

Technical Advisory Group Issue Paper

AGENDA ITEM: TAGED14-09
28-29 September 2023 – Hybrid

Exposure Draft 3 - Section 16 (Investment property), Section 17 (Property, plant and equipment), Section 18 (Intangibles other than goodwill and Section 20 (Leases)

Summary	This paper provides TAG members with the draft authoritative guidance for Section 16 <i>Investment property</i> , Section 17 <i>Property, plant and equipment</i> , Section 18 <i>Intangibles other than goodwill</i> and Section 20 <i>Leases</i> .
Purpose/Objective of the paper	To allow TAG members to consider the consequential impact of changes to these Sections, which have been updated to align with changes to other sections. The paper sets out the approach to alignment issues and draws out significant issues for consideration.
Other supporting items	None
Prepared by	Karen Sanderson/Alistair Jenkins
Actions for this meeting	<u>Comment and advise</u> on: (i) approach to the updates taken across all three sections (ii) the approach to application guidance taken for these sections (iii) the draft authoritative guidance

Technical Advisory Group

1. Exposure Draft 3 - Section 16 (Investment property), Section 17 (Property, plant and equipment), Section 18 (Intangibles other than goodwill and Section 20 (Leases)

2. Background

- 2.1 In line with responses to the Consultation Paper it was agreed to prioritise a limited number of topics for inclusion in the first edition of INPAG. Following discussions with the TAG it was agreed that other topics in the *IFRS for SMEs* Accounting Standard would be updated to align with the terminology being used in the remainder of INPAG.
- 2.2 As INPAG is being developed there are other consequential amendments that may need to be made that go beyond changes to terminology previously discussed. A limited number of changes are therefore proposed to ensure that INPAG is cohesive. These consequential amendments do not constitute a full review of the text in these topic areas.

3. Investment property

- 3.1 Section 16 has been updated to reflect NPO related terminology, to align with other content and for consequential amendments.
- 3.2 The text in Section 16 is aimed at investment proposed that has been acquired requiring it to be measured at cost at initial recognition. It is, however, possible that an NPO is donated property that would be considered investment property in that it would not be used directly for its missional purposes. For example, a domestic residence could be bequeathed to an NPO. As a consequence it is proposed to distinguish between purchased and donated investment property, with a new paragraph added at G16.7. This requires a donated investment property to be measured at fair value in line with Section 12 *Fair value measurement* on initial recognition. Secretariat consider this to be a consequential amendment from Section 23 Part I *Revenue from grants and donations*.

Question 1: Do TAG members agree that the new text on donated investment property should be included and with the proposals made?

Question 2: Do TAG members have any other comments on this Section, including the use of terminology?

4. Property, plant and equipment

- 4.1 As with Section 16, Section 17 has been updated to reflect NPO related terminology, alignment with other content and consequential amendments. Of note it includes service potential alongside economic benefit when considering whether an item of property, plant and equipment is an asset.
- 4.2 As with Section 16, it is proposed that an additional paragraph is added for property, plant and equipment that has been donated. As with investment property it is proposed that these donations are measured at initial recognition at fair value in line with Section 12. It is proposed that this measurement value is then used as the deemed costs of the donated asset. This is also considered a consequential amendment from Section 23 Part I.
- 4.3 Pending a full review of Section 17, which will be prioritised for review in Phase 2, no additional application guidance is proposed for Section 17 as Secretariat is of the view that the additional guidance in Section 12 is sufficient to address the needs of those NPOs that have donated property, plant and equipment.

Question 3: Do TAG members agree with the new text on donated property, plant and equipment? Do TAG members agree that this becomes the deemed cost?

Question 4: Do TAG member agree that application guidance for Section 17 is not provided, with reliance placed on the guidance in Section 12?

Question 5: Do TAG members have any other comments on this Section, including the use of terminology?

5. Intangibles not including goodwill

- 5.1 As with the other sections, Section 18 has been updated to reflect NPO related terminology, alignment with other content and consequential amendments. This section also includes service potential alongside economic benefit when considering whether an item is an intangible asset.
- 5.2 Unlike Sections 16 and 17, it is not currently proposed to include a new section on donated intangible assets. It should be noted that paragraph G18.14 provides for intangible assets acquired by way of government grants to be measured at fair value at the date the grant is received or receivable. While a government grant does not cover all grants and is not the same as a donation, it does establish the principle of fair valuing intangible assets received by way of grant. This could be sufficient. If a paragraph were to be introduced it would follow the same approach as outlined for Sections 16 and 17.

Question 6: What are TAG members' views on the need for a new paragraph for donated intangible assets and the relationship with the existing paragraph on government grants?

Question 7: Do TAG members have any other comments on this Section, including the use of terminology?

6. Leases

- 6.1 Section 20 has been updated to reflect NPO related terminology, alignment with other content and consequential amendments. It should be noted that Section 20 characterises amounts earned under a lease arrangement as income. It is not proposed to change this term as this is consistent with the definitions in Section 2 *Concepts and pervasive principles*.
- 6.2 No changes are proposed for this Section as there do not appear to be any NPO-specific issues arising from the accounting requirements outlined. The *IFRS for SMEs* Accounting Standard includes an illustrative example, which it is proposed to include in INPAG.

Question 8: Do TAG members have any other comments on this Section, including the use of terminology?

7. Next steps

- 7.1 The authoritative guidance will be amended to reflect TAG member feedback. A Basis for Conclusions will only be developed that reflects the considerations of the TAG and other input.

