

Friday, 5 September 2025

## **Preliminary Staff Views: AASB 16 Leases**

This document contains preliminary staff views on *Invitation to Comment (ITC) 55 Post-implementation Review of AASB 16 Leases*. We have not provided separate responses to Questions 2 and 3 of **Section 1 – AASB General Matters for Comment**, as they have been addressed within our responses to specific questions in **Sections 2 and 3**.

These views are informed by direct outreach and consultation with stakeholders, as well as discussions held in technical and professional forums.

### **Overall view**

Our overall view is that IFRS 16 achieves its technical objective of providing relevant and faithful representation of lease transactions, with users affirming its usefulness. Despite benefits such as improved data quality and coordination, the cost and complexity of compliance are widely seen as disproportionate. There is minimal appetite for fundamental change, but strong support exists for targeted improvements, clearer guidance in judgement-heavy areas, and simplification where feasible.

### **AASB General Matters for Comment (AASB ITC 55 Section 1)**

#### ***Question 1: Are there any regulatory issues or other issues arising in the Australian environment that adversely affect the application of AASB 16 Leases?***

- Stakeholder feedback indicated instances in Australia where leases are extended by way of amending the termination date and payment terms of the original lease, rather than issuing a new lease agreement. This creates uncertainty as to whether such changes constitute a lease modification or a new lease under AASB 16. We recommend that the AASB investigate this issue further and consider providing more specific guidance tailored to common Australian leasing practices.

### **NFP and public sector topics (AASB ITC 55 Section 2)**

#### ***Topic 1: Application of AASB 16***

- Users of NFP and public sector entities' financial statements are typically primarily concerned with funding, resourcing, and service allocation. As such, the undue cost and effort for these entities is often viewed as unjustified relative to its usefulness.
- Smaller NFP and public sector entities face heightened challenges due to system limitations and the complexity of scenarios such as subleases and multiple discount rates. Lower-cost software often lacks necessary functionality, requiring manual workarounds and increasing risk of error. Some entities advised the complexity necessitates full-time staff solely dedicated to lease accounting.

- Auditors advised that lease accounting consumes a sizable portion of audit effort, with several adjustments stemming from preparer misinterpretation or misapplication of the standard.
- While there is little appetite for fundamental change due to potential disruption, these entities consistently support targeted simplifications such as practical expedients, materiality thresholds and “plain English” language in guidance.

### **Topic 2: Lease term**

- Lease term assessment is particularly complicated in NFP and public sector due to the existence of informal or open-ended arrangements, which lack clear documentation and duration, making consistent application of the standard difficult.
- Public sector entities frequently face uncertainty in determining the lease commencement date, particularly when properties are accessed for fitouts prior to the lease agreement commencement date.

### **Topic 3: Lease modifications**

- Modifications and reassessments are consistently identified as a key challenge.
- The complexity of determining whether a change constitutes a modification or reassessment is exacerbated by the informal arrangements and cost-sharing agreements prevalent in these sectors.
- Stakeholders have called for explicit criteria, decision trees or illustrative examples to assist in distinguishing reassessments from modifications.

### **Topic 4: Measurement of lease liabilities – incremental borrowing rate**

- The interest rate implicit in the lease is rarely available or determinable, and as a result, many default to using the incremental borrowing rate (IBR). However, this is also challenging, as entities in these sectors often lack access to market-based borrowing rates, making it difficult to determine a realistic IBR. Simplified principles and clearer guidance tailored to these sectors would be welcomed.
- Preparers and auditors generally accept that the IBR determined may not be entirely accurate but consider the impact immaterial.

### **Topic 5: Public sector concessionary leases**

- There is unanimous support for making the temporary accounting policy choice to measure concessionary ROU assets at either cost or fair value permanent for NFP public sector entities (like the choice available to NFP private sector entities). It is viewed as a practical expedient that accurately reflects how these entities operate.
- Determining control and assessing whether a sale has occurred is particularly challenging in these sectors when repurchase rights exist, or costs are nominal. Clearer guidance is needed to ensure consistent interpretation.

### Topic 6: Sale and leaseback arrangements

- Sale and leaseback arrangements are prevalent in the NFP and public sectors, but are difficult to account for due to nominal values, informal agreements, inter-agency agreements and cost-sharing structures.
- Determining control and assessing whether a sale has occurred is particularly challenging when repurchase rights exist, or costs are nominal. Clearer guidance is needed to ensure consistent interpretation.
- Preparers would benefit from illustrative examples and decision trees to determine whether a sale has occurred, whether a change is a modification or reassessment, and whether informal arrangements are enforceable.

### IASB Request for Information (AASB ITC 55 Section 3)

#### Question 1: Overall assessment of IFRS 16

- Many stakeholders agreed that IFRS 16 meets its technical objective of providing relevant information that faithfully represents lease transactions.
- While IFRS 16 provides a more comprehensive view of lease obligations than IAS 17, several preparers and users indicated that pre-IFRS 16 figures better reflect an entity's cash position and are therefore preferred for internal decision-making, performance monitoring, and external financing and valuation considerations.
- The indirect benefit of IFRS 16 leading to improvements in data quality and interdepartmental coordination have been acknowledged, but many stakeholders believe the cost of compliance remains disproportionate to the benefits.
- While there is a minimal appetite for fundamental change due to potential disruption, stakeholders support clarification of requirements, additional guidance in judgement-rich areas, and simplification where possible.
- In a poll of over 900 Chartered Accountants at a July 2025 webinar, we gathered targeted insights on the implementation and impact of IFRS 16. The following tables summarise the member responses:

***Do you agree that bringing all leases on the balance sheet has improved the quality and comparability of financial statements?***

■ Strongly agree ■ Agree ■ Neither agree or disagree ■ Disagree ■ Strongly disagree



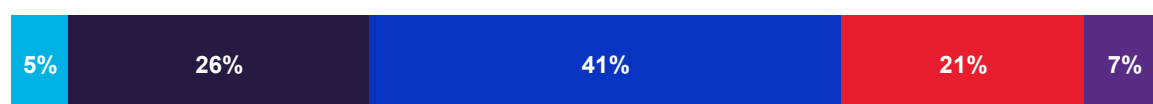
### How would you rate the ongoing cost of applying IFRS 16 Leases compared to expectations?

