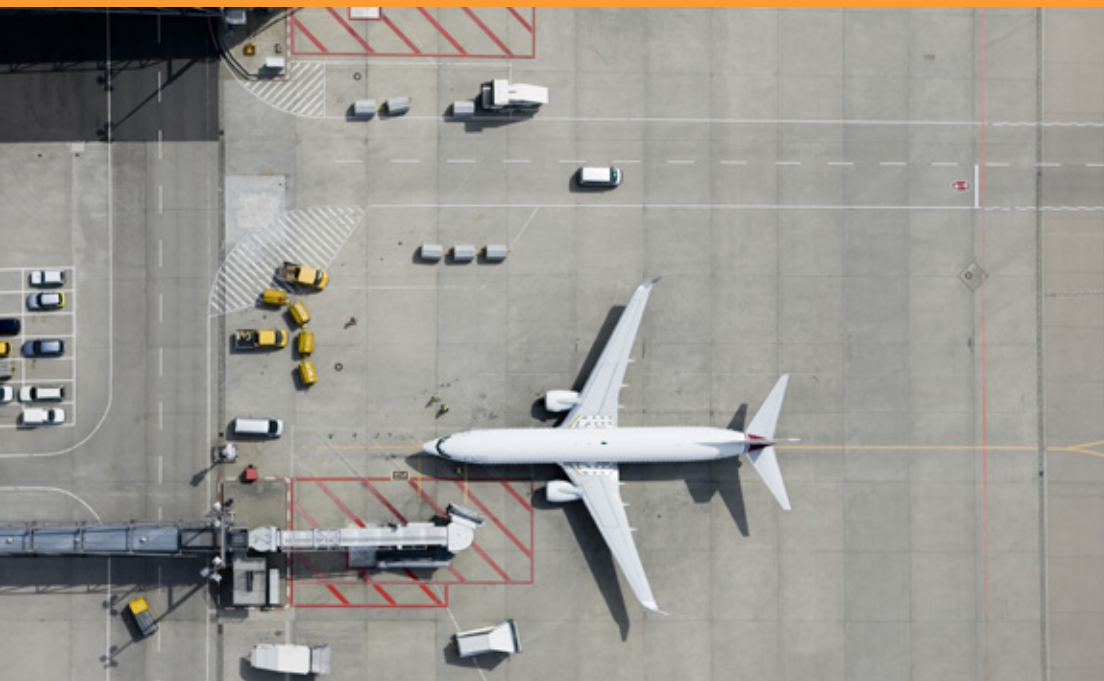


# Guidance on the New Big-3 Standards

## Transportation and Logistics Sector

October 2019



# Introduction

Indonesia is committed to supporting International Financial Reporting Standards (IFRS) as the globally - accepted accounting standards, and to continue with the IFRS convergence process, while further minimising the gap between *Standar Akuntansi Keuangan* (SAK) and IFRS. The decision to elect the convergence approach instead of a full adoption was based on the consideration of the potential interpretation and implementation issues.

Since making the public commitment to support IFRS on 8 December 2008, the *Dewan Standar Akuntansi Keuangan – Institut Akuntansi Indonesia* (DSAK-IAI) has been converging the SAK towards IFRS. The DSAK-IAI is currently working to reduce the gap between SAK and IFRS implementation to one year.

As part of IFRS convergence, DSAK-IAI has adapted IFRS 9 Financial Instruments, IFRS 15 Revenue from Contracts with Customers and IFRS 16 Leases to IFAS by issuing PSAK 71, PSAK 72 and PSAK 73, respectively, in 2017.

This publication reflects the implementation developments and provides guidance on the application of the new standards (PSAK 71, PSAK 72 and PSAK 73) specific to the transportation and logistics industry.

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# PSAK 71

## Financial instruments

*In 2017, DSAK-IAI published the complete version of PSAK 71, 'Financial instruments', which replaces most of the guidance in PSAK 55 'Financial Instruments: Recognition and Measurement'. This includes amended guidance for the classification and measurement of financial assets by introducing a fair value through the other comprehensive income category for certain debt instruments. It also contains a new impairment model, which will result in earlier recognition of losses.*

*No changes were introduced for the classification and measurement of financial liabilities, except for the recognition of changes in the entity's credit risk in other comprehensive income for liabilities designated at fair value through the profit or loss. It also includes the new hedging guidance. These changes are likely to have a significant impact on entities that have significant financial assets.*

*PSAK 71 will be effective for annual periods beginning on or after 1 January 2020.*

# PSAK 71 – Financial Instruments

## Application in the transportation and logistics industry

### Overview

PSAK 71 will affect the transportation and logistics industry with an effective date of 1 January 2020.

Transportation and logistics entities hold a number of financial instruments arising from their core operations (trade and lease receivables), from risk management activities (foreign exchange and interest rate hedges), or cash management and investing activities (debt and equity investments). All financial assets need to be carefully assessed, to understand the classification and impairment implications.

PSAK 71 replaces the majority of PSAK 55; it covers classification, measurement, recognition and derecognition of financial assets and financial liabilities, and impairment of financial assets, and it provides a new hedge accounting model.

“[PSAK 71 – Financial Instruments: Understanding the Basics](#)” provides a comprehensive analysis of the new standards. This publication discusses some of the more significant impacts on entities within the transportation and logistics industry.