Annex A Investment property

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Section 16 – *Investment property*

Scope of this section

G16.1 This section applies to accounting for investments in land or buildings that meet the definition of **investment property** in paragraph G16.2 and some property interests held by a lessee under an **operating lease** (see paragraph G16.3) that are treated like investment property. Only investment property whose **fair value** can be measured reliably without undue cost or effort on an ongoing basis is accounted for in accordance with this section at fair value through **surplus or deficit**. All other investment property is accounted for using the cost model in Section 17 *Property, plant and equipment* and remains within the scope of Section 17 unless a reliable measure of fair value becomes available and it is expected that fair value will be reliably measurable on an ongoing basis.

Definition and initial recognition of investment property

- G16.2 Investment property is property (land or a building, or part of a building, or both) held by the owner or by the lessee under a **finance lease** to earn rentals or for capital appreciation or both, instead of for:
- a) use in the **ordinary activities of the NPO**, or for **NPO's** administrative purposes; or
 - b) sale **where this is in** the ordinary course of **NPO activity**.
- G16.3 A property interest that is held by a lessee under an operating lease may be classified and accounted for as investment property using this section if, and only if, the property would otherwise meet the definition of an investment property and the lessee can measure the fair value of the property interest without undue cost or effort on an ongoing basis. This classification alternative is available on a property-by-property basis.
- G16.4 An **NPO** shall use its judgement to determine whether the acquisition of investment property is the acquisition of an asset or of a group of assets, or a business combination within the scope of Section 19 *Business combinations and goodwill*. Determining whether a specific transaction meets the definition of a business combination as defined in Section 19 and includes an investment property as defined in this section requires the separate application of both sections.
- G16.5 Mixed use property shall be separated between investment property and **property, plant and equipment**. However, if the fair value of the investment property component cannot be measured reliably without undue cost or effort, the entire property shall be accounted for as property, plant and equipment in accordance with Section 17.

Measurement at initial recognition

- G16.6 An NPO shall measure **purchased** investment property at its cost at initial **recognition**. The cost of a purchased investment property comprises its purchase price and any directly attributable expenditure such as legal and brokerage fees, property transfer taxes and other **transaction costs**. If payment is deferred beyond normal credit terms, the cost is the **present value** of all future payments. A NPO shall determine the cost of a self-constructed investment property in accordance with paragraphs G17.10–G17.14.
- G16.7 An NPO shall measure **donated investment property** at fair value at initial recognition. Fair value shall be determined in accordance with Section 12 *Fair value measurement*.
- G16.8 The initial cost of a property interest held under a **lease** and classified as an investment property shall be as prescribed for a finance lease by paragraph G20.9, even if the lease would otherwise be classified as an operating lease if it was in the scope of Section 20 *Leases*. In other words, the **asset** is recognised at the lower of the fair value of the property and the present value of the **minimum lease payments**. An equivalent amount is recognised as a **liability** in accordance with paragraph G20.9.

Measurement after initial recognition

- G16.9 Investment property whose fair value can be measured reliably without undue cost or effort shall be measured at fair value at each **reporting date** with changes in fair value recognised in **surplus or deficit**. If a property interest held under a lease is classified as investment property, the item accounted for at fair value is that interest and not the underlying property. Section 12 *Fair value measurement* provides guidance on determining fair value. A NPO shall account for all other investment property using the cost model in Section 17.

Transfers

- G16.10 If a reliable measure of fair value is no longer available without undue cost or effort for an item of investment property measured using the fair value model, the NPO shall thereafter account for that item in accordance with Section 17 until a reliable measure of fair value becomes available. The **carrying amount** of the investment property on that date becomes its cost under Section 17. Paragraph G16.12(d)(iii) requires disclosure of this change. It is a change of circumstances and not a change in accounting policy.
- G16.11 Other than as required by paragraph G16.10, an NPO shall transfer a property to, or from, investment property only when there is a change of use. This occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of a change in use.

Disclosures

G16.12 An **NPO** shall disclose the following for all investment property accounted for at fair value through **surplus or deficit** (paragraph **G16.9**):

- a) the extent to which the fair value of investment property (as measured or disclosed in the financial statements) is based on a valuation by an independent valuer who holds a recognised and relevant professional qualification and has recent experience in the location and class of the investment property being valued. If there has been no such valuation, that fact shall be disclosed.
- b) the existence and amounts of restrictions on the realisability of investment property or the remittance of **income** and proceeds of disposal.
- c) contractual obligations to purchase, construct or develop investment property or for repairs, maintenance or enhancements.
- d) a reconciliation between the carrying amounts of investment property at the beginning and end of the period, showing separately:
 - i. additions, disclosing separately those additions resulting from acquisitions through **business combinations**;
 - ii. net **gains** or losses from fair value adjustments;
 - iii. transfers to and from investment property carried at cost less accumulated **depreciation** and **impairment** (see paragraph **G16.10**);
 - iv. transfers to and from **inventories** and owner-occupied property; and
 - v. other changes.

This reconciliation need not be presented for prior periods.

G16.13 In accordance with Section 20, the owner of an investment property provides lessors' disclosures about leases into which it has entered. An **NPO** that holds an investment property under a finance lease or operating lease provides lessees' disclosures for finance leases and lessors' disclosures for any operating leases into which it has entered.