■ Much higher than expected ■ Higher than expected ■ As expected ■ Lower than expected



### Do you believe the benefits of IFRS 16 Leases exceed the costs?

■ Strongly agree ■ Agree ■ Neither agree or disagree ■ Disagree ■ Strongly disagree



#### Question 2: Lessees' application of judgement

- Broadly, stakeholders agreed that the lessee's application of judgement reduces comparability across entities, thereby reducing the usefulness of the financial information. In addition, the complexity increases preparation and audit costs.
- Areas of specific concern include determination of lease term, discount rates, variable lease payments, and the distinction between reassessment versus modifications.
- **Lease term:** Significant ambiguity exists around assessing the "reasonably certain" threshold for determining lease term, especially in the context of incentives, extension options, and informal or undocumented arrangements. Clearer guidance and illustrative examples are needed to support consistent interpretation.
- **Discount rates:** Many preparers default to using their incremental borrowing rate (IBR) to calculate the discount rate as the information required to calculate the interest rate implicit in the lease is not as readily available. Reference benchmarks or simplified methodologies would assist smaller entities.
- **Variable lease payments:** Payments that appear variable but are economically unavoidable require nuanced interpretation and are often inconsistently applied. While IFRS 16 requires disclosure of excluded variable lease payments, the usefulness of this information depends on how clearly and consistently it is presented. It was suggested to introduce clearer criteria to distinguish between truly variable payments and in-substance fixed payments, particularly for market rent reviews and CPI-linked adjustments.

- **Reassessment or modification:** The distinction is complex, often unclear in practice, and may be unnecessarily burdensome. Stakeholders have called for explicit criteria or decision trees to guide the determination.

### **Question 3: Cash flow**

- Users have indicated a preference for presenting the principal and interest components of lease payments within the same category in the cash flow statement. While IAS 7.31 does not specify a classification for interest paid, grouping the components may improve understandability of the complete transaction.
- Some stakeholders feel the current cash flow presentation of principal payments under financing activities does not always align with the entity's business operations (especially in industries like retail and telecoms). It was suggested that flexibility is permitted in the classification of such lease-related cash flows, possibly drawing on the concept in IFRS 18.50 allowing entities with specified main business activities to classify certain income and expenses in the operating category, even if they would otherwise be classified as investing or financing.
- Classification as financing activities has made it more complex for certain key users (banks, investors, valuers) to compare entities, leading to requests for pre-IFRS 16 adjusted figures.
- We recommend that lease-related cash flows be explored further as part of the IASB's [Statement of Cash Flows and Related Matters](#) project.

### **Question 4: Ongoing costs**

- The IASB anticipated that ongoing costs would be little more than IAS 17 depending on the entity's software (i.e., whether the entity could extend its existing software, or if they needed to migrate to a new system, either entirely or just for lease accounting) and number of leases. Many stakeholders advised that they continue to incur high ongoing costs and see limited benefits.
- Specialist software, outsourcing, or dedicated lease accounting staff are often required to manage the complexity of lease accounting, all of which are costly.
- Main drivers of ongoing costs include initial and subsequent measurement, collection of disclosure information, and determination of discount rate and lease term.
- IFRS 16 issues contribute to a large portion of audit time and cost, with many queries and findings arising from misunderstanding of principals or application of judgment.
- Annual CPI-based lease liability adjustments are operationally burdensome; the US GAAP approach, which does not require remeasurement unless the lease is modified, is more practical.

**Question 5: Transition requirements**

- The first year of reporting under IFRS 16 was particularly challenging due to the volume and complexity of data required, especially for entities with large lease portfolios.
- The practical expedients and exemptions, such as for low-value and short-term leases, significantly assisted in reducing the implementation burden both during the initial transition and ongoing compliance.
- Transition guidance or instructions issued by the IASB, well before the standard was effective, would have been helpful to assist preparers collect new data, and update systems and processes.
- Several stakeholders noted that specialised software solutions were not available in time for the standard's effective date. As a result, some entities had to adopt a two-phased implementation approach and initially rely on manual workarounds or interim systems before transitioning to purpose-built software once available. A longer lead time may have enabled providers to develop and release appropriate tools prior to the effective date, easing the transition burden.

**Question 6.1: Rent concessions**

- The specific scenario in Spotlight 6.1 is not common amongst those consulted.
- Broadly, it was agreed there is a lack of guidance on distinguishing between a lease modification as defined in IFRS 16 and an extinguishment (or partial extinguishment) of a lease liability accounted for in accordance with IFRS 9.
- We support the IFRS Interpretations Committee's recommendation for the IASB to conduct a narrow-scope standard-setting project to clarify this distinction.

**Question 6.2 & 6.3: Sale and leaseback transactions**

- Stakeholders confirmed it is difficult to determine whether the transfer of an asset by the seller-lessee in a sale and leaseback transaction is a sale in accordance with IFRS 15. Additional illustrative examples or decision trees may assist in determining whether a sale has occurred.
- Restricting the gain or loss an entity recognises in a sale and leaseback transaction was broadly supported.