### What to do now?

#### Transportation and logistics to-do list

Here is your immediate to-do list for the implementation of PSAK 71 (read the guide for more detail in each area)

1. **Equity investments** will ALL be held at fair value, even if they are unquoted. There is no cost exemption. An entity needs to decide if it will make an irrevocable election to hold any equity instruments at fair value through other comprehensive income. This can be done on an instrument-by-instrument basis. Note that this applies only to those investments in the scope of PSAK 71 that are equity instruments in the meaning of PSAK 50 paragraph 11. Instruments that are puttable or that impose a requirement on an entity to deliver cash on liquidation are not equity instruments in the meaning of PSAK 71.
2. The **impairment model** has changed and, in many cases, this will lead to a higher impairment provision. Entities need to work through the expected credit loss model, ensuring that expectations of forward-looking data are incorporated.
3. Where PSAK 71 is applied, all **hedging documentation** must be re-done to show how the new hedge accounting criteria have been satisfied.

### A snapshot of the financial position of a transportation and logistics company

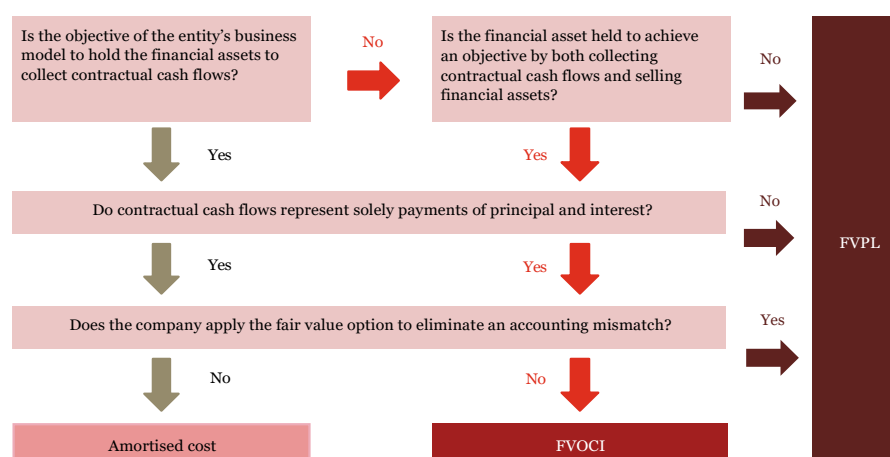
A typical balance sheet of a transportation and logistics company might include the following financial instruments or receivables that fall under PSAK 71:

Current assets	Non-current assets	Current and non-current liabilities
<ul style="list-style-type: none"> <li>Lease and trade receivables</li> <li>Derivative financial assets</li> <li>Amounts due from customers for contract work</li> </ul>	<ul style="list-style-type: none"> <li>Equity investments</li> <li>Loan receivables, including intercompany loans</li> </ul>	<ul style="list-style-type: none"> <li>Borrowings</li> <li>Lease liabilities</li> <li>Derivative financial liabilities</li> </ul>

# Classification and measurement – Business model assessment

## Debt investments (including receivables)

Classification under PSAK 71 of debt investments, is driven by the entity's business model for managing the financial assets and whether the contractual characteristics of the financial assets represent solely payments of principal and interest (SPPI).



## Business model assessment

The classification and measurement of financial assets under PSAK 71 is determined based on two criteria:

- The business model within which the entity holds the asset (business model test), and
- The cash flows arising from the asset (SPPI test – that is, the financial asset gives rise to cash flows that are solely payments of principal and interest).

The business model test will determine the classification of financial assets that pass the SPPI test. PSAK 71 makes a distinction between three different business models:

- **Hold to collect:** The entity holds the financial assets in order to collect the contractual cash flows. The entity measures such assets at amortised cost.
- **Hold to collect and sell:** The entity holds the financial assets for both selling and collecting contractual cash flows. The entity measures such assets at fair value through other comprehensive income (FVOCI).
- **Hold to sell:** The entity holds the financial assets with an intention to sell them before their maturity. The entity measures such assets at fair value through profit or loss (FVPL).

In addition, note that if a financial asset is not held within *hold to collect* or *hold to collect and sell*, it should be measured at FVPL – this is the residual category in PSAK 71. Furthermore, a business model in which an entity manages financial assets, with the objective of realising cash flows through solely the sale of the assets, would also result in a FVPL business model.

# Classification and measurement – Business model assessment (*cont'd*)

## Contractual cash flows analysis

Management should also assess whether the asset's contractual cash flows represent solely payments of principal and interest ('the SPPI condition').

This condition is necessary for the financial asset, or a group of financial assets, to be classified at amortised cost or FVOCI. *Principal* and *interest* are defined as follows:

- **Principal** is the fair value of the financial asset at initial recognition. However, that principal amount might change over the life of the financial asset (for example if there are repayments of principal).
- **Interest** is typically the compensation for the time value of money and credit risk.

However, interest can also include consideration for other basic lending risks (for example liquidity risk) and costs (for example, servicing or administrative costs) associated with holding the financial asset for a period of time, as well as a profit margin.