Annex B – Property, plant and equipment

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Section 17 – *Property, plant and equipment*

Scope of this section

- G17.1 This section applies to accounting for **property, plant and equipment** and accounting for **investment property** whose **fair value** cannot be measured reliably without undue cost or effort on an ongoing basis. Section 16 *Investment property* applies to investment property whose fair value can be measured reliably without undue cost or effort.
- G17.2 Property, plant and equipment are tangible **assets** that:
- are held for use in the **ordinary activities of the NPO**, for rental to others, or for NPO's administrative purposes; and
 - are expected to be used during more than one period.
- G17.3 Property, plant and equipment does not include:
- biological assets** related to **agricultural activity** other than bearer plants that can be measured separately from the produce on them without undue cost or effort (see Section 34 *Specialised activities*). This section applies to bearer plants but it does not apply to the produce on bearer plants; and
 - mineral rights and mineral reserves, such as oil, natural gas and similar non-regenerative resources.

Recognition

- G17.4 An **NPO** shall recognise the cost of an item of property, plant and equipment as an asset if, and only if:
- it is **probable** that **economic benefits or service potential** associated with the item will flow to the **NPO**; and
 - the cost of the item can be measured reliably.
- G17.5 Items such as spare parts, stand-by equipment and servicing equipment are recognised in accordance with this section when they meet the definition of property, plant and equipment. Otherwise, such items are classified as **inventory**.
- G17.6 Parts of some items of property, plant and equipment may require replacement at regular intervals (for example, the roof of a building). An **NPO** shall add to the **carrying amount** of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if the replacement part is expected to provide incremental future **benefit or service potential** to the **NPO**. The carrying amount of those parts that are replaced is **derecognised** in accordance with paragraphs G17.32–G17.35

regardless of whether the replaced parts had been depreciated separately. If it is not practicable for an NPO to determine the carrying amount of the replaced part, the NPO may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or constructed. Paragraph G17.21 provides that if the major components of an item of property, plant and equipment have significantly different patterns of consumption of **economic benefits or service potential**, an NPO shall allocate the initial cost of the asset to its major components and **depreciate** each such component separately over its **useful life**.

- G17.7 A condition of continuing to operate an item of property, plant and equipment (for example, a bus) may be performing regular major inspections for faults regardless of whether parts of the item are replaced. When each major inspection is performed, its cost is recognised in the carrying amount of the item of property, plant and equipment as a replacement if the recognition criteria are satisfied. Any remaining carrying amount of the cost of the previous major inspection (as distinct from physical parts) is derecognised. This is done regardless of whether the cost of the previous major inspection was identified in the transaction in which the item was acquired or constructed. If necessary, the estimated cost of a future similar inspection may be used as an indication of what the cost of the existing inspection component was when the item was acquired or constructed.
- G17.8 Land and buildings are separable assets and an NPO shall account for them separately, even when they are acquired together.

Measurement at recognition

- G17.9 An NPO shall measure an item of property, plant and equipment **that has been acquired or constructed** at initial recognition at its cost.

Elements of cost

- G17.10 The cost of an item of property, plant and equipment comprises all of the following:
- its purchase price, including legal and brokerage fees, import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
 - any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. These can include the costs of site preparation, initial delivery and handling, installation and assembly and testing of functionality.
 - the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

- G17.11 The following costs are not costs of an item of property, plant and equipment and an NPO shall recognise them as an **expense** when they are incurred:
- a) costs of opening a new facility;
 - b) costs of introducing a new **service or product** (including costs of advertising and promotional activities);
 - c) costs of conducting **operations** in a new location or with a new class of **service recipient or customer** (including costs of staff training);
 - d) administration and other general overhead costs; and
 - e) **borrowing costs** (see Section 25 *Borrowing costs*).
- G17.12 The **income** and related expenses of incidental operations during construction or development of an item of property, plant and equipment are recognised in **surplus or deficit** if those operations are not necessary to bring the item to its intended location and operating condition.

Measurement of cost

- G17.13 The cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the cost is the **present value** of all future payments.

Exchanges of assets

- G17.14 An item of property, plant or equipment may be acquired in exchange for a non-monetary asset, or assets, or a combination of monetary and non-monetary assets. An NPO shall measure the cost of the acquired asset at fair value unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset received nor the asset given up is reliably measurable. In that case, the asset's cost is measured at the carrying amount of the asset given up.
- G17.15 An NPO shall measure the cost of an item of property, plant and equipment that has been donated at initial recognition at its fair value in line with the guidance in Section 12 *Fair value measurement*.

Measurement after initial recognition

- G17.16 An NPO shall choose either the cost model in paragraph G17.17 or the revaluation model in paragraph G17.18 as its accounting policy and shall apply that policy to an entire class of property, plant and equipment. An NPO shall apply the cost model to investment property whose fair value cannot be measured reliably without undue cost or effort. An NPO shall recognise the costs of day-to-day servicing of an item of property, plant and equipment in **surplus or deficit** in the period in which the costs are incurred.

Cost model

G17.17 An **NPO** shall measure an item of property, plant and equipment after initial recognition at cost less any accumulated **depreciation** and any accumulated **impairment losses**.

Revaluation model

G17.18 An **NPO** shall measure an item of property, plant and equipment whose fair value can be measured reliably at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ **materially** from that which would be determined using fair value at the end of the **reporting period**. Section 12 provides guidance on determining fair value. If an item of property, plant and equipment is revalued, the entire class of property, plant and equipment to which that asset belongs shall be revalued.

G17.19 If an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognised in the **Statement of Changes in Net Assets** and accumulated ~~in equity~~ under the heading of revaluation surplus. However, the increase shall be recognised in **surplus or deficit** to the extent that it reverses a revaluation decrease of the same asset previously recognised in **surplus or deficit**.

