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



BDO LEASE MANAGEMENT SERVICES (OUTSOURCING)

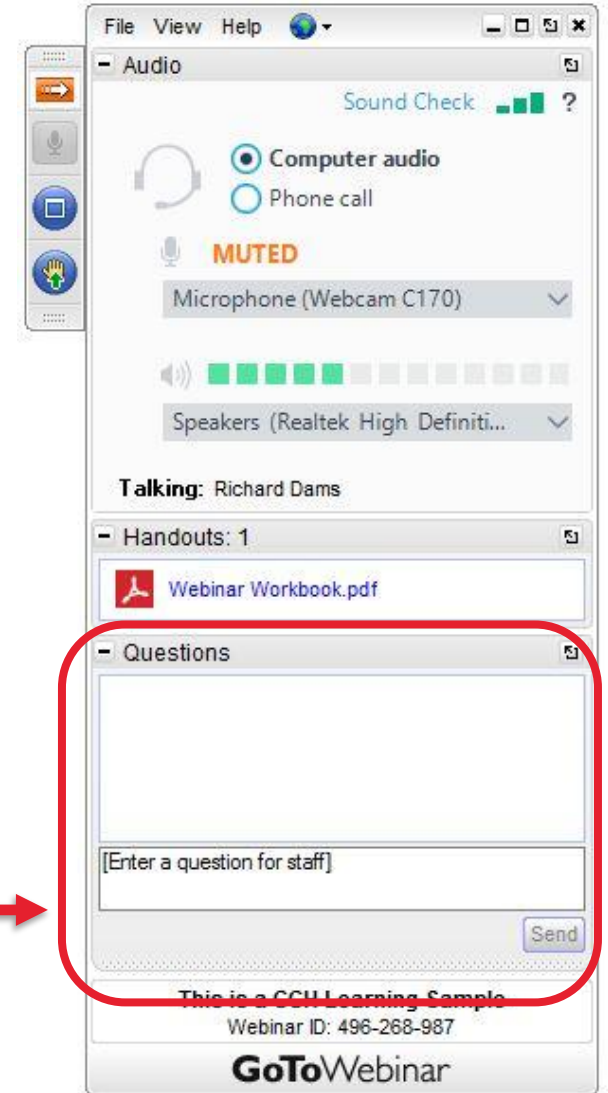


Questions?

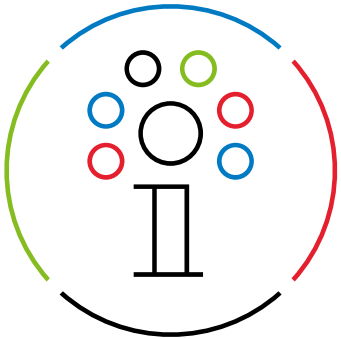


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- 26 March – Initial Meeting to Profitable Client
- 27 March – Practical Issues with the Main Residence Exemption

Questions?



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- National Leader ESG & Sustainability
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- Aletta.Boshoff@bdo.com.au

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