## Equity investments

Investments in equity instruments (as defined in PSAK 50, from the perspective of the issuer) are always measured at fair value under PSAK 71. The cost exception under PSAK 55 has been removed even for unquoted investments. In limited circumstances, cost may be the appropriate estimate of fair value [PSAK 71 para PP.5.2.3]. Although there are some circumstances in which cost might be representative of fair value, those circumstances would never apply to equity investments held by particular entities, such as financial institutions and investment funds.

Equity instruments that are held for trading are required to be classified at FVTPL, with dividend income recognised in the profit or loss. For all other equities within the scope of PSAK 71, management can make an irrevocable election on initial recognition, on an instrument-by-instrument basis, to present changes in fair value in other comprehensive income (OCI) rather than in the profit or loss. Dividends are recognised in the profit or loss unless they clearly represent a recovery of part of the cost of an investment, in which case they are recognised in OCI. There is no recycling of amounts from OCI to the profit or loss (for example, on the sale of an equity investment) and neither are there any impairment requirements. There are additional disclosure requirements if an entity elects to measure equity instruments at FVOCI. [PSAK 60 paras 11A 11B].

No expected credit loss (ECL) provision is recognised on equity investments (see the section on ECL on debt measurement below.)

# Classification and measurement – Business model assessment (*cont'd*)

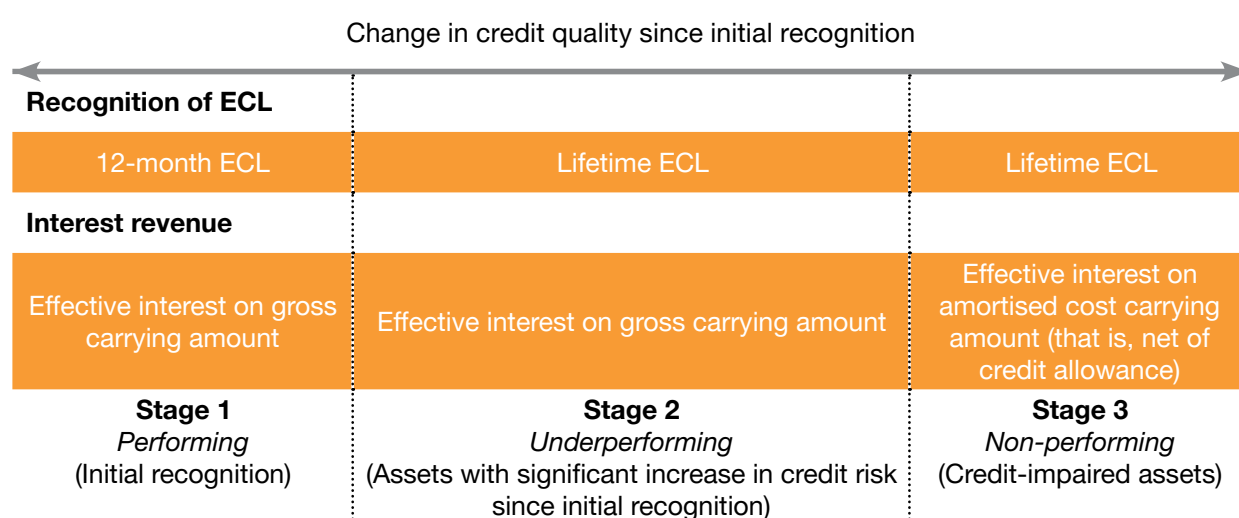
## ***What does this mean for the transportation and logistics industry?***

Trade receivables	<ul style="list-style-type: none"> <li>Trade and lease receivables in a transportation and logistics entity will in principle meet the hold to collect criterion. The payments would normally comprise solely the principal and interest. As such, they would be measured at amortised cost.</li> </ul>
Equity investments	<ul style="list-style-type: none"> <li>Equity instruments are measured at fair value under all circumstances. An entity can make an irrevocable election to measure equity investments at fair value through OCI. There are additional disclosure requirements if this election is used. No ECL is recognised for equity investments.</li> </ul>
Investments in bonds	<ul style="list-style-type: none"> <li>For long-term investments, such as bonds, the entity will need to assess the business model.</li> <li>They might be classified at amortised cost, fair value through other comprehensive income or fair value through profit or loss.</li> </ul>
Derivatives	<ul style="list-style-type: none"> <li>Derivatives remain classified at fair value through profit or loss.</li> </ul>
Contingent consideration	<ul style="list-style-type: none"> <li>Monetary contingent consideration that the acquirer is due to pay or receive is within the scope of PSAK 71. Contingent consideration assets and liabilities are measured at fair value through profit or loss. Any contingent consideration receivable previously classified as AFS will need to be reclassified to FVTPL.</li> </ul>



# Impairment of assets measured at amortised cost

The impairment rules of PSAK 71 introduce a new, forward-looking, ECL impairment model, which will generally result in earlier recognition of losses compared to PSAK 55.



- **Stage 1** includes financial instruments that have not had a significant increase in credit risk since initial recognition or that have low credit risk at the reporting date. For these assets, 12-month ECL is recognised and interest revenue is calculated on the gross carrying amount of the asset.
- **Stage 2** includes financial instruments that have had a significant increase in credit risk since the initial recognition (unless they have low credit risk at the reporting date) but are not credit-impaired. For these assets, lifetime ECL is recognised, and interest revenue is still calculated on the gross carrying amount of the asset.
- **Stage 3** consists of financial assets that are credit-impaired (that is, where one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred). For these assets, lifetime ECL is also recognised, but interest revenue is calculated on the net carrying amount (that is, net of the ECL allowance).