G17.20 If an asset's carrying amount is decreased as a result of a revaluation, the decrease shall be recognised in **surplus or deficit**. However, the decrease shall be recognised in **Statement of Changes in Net Assets** to the extent of any credit balance existing in the revaluation surplus in respect of that asset. The decrease recognised in **Statement of Changes in Net Assets** reduces the amount accumulated ~~in equity~~ under the heading of revaluation surplus.

Depreciation

G17.21 If the major components of an item of property, plant and equipment have significantly different patterns of consumption of **economic benefits or service potential**, an **NPO** shall allocate the initial cost of the asset to its major components and depreciate each such component separately over its useful life. Other assets shall be depreciated over their useful lives as a single asset. With some exceptions, such as quarries and sites used for landfill, land has an unlimited useful life and therefore is not depreciated.

G17.22 The depreciation charge for each period shall be recognised in **surplus or deficit** unless another section of this **Guidance** requires the cost to be recognised as part of the cost of an asset. For example, the depreciation of manufacturing property, plant and equipment is included in the costs of inventories (see Section 13 *Inventories*).

Depreciable amount and depreciation period

- G17.23 An **NPO** shall allocate the **depreciable amount** of an asset on a systematic basis over its useful life.
- G17.24 Factors such as a change in how an asset is used, significant unexpected wear and tear, technological advancement and changes in market prices may indicate that the **residual value** or useful life of an asset has changed since the most recent annual **reporting date**. If such indicators are present, an **NPO** shall review its previous estimates and, if current expectations differ, amend the residual value, depreciation method or useful life. The **NPO** shall account for the change in residual value, depreciation method or useful life as a change in an **accounting estimate** in accordance with paragraphs G10.19–G10.22.
- G17.25 Depreciation of an asset begins when it is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases when the asset is derecognised. Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.
- G17.26 An **NPO** shall consider all the following factors in determining the useful life of an asset:
- a) the expected usage of the asset. Usage is assessed by reference to the asset's expected capacity or physical output.
 - b) expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme, and the care and maintenance of the asset while idle.
 - c) technical or commercial obsolescence arising from changes or improvements in **usage**, or from a change in the market demand for the service **or product** output of the asset. Expected future reductions in the selling price of an item that was produced using an asset could indicate the expectation of technical or commercial obsolescence of the asset.
 - d) legal or similar limits on the use of the asset, such as the expiry dates of related **leases**.

Depreciable method

- G17.27 An **NPO** shall select a depreciation method that reflects the pattern in which it expects to consume the asset's **economic benefits or service potential**. The possible depreciation methods include the straight-line method, the diminishing balance method and a method based on usage such as the units of production method. A depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is not appropriate.

G17.28 If there is an indication that there has been a significant change since the last annual reporting date in the pattern by which an NPO expects to consume an asset's future economic benefits, the NPO shall review its present depreciation method and, if current expectations differ, change the depreciation method to reflect the new pattern. The NPO shall account for the change as a change in an accounting estimate in accordance with paragraphs G10.19–G10.22.

Impairment

Recognition and measurement of impairment

G17.29 At each reporting date, an NPO shall apply Section 27 *Impairment of Assets* to determine whether an item or group of items of property, plant and equipment is impaired and, if so, how to recognise and measure the impairment loss. That section explains when and how an NPO reviews the carrying amount of its assets, how it determines the **recoverable amount** of an asset, and when it recognises or reverses an impairment loss.

Compensation for impairment

G17.30 An NPO shall include in **surplus or deficit** compensation from third parties for items of property, plant and equipment that were impaired, lost or given up only when the compensation becomes receivable.

Property, plant and equipment held for sale

G17.31 Paragraph **G27.9(f)** states that a plan to dispose of an asset before the previously expected date is an indicator of impairment that triggers the calculation of the asset's recoverable amount for the purpose of determining whether the asset is impaired.

Derecognition

G17.32 An NPO shall derecognise an item of property, plant and equipment:

- a) on disposal; or
- b) when no future **economic benefits or service potential** are expected from its use or disposal.

G17.33 An NPO shall recognise the **gain** or loss on the **derecognition** of an item of property, plant and equipment in **surplus or deficit** when the item is derecognised (unless Section 20 *Leases* requires otherwise on a sale and leaseback). The NPO shall not classify such gains as **revenue**.

- G17.34 The date of disposal of an item is the date the recipient obtains control of that item in accordance with the requirements in paragraphs G23.142–G23.157 for determining when a promise is satisfied. Section 20 applies to disposal by a sale and leaseback.
- G17.35 An NPO shall determine the gain or loss arising from the derecognition of an item of property, plant and equipment as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

Disclosures

- G17.36 An NPO shall disclose the following for each class of property, plant and equipment determined in accordance with paragraph G4.11(a) and separately for investment property carried at cost less accumulated depreciation and impairment:
- the **measurement** bases used for determining the gross carrying amount;
 - the depreciation methods used;
 - the useful lives or the depreciation rates used;
 - the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period; and
 - a reconciliation of the carrying amount at the beginning and end of the reporting period showing separately:
 - additions;
 - disposals;
 - acquisitions through **business combinations**;
 - increases or decreases resulting from revaluations under paragraphs G17.18–G17.20 and from impairment losses recognised or reversed in the *Statement of Changes in Net Assets* in accordance with Section 27;
 - transfers to and from investment property carried at fair value through *surplus or deficit* (see paragraph G16.10);
 - impairment losses recognised or reversed in *surplus or deficit* in accordance with Section 27;
 - depreciation; and
 - other changes.