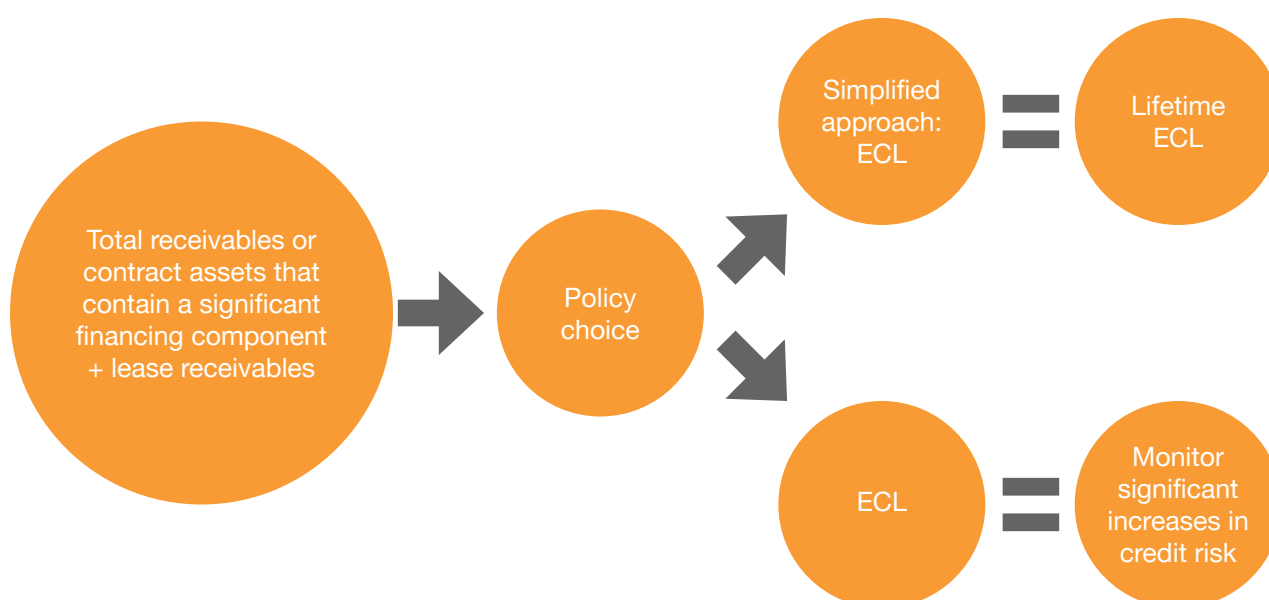
# Impairment – Scope exception for trade receivables: The simplified approach

The general impairment model includes some operational simplifications for trade receivables, contract assets and lease receivables, because they are often held by entities that do not have sophisticated credit risk management systems.

These simplifications eliminate the need to calculate 12-month ECL and to assess when a significant increase in credit risk has occurred.

For trade receivables or contract assets that do not contain a significant financing component, the loss allowance should be measured at initial recognition and throughout the life of the receivable, at an amount equal to lifetime ECL. As a practical expedient, a provision matrix could be used to estimate ECL for these financial instruments.

For trade receivables or contract assets that contain a significant financing component (in accordance with PSAK 72) and lease receivables, an entity has an accounting policy choice: either it can apply the simplified approach (that is, to measure the loss allowance at an amount equal to lifetime ECL at initial recognition and throughout its life), or it can apply the general model. An entity can apply the policy election for trade receivables, contract assets and lease receivables independently of each other, but it must apply the policy choice consistently.



# Impairment – Scope exception for trade receivables: The simplified approach *(cont'd)*

## ***What does this mean for the transportation and logistics industry?***

<b>Short-term trade receivables</b>	<ul style="list-style-type: none"> <li>A trade receivable with a maturity of less than one year will most likely qualify for the simplified model, since it will generally not contain a significant financing component. The entity will recognise lifetime expected credit losses throughout the life of the receivable. Materially higher provisions might not arise for short term trade receivables with customers with a good collection history.</li> </ul>
<b>Long-term trade receivables</b>	<ul style="list-style-type: none"> <li>For trade receivables that contain a significant financing component, for example long-term receivables, the entity will have an accounting policy option.</li> <li>Intercompany loans would normally not qualify for the scope exclusion and the full three-stage model would need to be applied.</li> </ul>
<b>Financial investments in bonds</b>	<ul style="list-style-type: none"> <li>For long term investments, such as bonds, the entity will need to apply the full three-stage model.</li> </ul>

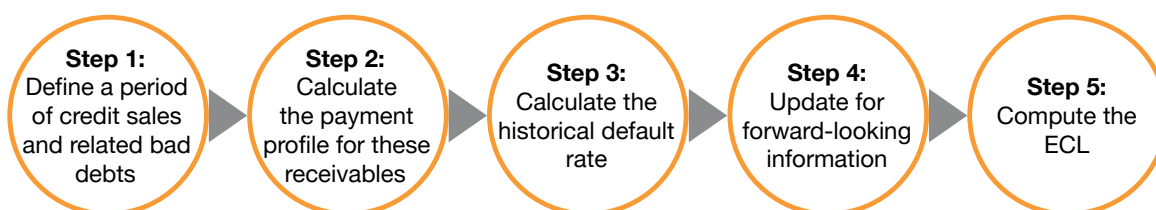


# Provision matrix

PSAK 71 allows an operational simplification whereby companies can use a provisions matrix to determine their ECL under the impairment model.

## How does a provision matrix work?

A provision matrix method uses past and forward information to estimate the probability of default of trade receivables.



### Step 1

The first step, when using a provision matrix, is to define an appropriate period of time to analyse the proportion of trade receivables written off as bad debts. This period should be sufficient to provide useful information. Too short a period might result in information that is not meaningful. Too long might mean that changes in market conditions or the customer base make the analysis no longer valid. In the example, we have selected one year. The overall lease receivables were CU10,000 and the receivables ultimately written off were CU300 in that period.

Total sales	CU10,000
Bad debts written off out of these sales	CU300

### Step 2

In step 2, we determine the amount of receivables outstanding at the end of each time bucket, up until the point at which the bad debt is written off. The ageing profile calculated in this step is critical for the next step, when calculating default rate percentages.

Total sales (CU)	10,000	Total paid	Ageing profile of sales (step 3)
Paid in 30 days	(2,000)	(2,000)	8,000
Paid between 30 and 60 days	(3,500)	(5,500)	4,500
Paid between 60 and 90 days	(3,000)	(8,500)	1,500
Paid after 90 days	(1,200)	(9,700)	300 (written off)

# Provision matrix (cont'd)

## Step 3

In this step, the entity calculates the historical default rate percentage. The default rate for each bucket is the quotient of the default receivables in each bucket over the outstanding credit sales for that period. For example, in the above information, CU300 out of the CU10,000 lease income for the period, was written off.

### Current sales – historical rate of default

Since all of the receivables relating to the sales made and those written off were current at some stage, it can be derived that for all current amounts, the entity might incur an eventual loss of CU300. The default rate would therefore be 3% (CU300/CU10,000) = For all current amounts.

### Sales payments outstanding after 30 days

An amount of CU8,000 was not paid within 30 days. An eventual loss of CU300 was a result of these outstanding receivables. Therefore, the default rate for amounts outstanding after 30 days would be 3.75%.

### Remaining buckets

The same calculation is then performed for 60 days and after 90 days. Although the amount outstanding reduces for each subsequent period, the eventual loss of CU300 was, at some stage, part of the population within each of the time buckets, and so it is applied consistently in the calculation of each of the time bucket default rates.

The historical default rates are determined as follows:

	Current sales	Sales payments outstanding after 30 days	Sales payments outstanding after 60 days	Sales payments outstanding after 90 days
<b>Ageing profile of sales(1)</b>	10,000	8,000	4,500	1,500
<b>Loss: (2)</b>	300	300	300	300
<b>Default rate: (2)/(1) (%)</b>	<b>3</b>	<b>3.75</b>	<b>6.67</b>	<b>20</b>

# Provision matrix (cont'd)

## Step 4

PSAK 71 is an ECL model, so consideration should also be given to forward-looking information.

Such forward-looking information would include:

- Changes in economic, regulatory, technological and environmental factors (such as industry outlook, GDP, employments and politics);
- External market indicators; and
- Customer base.

For example, the entity concludes that the defaulted receivables should be adjusted by CU100 to CU400 as a result of economic changes affecting the industry. The entity also concludes that the payment profile and amount of sales are the same. Each entity should make its own assumption of forward-looking information. The provision matrix should be updated accordingly.

The default rates are then recalculated for the various time buckets, based on the expected future losses.

	Current sales	Sales payments outstanding after 30 days	Sales payments outstanding after 60 days	Sales payments outstanding after 90 days
<b>Ageing profile of sales (1)</b>	10,000	8,000	4,500	1,500
<b>Loss: (2)</b>	400	400	400	400
<b>Default rate: (2)/(1) (%)</b>	<b>4</b>	<b>5</b>	<b>8.9</b>	<b>27</b>

## Step 5

Finally, take the default rates from step 4 and apply them to the actual receivables, at the period end, for each of the time buckets. There is a credit loss of CU12 in the example illustrated.

	Total	Current (0-30 days)	30-60 days	60-90 days	After 90 days
<b>Trade receivable balances at year end: (1)</b>	140	50	40	30	20
<b>Default rate: (2) (%)</b>		4	5	8.9	27
<b>Expected credit loss: (1)*(2)</b>	<b>CU 12</b>	<b>CU 2</b>	<b>CU 2</b>	<b>CU 3</b>	<b>CU 5</b>

# Intra-group loans

The scope for the accounting of intra-group loans and loans to joint ventures and associates (“funding”) is not expected to change from the introduction of PSAK 71. Funding, previously within the scope of PSAK 55, ‘Financial instruments: Recognition and measurement’ will also be within the scope of PSAK 71.

The impact of PSAK 71 on intra-group funding might often be dismissed, because it is eliminated on consolidation. However, the impact in separate financial statements could be significant.