This reconciliation need not be presented for prior periods.
- G17.37 An NPO shall also disclose the following:
- the existence and carrying amounts of property, plant and equipment to which the NPO has restricted title or that is pledged as security for **liabilities**;
 - the amount of contractual commitments for the acquisition of property, plant and equipment; and
 - if an NPO has investment property whose fair value cannot be measured reliably without undue cost or effort it shall disclose that fact and the reasons why fair value

measurement would involve undue cost or effort for those items of investment property.

G17.38 If items of property, plant and equipment are stated at revalued amounts, an entity shall disclose the following:

- a) the effective date of the revaluation;
- b) whether an independent valuer was involved;
- c) for each revalued class of property, plant and equipment, the carrying amount that would have been recognised had the assets been carried under the cost model; and
- d) the revaluation surplus, indicating the change for the period and any restrictions on the distribution of the balance to ~~shareholders~~ those that have a controlling interest the NPO.

Annex C – Intangible not including goodwill

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Section 18 – *Intangibles not including goodwill*

Scope and objective of this section

- G18.1 This section applies to accounting for all **intangible assets** other than **goodwill** (see Section 19 *Business combinations and goodwill*), intangible assets held by an **NPO** for sale in the ordinary course of business (see Section 13 *Inventories*) and assets arising from contracts with customers (see Section 23 *Revenue*).
- G18.2 An intangible asset is an identifiable non-monetary **asset** without physical substance. Such an asset is identifiable when:
- a) it is separable, ie capable of being separated or divided from the **NPO** and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, asset or **liability**; or
 - b) it arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the **NPO** or from other rights and obligations.
- G18.3 This section does not apply to the following:
- a) **financial assets**; or
 - b) mineral rights and mineral reserves, such as oil, natural gas and similar non-regenerative resources.

Recognition

- G18.4 An **NPO** shall recognise an intangible asset as an asset if, and only if:
- a) it is **probable** that the expected **economic benefit or service potential** that are attributable to the asset will flow to the **NPO**;
 - b) the cost or value of the asset can be measured reliably; and
 - c) the asset does not result from expenditure incurred internally on an intangible item.

General principle for recognising intangible assets

- G18.5 This section uses the term asset in a way that differs in some respects from the definition of an asset in the Glossary. Therefore, when applying this section, an **NPO** shall apply the definition of an asset in paragraph **G18.6**.
- G18.6 For the purpose of this section, an asset is a resource controlled by the **NPO** as a result of past events and from which **economic benefit or service potential** are expected to flow to the **NPO**.

- G18.7 An NPO shall assess the probability of expected **economic benefit or service potential** using reasonable and supportable assumptions that represent management's best estimate of the economic conditions that will exist over the **useful life** of the asset.
- G18.8 An NPO uses judgement to assess the degree of certainty attached to the flow of **economic benefit or service potential** that are attributable to the use of the asset on the basis of the evidence available at the time of initial recognition, giving greater weight to external evidence.
- G18.9 The probability recognition criterion in paragraph **G18.4(a)** is always considered satisfied for intangible assets that are separately acquired.
- G18.10 An intangible asset acquired in a **business combination** shall be recognised unless its **fair value** cannot be measured reliably without undue cost or effort at the acquisition date.

Initial Measurement

- G18.11 An NPO shall measure an intangible asset initially at cost.

Separate acquisition

- G18.12 The cost of a separately acquired intangible asset comprises:
- its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates; and
 - any directly attributable cost of preparing the asset for its intended use.

Acquisition as part of a business combination

- G18.13 An intangible asset acquired in a business combination shall be recognised unless its **fair value** cannot be measured reliably without undue cost or effort at the acquisition date.

Acquisition by way of government grant

- G18.14 If an intangible asset is acquired by way of a **government grant**, the cost of that intangible asset is its fair value at the date the grant is received or receivable in accordance with Section ~~24 Government Grants~~ 23 Part I *Revenue from grants and donations*.

Exchanges of assets

- G18.15 An intangible asset may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. An NPO shall measure the cost of such an intangible asset at fair value unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset received nor the asset given up is

reliably measurable. In that case, the asset's cost is measured at the **carrying amount** of the asset given up.

Internally generated assets

- G18.16 An **NPO** shall recognise expenditure incurred internally on an intangible item, including all expenditure for both **research** and **development** activities, as an **expense** when it is incurred unless it forms part of the cost of another asset that meets the recognition criteria in this **Guidance**.
- G18.17 As examples of applying the preceding paragraph, an **NPO** shall recognise expenditure on the following items as an expense and shall not recognise such expenditure as intangible assets:
- internally generated brands, logos, publishing titles, customer lists and items similar in substance;
 - start-up activities (ie start-up costs), which include establishment costs such as legal and secretarial costs incurred in establishing an **NPO**, expenditure to open a new facility or **activity** (ie pre-opening costs) and expenditure for starting new operations or launching new products or processes (ie pre-operating costs);
 - training activities;
 - advertising and promotional activities;
 - relocating or reorganising part or all of an **NPO**; and
 - internally generated goodwill.
- G18.18 Paragraph G18.17 does not preclude recognising a prepayment as an asset when payment for goods or services has been made in advance of the delivery of the goods or the rendering of the services.

Past expenses not to be recognised as an asset

- G18.19 Expenditure on an intangible item that was initially recognised as an expense shall not be recognised at a later date as part of the cost of an asset.

Measurement after recognition

- G18.20 An **NPO** shall measure intangible assets at cost less any accumulated **amortisation** and any accumulated **impairment losses**. The requirements for amortisation are set out in this section. The requirements for recognition of impairment are set out in Section 27 *Impairment of assets*.

Useful life

- G18.21 For the purpose of this **Guidance**, all intangible assets shall be considered to have a finite useful life. The useful life of an intangible asset that arises from contractual or other legal

rights shall not exceed the period of the contractual or other legal rights, but may be shorter depending on the period over which the NPO expects to use the asset. If the contractual or other legal rights are conveyed for a limited term that can be renewed, the useful life of the intangible asset shall include the renewal period(s) only if there is evidence to support renewal by the entity without significant cost.

G18.22 If the useful life of an intangible asset cannot be established reliably, the life shall be determined based on management's best estimate but shall not exceed ten years.

Amortisation period and amortisation method

G18.23 An NPO shall allocate the **depreciable amount** of an intangible asset on a systematic basis over its useful life. The amortisation charge for each period shall be recognised as an expense, unless another section of this Guidance requires the cost to be recognised as part of the cost of an asset such as **inventories** or **property, plant and equipment**.

G18.24 Amortisation begins when the intangible asset is available for use, ie when it is in the location and condition necessary for it to be usable in the manner intended by management. Amortisation ceases when the asset is derecognised. The NPO shall choose an amortisation method that reflects the pattern in which it expects to consume the asset's **economic benefit or service potential**. If the NPO cannot determine that pattern reliably, it shall use the straight-line method.

G18.25 There is a presumption that an amortisation method based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate. However, an NPO may rebut this presumption and use an amortisation method based on revenue generated by an activity that includes the use of an intangible asset only if it provides a reliable pattern of how **economic benefit or service potential** are consumed:

- a) in which the intangible asset is expressed as a measure of revenue (that is, when rights over the use of an intangible asset is specified as a fixed total amount of revenue to be generated); or
- b) when it can be demonstrated that revenue and the consumption of the intangible asset's **economic benefit or service potential** are highly correlated.

Residual value

G18.26 An NPO shall assume that the **residual value** of an intangible asset is zero unless:

- a) there is a commitment by a third party to purchase the asset at the end of its useful life; or
- b) there is an **active market** for the asset and:
 - i. residual value can be determined by reference to that market; and
 - ii. it is probable that such a market will exist at the end of the asset's useful life.

Review of amortisation period and amortisation method

G18.27 Factors such as a change in how an intangible asset is used, technological advancement; and changes in market prices may indicate that the residual value or useful life of an intangible asset has changed since the most recent annual **reporting date**. If such indicators are present, an NPO shall review its previous estimates and, if current expectations differ, amend the residual value, amortisation method or useful life. The NPO shall account for the change in residual value, amortisation method or useful life as a **change in an accounting estimate** in accordance with paragraphs G10.19–G10.22.

Recoverability of the carrying amount—impairment losses

G18.28 To determine whether an intangible asset is impaired, an NPO shall apply Section 27. That section explains when and how an NPO reviews the carrying amount of its assets, how it determines the **recoverable amount**, of an asset and when it recognises or reverses an impairment loss.

Retirements and disposals

G18.29 An NPO shall derecognise an intangible asset, and shall recognise a **gain** or loss in **surplus or deficit**:

- a) on disposal; or
- b) when no **economic benefit or service potential** are expected from its use or disposal.

Disclosures

G18.30 A NPO shall disclose the following for each class of intangible assets:

- a) the useful lives or the amortisation rates used;
- b) the amortisation methods used;
- c) the gross carrying amount and any accumulated amortisation (aggregated with accumulated impairment losses) at the beginning and end of the **reporting period**;
- d) the line item(s) in the **Statement of Income and Expenses**, in which any amortisation of intangible assets is included; and
- e) a reconciliation of the carrying amount at the beginning and end of the reporting period showing separately:
 - i. additions;
 - ii. disposals;
 - iii. acquisitions through business combinations;
 - iv. amortisation;
 - v. impairment losses recognised or reversed in **surplus or deficit** in accordance with Section 27; and
 - vi. other changes.
 This reconciliation need not be presented for prior periods.

G18.31 An NPO shall also disclose:



- a) a description, the carrying amount and remaining amortisation period of any individual intangible asset that is **material** to the **NPO's financial statements**;
- b) for intangible assets acquired by way of a grant and initially recognised at fair value (see paragraph **G18.14**):
 - i. the fair value initially recognised for these assets; and
 - ii. their carrying amounts.
- c) the existence and carrying amounts of intangible assets to which the **NPO** has restricted title or that are pledged as security for liabilities; and
- d) the amount of contractual commitments for the acquisition of intangible assets.

G18.32 An **NPO** shall disclose the aggregate amount of research and development expenditure recognised as an expense during the period (ie the amount of expenditure incurred internally on research and development that has not been capitalised as part of the cost of another asset that meets the recognition criteria in this **Guidance**).

Annex D – Leases

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Section 20 – Leases

Scope of this section

- G20.1 This section covers accounting for all leases other than:
- a) leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources (see Section 34 Specialised activities);
 - b) licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights (see Section 18 Intangible assets other than goodwill);
 - c) measurement of property held by lessees that is accounted for as investment property and measurement of investment property provided by lessors under operating leases (see Section 16 Investment property);
 - d) measurement of biological assets held by lessees under finance leases and biological assets provided by lessors under operating leases (see Section 34);
 - e) leases that could lead to a loss to the lessor or the lessee as a result of contractual terms that are unrelated to changes in the price of the leased asset, changes in foreign exchange rates, changes in lease payments based on variable market interest rates, or a default by one of the counterparties (see paragraph G11.60(f)); and
 - f) operating leases that are onerous.
- G20.2 This section applies to agreements that transfer the right to use assets even though substantial services by the lessor may be called for in connection with the operation or maintenance of such assets. This section does not apply to agreements that are contracts for services that do not transfer the right to use assets from one contracting party to the other.
- G20.3 Some arrangements, such as some outsourcing arrangements, telecommunication contracts that provide rights to capacity and take-or-pay contracts, do not take the legal form of a lease but convey rights to use assets in return for payments. Such arrangements are in substance leases of assets and they shall be accounted for under this section.