## ***Impairment of intra-group loans***

Intra-group loans and loans to joint ventures and associates do not qualify for the simplifications in PSAK 71. The full impairment model needs to be applied, so 12-month ECL will be recorded on the day when funding is advanced.

Subsequently, if there is a significant increase in credit risk (for example, if the subsidiary’s, joint venture’s or associate’s trading performance declines), the impairment loss will be increased to a lifetime expected credit loss.

### **What does this mean for Transportation and Logistics Sector?**

Intra-group funding and loans to joint ventures and associates with written terms would generally fall within the scope of PSAK 71. All requirements of PSAK 71 will therefore apply, including impairment.

Under PSAK 71, entities will be required to ensure that they implement adequate processes for collection of the information needed for impairment, for example:

- Indicators for a significant increase in credit risk must be developed.
- Forward-looking information, as well as past events, must be incorporated.
- The contractual period over which to assess impairment may not be clear.

# Intra-group loans *(cont'd)*

## **Cash advanced might not be at fair value**

Intra-group loans within the scope of PSAK 71 and loans to joint ventures and associates are required to be measured at fair value on initial recognition. These loans may sometimes be either interest-free or provided at below-market interest rates. In those cases, the amount lent is, therefore, not fair value.

### What does this mean for Transportation and Logistics Sector?

Loans at below market or nil interest rate are not advanced at fair value. Practically, this means that the cash advanced will not be the receivable recorded. Instead, the receivable will be recorded at a lower amount, to take into account the impact of discounting at a market interest rate.

A day one difference arises between the cash advanced and the recorded receivable. If the loan is advanced from a parent entity to its subsidiary, this difference is added to the cost of investment in the subsidiary because it is the nature of the relationship that gives rise to the off-market/interest-free loan. For loans to joint ventures and associates, this difference would also generally be added to the cost of investment as the relationship between the investor and the joint venture or associate is often the reason for the loan being off-market/interest-free.





# Hedging

*Hedging* is a risk management activity. More specifically, it is the process of using a financial instrument (usually a derivative) to mitigate all or some of the risk of a hedged item. *Hedge accounting* changes the timing of recognition of gains and losses on either the hedged item or the hedging instrument so that both are recognised in profit or loss in the same accounting period in order to record the economic substance of the combination of the hedged item and hedging instrument.



For a transaction to qualify for hedge accounting PSAK 71 includes the following requirements:

- An entity should formally designate and document the hedging relationship at the inception of the hedge. PSAK 71 requires additional documentation to show sources of ineffectiveness and how the hedge ratio is determined.
- There must be an economic relationship between the hedging instrument and the hedged item.
- Credit risk should not dominate value changes.
- The hedge ratio should be aligned with the economic hedging strategy (risk management strategy) of the entity.

## What does this mean for Transportation and Logistics Sector?

Transportation and logistics entities mostly hedge interest rate risks and, where relevant, foreign exchange currency risks, by entering into interest rate and foreign currency swaps, forwards and options.

Entities will need to update their hedging documentation and ensure that a qualitative assessment of effectiveness for each hedging relationship is performed.

There is no longer an 80-125% effectiveness bright line effectiveness test. As such, a retrospective effectiveness test is no longer required to prove that the effectiveness was between 80 and 125%. However, all ineffectiveness should still be recorded in the income statement.

PSAK 71 gives companies a free choice over whether to adopt its new hedge accounting requirements when the remainder of PSAK 71 becomes mandatory in 2020. A company must either move all of its hedge accounting to PSAK 71, or it must continue to apply PSAK 55 to all of its hedges.

However, all entities have to apply PSAK 71's new disclosure requirements – including the new disclosures around hedge accounting.

# Financial liabilities

## Debt modifications

Transportation and logistics entities might restructure borrowings with banks to adjust interest rates and maturity profiles and hence modify their debt.

When a financial liability measured at amortised cost is modified without this resulting in derecognition, a difference arises between the original contractual cash flows and the modified cash flows discounted at the original effective interest rate (the 'gain/loss').

Entities were permitted, although not required, to recognise the gain/loss in the income statement at the date of modification of a financial liability under PSAK 55. Many entities deferred the gain/loss under PSAK 55 over the remaining term of the modified liability by recalculating the effective interest rate.

This will change on transition to PSAK 71 because the accounting will change. When a PSAK 71 financial liability measured at amortised cost is modified without this resulting in derecognition, the gain/loss should be recognised in the profit or loss. Entities are no longer able to defer the gain/loss.

The changes in accounting for modifications of financial liabilities will impact all preparers, particularly entities which were applying different policies for recognising gains and losses under PSAK 55.

Whilst entities were not required to change their PSAK 55 accounting policy, the impact on transition to PSAK 71 should be considered. PSAK 71 is required to be applied retrospectively, so modification gains and losses arising from financial liabilities that are still recognised at the date of initial application (for example, 1 January 2020 for calendar year end companies) would need to be recalculated and adjusted through opening retained earnings on transition. This will affect the effective interest rate and, therefore, the finance cost for the remaining life of the liability.