Classification of Leases

- G20.4 A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.
- G20.5 Whether a lease is a finance lease or an operating lease depends on the substance of the transaction instead of the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:

- a) the lease transfers ownership of the asset to the lessee by the end of the lease term;
- b) the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the **fair value** at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised;
- c) the lease term is for the major part of the economic life of the asset even if title is not transferred;
- d) at the inception of the lease the **present value** of the **minimum lease payments** amounts to at least substantially all of the fair value of the leased asset; and
- e) the leased assets are of such a specialised nature that only the lessee can use them without major modifications.

G20.6 Indicators of situations that individually or in combination could also lead to a lease being classified as a finance lease are:

- a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
- b) **gains** or losses from the fluctuation in the **residual value** of the leased asset accrue to the lessee (for example, in the form of a rent rebate equalling most of the sales proceeds at the end of the lease); and
- c) the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

G20.7 The examples and indicators in **paragraphs G20.5 and G20.6** are not always conclusive. If it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease. For example, this may be the case if ownership of the asset is transferred to the lessee at the end of the lease for a variable payment equal to the asset's then fair value, or if there are contingent rents, as a result of which the lessee does not have substantially all risks and rewards incidental to ownership.

G20.8 Lease classification is made at the inception of the lease and is not changed during the term of the lease unless the lessee and the lessor agree to change the provisions of the lease (other than simply by renewing the lease), in which case the lease classification shall be re-evaluated.

Financial statements of lessees—finance leases

Initial recognition

G20.9 At the commencement of the lease term, a lessee shall recognise its rights of use and obligations under finance leases as assets and liabilities in its **Statement of Financial Position** at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, determined at the inception of the lease. Any

initial direct costs of the lessee (incremental costs that are directly attributable to negotiating and arranging a lease) are added to the amount recognised as an asset.

G20.10 The present value of the minimum lease payments shall be calculated using the **interest rate implicit in the lease**. If this cannot be determined, the **lessee's incremental borrowing rate** shall be used

Subsequent measurement

G20.11 A lessee shall apportion minimum lease payments between the finance charge and the reduction of the outstanding liability using the **effective interest method** (see paragraphs G11.19–G11.24). The lessee shall allocate the finance charge to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. A lessee shall charge contingent rents as **expenses** in the periods in which they are incurred.

G20.12 A lessee shall depreciate an asset leased under a finance lease in accordance with the relevant section of this Standard for that type of asset, for example, Section 17 *Property, plant and equipment*, Section 18 or Section 19 *Business combinations and goodwill*. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its **useful life**. A lessee shall also assess at each **reporting date** whether an asset leased under a finance lease is impaired (see Section 27 *Impairment of assets*).

Disclosures

G20.13 A lessee shall make the following disclosures for finance leases:

- a) for each **class of asset**, the net **carrying amount** at the end of the **reporting period**;
- b) the total of future minimum lease payments at the end of the reporting period, for each of the following periods:
 - i. not later than one year;
 - ii. later than one year and not later than five years; and
 - iii. later than five years.
- c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases and restrictions imposed by lease arrangements.

G20.14 In addition, the requirements for disclosure about assets in accordance with Sections 17, 18, 27 and 34 apply to lessees for assets leased under finance leases.

Financial statements of lessees—operating leases

G20.15 A lessee shall recognise lease payments under operating leases (excluding costs for services such as insurance and maintenance) as an expense over the lease term on a straight-line basis unless either:

- a) another systematic basis is representative of the time pattern of the user's benefit, even if the payments are not on that basis; or
- b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases.

If payments to the lessor vary because of factors other than general inflation, then the condition (b) is not met.

Disclosures

G20.16 A lessee shall make the following disclosures for operating leases:

- a) the total of future minimum lease payments under non-cancellable operating leases for each of the following periods:
 - i. not later than one year;
 - ii. later than one year and not later than five years; and
 - iii. later than five years.
- b) lease payments recognised as an expense; and
- c) a general description of the lessee's significant leasing arrangements including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

Financial statements of lessors—finance leases

Initial recognition and measurement

G20.17 A lessor shall recognise assets held under a finance lease in its **Statement of Financial Position** and present them as a receivable at an amount equal to the **net investment in the lease**. The net investment in a lease is the lessor's **gross investment in the lease** discounted at the interest rate implicit in the lease. The gross investment in the lease is the aggregate of:

- (a) the minimum lease payments receivable by the lessor under a finance lease; and
- (b) any unguaranteed residual value accruing to the lessor..

G20.18 For finance leases other than those involving manufacturer or dealer lessors, initial direct costs (costs that are incremental and directly attributable to negotiating and arranging a lease) are included in the initial measurement of the finance lease receivable and reduce the amount of revenue recognised over the lease term.

Subsequent measurement

G20.19 The **recognition** of finance income shall be based on a pattern reflecting a constant periodic rate of return on the lessor's net investment in the finance lease. Lease payments relating to the period, excluding costs for services, are applied against the gross investment in the lease to reduce both the principal and the unearned finance income. If there is an indication that the estimated unguaranteed residual value used in computing the lessor's gross investment in the lease has changed significantly, the income allocation over the lease term is revised, and any reduction in respect of amounts accrued is recognised immediately in **surplus or deficit**.