# PSAK 72

## Revenue from contracts with customers

*In 2017, the DSAK-IAI published the long-awaited standard on revenue recognition. Almost all entities will be affected to some extent by the change, although the effect will vary depending on the industry and current accounting practices. However, almost all entities will see a significant increase in required disclosures.*

# Implementation in the transportation and logistics sector

## Overview

The transportation and logistics industry includes companies associated with shipping, railways, airlines, trucking and logistics, and cruise lines. Customers generally pay a fee for the movement of cargo or passengers between two or more specified points. Customer incentives are limited, and primarily arise from volume discounts, or airlines' customer loyalty programmes, in which awards are earned based on mileage flown and can be redeemed for a variety of products or services.

This publication discusses the areas in which the final revenue standard (PSAK 72, Revenue from Contracts with Customers) is expected to have the greatest impact on companies in the transportation and logistics industry, broken down by step of the model. The content in this publication should be considered together with our [“PSAK 72 – A Comprehensive Look at The New Revenue Model”](#).

### Scope

The new revenue standard applies to all contracts with customers except for:

- Lease contracts
- Insurance contracts
- Certain contractual rights or obligations within the scope of other standards, including financial instrument contracts
- Certain guarantees (other than product warranties) within the scope of other standards
- Nonmonetary exchanges (between companies in the same line of business) to facilitate a sale to another party

Some contracts within the transportation and logistics industry may include components that are in the scope of the revenue standard and components that are in the scope of other standards (for example, a lease contract that also includes maintenance or other services). The new standard states that if a contract is partially within the scope of another standard, a company should apply any separation and/or measurement guidance in the other standard first. Otherwise, the principles in the revenue standard should be applied to separate and/or initially measure the component(s) of the contract.

The determination of whether an arrangement contains a lease might have significant accounting implications. Careful consideration of the relevant standard is required before applying the revenue standard to a contract. Contracts that involve providing or using fixed assets (for example, vessel time charters) might contain a lease. The board issued a new leasing standard that amends the guidance about what constitutes a lease. Management will need to carefully assess which arrangements or components of arrangements fall outside the scope of lease accounting and should be treated as revenue contracts.

The following discussion relates only to contracts and/or components of contracts that are within the scope of the revenue standard.



# 1. Identify the contract

A contract can be written, orally discussed, or implied by a company's customary business practices. Generally, any agreement with a customer that creates legally enforceable rights and obligations meets the definition of a contract. Legal enforceability depends on the interpretation of the law and could vary across legal jurisdictions where the rights of the parties are not enforced in the same way.

Transportation and logistics companies should consider any history of entering into amendments or side agreements to a contract that either changes the terms of, or adds to, the rights and obligations of a contract. These can be verbal or written, and could include cancellation, termination or other provisions. They could also provide customers with options or discounts, or change the substance of the arrangement. All of these have implications for revenue recognition. Therefore, understanding the entire contract, including any amendments, is important to the accounting conclusion.

As part of identifying the contract, companies are required to assess whether collection of the consideration is probable, which is generally interpreted as a greater than 50% likelihood in PSAK. This assessment is made after considering any price concessions expected to be provided to the customer. In other words, price concessions are variable consideration (which affects the transaction price), rather than a factor to consider in assessing collectability.

New guidance	Current PSAK
<p>A company accounts for a contract with a customer when:</p> <ul style="list-style-type: none"> <li>Contract has been approved and the parties are committed</li> <li>Each party's rights are identified</li> <li>Payment terms are defined</li> <li>Contract has commercial substance</li> <li>Collection is probable.</li> </ul> <p>In evaluating whether an amount is collectible, management should consider whether a customer has the ability and intention to pay the promised consideration when it is due. The amount of consideration to which the company will be entitled may be less than the price stated in the contract if the consideration is variable. For example, the company may offer the customer a price concession.</p> <p>When collectability of the transaction price is not probable at inception, management should continue to assess the contract each reporting period to determine if collectability is probable. If collectability of the transaction price is not probable and the company receives consideration from the customer, it should recognise the consideration received as revenue only when one of the following events has occurred:</p> <ul style="list-style-type: none"> <li>There are no remaining obligations to transfer goods or services to the customer, and substantially all of the consideration has been received and is non-refundable.</li> <li>The contract has been terminated, and the consideration received is non-refundable.</li> </ul>	<p>A company is required to consider the underlying substance and economics of an arrangement, not merely its legal form.</p> <p>Management must establish that it is probable that economic benefits will flow before revenue can be recognised.</p>



# 1. Identify the contract *(cont'd)*

## **Potential impact:**

The assessment of whether a contract with a customer exists under the new revenue guidance requires considering whether an agreement between two parties (either written, oral, or implied) creates legally enforceable rights and obligations between them.

The purpose of the collectability assessment under the new guidance is to determine whether there is a substantive contract between the company and the customer. This differs from current guidance in which collectability is a constraint on revenue recognition.

The new guidance also eliminates the cash-basis method of revenue recognition that is often applied today if collectability is not reasonably probable. Any cash received is recognised as a contract liability until either collectability of the transaction price is probable or one of the criteria for recognition is met. This could result in revenue being recorded later than under current guidance in some situations.





## 2. Identify performance obligations

Many transportation and logistics companies provide multiple products or services to their customers as part of a single arrangement. Management must identify the separate performance obligations in an arrangement based on the terms of the contract and the company's customary business practices. A bundle of goods and services might be accounted for as a single performance obligation in certain fact patterns.