Manufacturer or dealer lessors

G20.20 Manufacturers or dealers often offer to customers the choice of either buying or leasing an asset. A finance lease of an asset by a manufacturer or dealer lessor gives rise to two types of income:

- a) **surplus or deficit** equivalent to the **surplus or deficit** resulting from an outright sale of the asset being leased, at normal selling prices, reflecting any applicable volume or trade discounts; and
- b) finance income over the lease term.

G20.21 The sales **revenue** recognised at the commencement of the lease term by a manufacturer or dealer lessor is the fair value of the asset or, if lower, the present value of the minimum lease payments accruing to the lessor, computed at a market rate of interest. The cost of sale recognised at the commencement of the lease term is the cost, or carrying amount if different, of the leased asset less the present value of the unguaranteed residual value. The difference between the sales revenue and the cost of sale is the **selling surplus**, which is recognised in accordance with the NPO's policy for outright sales.

G20.22 If artificially low rates of interest are quoted, **selling surplus** shall be restricted to that which would apply if a market rate of interest were charged. Costs incurred by manufacturer or dealer lessors in connection with negotiating and arranging a lease shall be recognised as an expense when the **selling surplus** is recognised.

Disclosures

G17.23 A lessor shall make the following disclosures for finance leases:

- a) a reconciliation between the gross investment in the lease at the end of the reporting period and the present value of minimum lease payments receivable at the end of the reporting period. In addition, a lessor shall disclose the gross investment in the lease and the present value of minimum lease payments receivable at the end of the reporting period, for each of the following periods:

- i. not later than one year;
 - ii. later than one year and not later than five years; and
 - iii. later than five years.
- b) unearned finance income.
- c) the unguaranteed residual values accruing to the benefit of the lessor.
- d) the accumulated allowance for uncollectable minimum lease payments receivable.
- e) contingent rents recognised as income in the period.
- f) a general description of the lessor's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases, and restrictions imposed by lease arrangements.

Financial statements of lessors—operating leases

Recognition and Measurement

G20.24 A lessor shall present assets subject to operating leases in its **Statement of Financial Position** according to the nature of the asset.

G20.25 A lessor shall recognise lease income from operating leases (excluding amounts for services such as insurance and maintenance) in **surplus or deficit** on a straight-line basis over the lease term, unless either:

- a) another systematic basis is representative of the time pattern of the lessee's benefit from the leased asset, even if the receipt of payments is not on that basis; or
- b) the payments to the lessor are structured to increase in line with expected general inflation (based on published indexes or statistics) to compensate for the lessor's expected inflationary cost increases.

If payments to the lessor vary according to factors other than inflation, then condition (b) is not met.

G20.26 A lessor shall recognise as an expense costs, including **depreciation**, incurred in earning the lease income. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets.

G20.27 A lessor shall add to the carrying amount of the leased asset any initial direct costs it incurs in negotiating and arranging an operating lease and shall recognise such costs as an expense over the lease term on the same basis as the lease income.

G20.28 To determine whether a leased asset has become impaired, a lessor shall apply Section 27.

G20.29 A manufacturer or dealer lessor does not recognise any **selling surplus** on entering into an operating lease because it is not the equivalent of a sale.

Disclosures

G20.30 A lessor shall disclose the following for operating leases:

- a) the future minimum lease payments under non-cancellable operating leases for each of the following periods:
 - i. not later than one year;
 - ii. later than one year and not later than five years; and
 - iii. later than five years.
- b) total contingent rents recognised as income; and
- c) a general description of the lessor's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses and restrictions imposed by lease arrangements.

G20.31 In addition, the requirements for disclosure about assets in accordance with Sections 17, 18, 27 and 34 apply to lessors for assets provided under operating leases

Sale and leaseback transactions

G20.32 A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent because they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends on the type of lease.

Sale and leaseback transaction results in a finance lease

G20.33 If a sale and leaseback transaction results in a finance lease, the seller-lessee shall not recognise immediately, as income, any excess of sales proceeds over the carrying amount. Instead, the seller-lessee shall defer such excess and amortise it over the lease term.

Sale and leaseback transaction results in an operating lease

G17.34 If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, the seller-lessee shall recognise any **surplus or deficit** immediately. If the sale price is below fair value, the seller-lessee shall recognise any **surplus or deficit** immediately unless the **deficit** is compensated for by future lease payments at below market price. In that case the seller-lessee shall defer and amortise such **deficit** in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the seller-lessee shall defer the excess over fair value and amortise it over the period for which the asset is expected to be used.

Disclosures

G17.35 Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of significant leasing arrangements includes description of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.

Implementation guidance

Section 20 - Leases

Example of applying paragraph G20.15(b):

NPO X operates in a jurisdiction in which the consensus forecast by local banks is that the general price level index, as published by the government, will increase by an average of 10 per cent annually over the next five years. NPO X leases some office space from entity Y for five years under an operating lease. The lease payments are structured to reflect the expected 10 per cent annual general inflation over the five-year term of the lease as follows

Year 1	CU100,000
Year 2	CU110,000
Year 3	CU121,000
Year 4	CU133,000
Year 5	CU146,000

NPO X recognises annual rent expense equal to the amounts owed to the lessor. If the escalating payments are not clearly structured to compensate the lessor for expected inflationary cost increases based on published indexes or statistics, then NPO X recognises annual rent expense on a straight-line basis: CU122,000 each year (sum of the amounts payable under the lease divided by five years).