New guidance	Current PSAK
<p>A performance obligation is a promise in a contract to transfer to a customer either:</p> <ul style="list-style-type: none"> <li>• A good or service (or a bundle of goods or services) that is distinct; or</li> <li>• A series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer.</li> </ul> <p>A good or service is distinct if both of the following criteria are met:</p> <ul style="list-style-type: none"> <li>• The customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e., it is capable of being distinct).</li> <li>• The good or service is separately identifiable from other goods or services in the contract (i.e., it is distinct in the context of the contract).</li> </ul> <p>Factors that indicate that two or more promises to transfer goods or services to a customer are not separately identifiable include (but are not limited to):</p> <ul style="list-style-type: none"> <li>• The company provides a significant service of integrating the goods or services with other goods or services promised in the contract.</li> <li>• One or more of the goods or services significantly modifies or customises the other goods or services.</li> <li>• The goods or services are highly interdependent or highly interrelated.</li> </ul> <p>PSAK reporters should consider the application of materiality concepts when identifying performance obligations.</p>	<p>The revenue recognition criteria are usually applied separately to each transaction. In certain circumstances, it might be necessary to separate a transaction into identifiable components to reflect the substance of the transaction.</p> <p>Two or more transactions might need to be grouped together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole.</p>





## 2. Identify performance obligations *(cont'd)*

### **Potential impact:**

Assessing whether goods and services are capable of being distinct is similar to determining if deliverables are separate components under existing PSAKs. Under the new guidance, management will assess if the customer can benefit from the good or service with “resources that are readily available to the customer,” which could be a good or service sold separately by the company or another company, or a good or service the customer has already obtained.

Companies will need to determine whether the nature of the promise, within the context of the contract, is to transfer each of those goods or services individually or, instead, to transfer a combined item to which the promised goods or services are inputs. This will be a new assessment for companies as compared to today.

### **Change fees**

Change fees are common in the airline industry. The current industry practice is mixed with many companies treating a fee for exchanging a ticket as a separate transaction, while others may view the transaction as the result of the customer paying the lowest cost to obtain the new travel reservation (that is, paying the change fee instead of the price of a new ticket). Using the latter approach, the change fee is deferred and recognised when the travel occurs.

Under the new standard, distinct goods or services are not transferred to the customer when a change fee is paid, so they do not represent a separate performance obligation. The only performance obligation in the contract (setting aside any loyalty points) is the flight, so change fees will be deferred and recognised when the flight occurs.





### 3. Determine transaction price

The transaction price is the consideration to which the company expects to be entitled in exchange for goods or services. Determining the transaction price may be simple when the contract price is fixed and paid at the time services are provided. However, it may require more judgment if the consideration contains an element of variable or contingent consideration. Common forms of variable consideration in the transportation and logistics industry include discounts, volume rebates and performance bonuses.

New guidance	Current PSAK
<p>The transaction price is the consideration that the entity expects to be entitled to in exchange for transferring promised goods or services to the customer. It includes fixed amounts and an estimate of variable consideration based on either the expected value or most likely amount approach (whichever is most predictive).</p> <p>Variable consideration (e.g., discounts and rebates) included in the transaction price is subject to a constraint. The estimated amount of variable consideration is included in the transaction price up to an amount that is highly probable of not resulting in a significant reversal of cumulative revenue in the future.</p> <p>Management will need to determine if there is a portion of the variable consideration (that is, a minimum amount) that would not result in a significant revenue reversal and include that amount in the transaction price. Determining the amount of variable consideration to record, including any minimum amounts, requires judgment.</p>	<p>Revenue related to variable consideration is recognised when it is probable that the economic benefits will flow to the entity and the amount is reliably measurable, assuming all other revenue recognition criteria are met.</p> <p>Volume rebate payments are typically systematically accrued based on rebates expected to be taken. The rebate is recognised as a reduction of revenue based on the best estimate of the amounts potentially due to the customer. If the rebate cannot be reliably estimated, revenue is recognised at an amount no greater than the minimum consideration that the seller will retain.</p>

#### **Potential impact:**

The evaluation of variable consideration will require judgment in many cases. Some companies will need to recognise revenue before all contingencies are resolved, which might be earlier than under the current practice. Management might need to put into place new processes to monitor estimates on an ongoing basis as more experience is obtained.



## 3. Determine transaction price (cont'd)

New guidance	Current PSAK
<p>The revenue standard provides factors to consider when assessing whether variable consideration should be constrained.</p> <p>Management should reassess the estimate of the variable consideration each reporting period. Customers may not exercise all of their contractual rights related to a contract, such as rebates and other incentive offers. These unexercised rights are often referred to as a breakage. Management should adjust for changes in expectations when updating the estimated amount of consideration to which an entity expects to be entitled.</p> <p>Time value of money</p> <p>A company needs to adjust the amount of the promised consideration to reflect the time value of money if the contract includes a significant financing component. Factors to consider when determining whether a contract has a significant financing component include, but are not limited to:</p> <ul style="list-style-type: none"> <li>• The expected length of time between when the company transfers the promised goods or services and when the customer pays for them.</li> <li>• Whether the amount of consideration would differ substantially if the customer paid in cash promptly in accordance with typical credit terms in the industry and jurisdiction, and</li> <li>• The interest rate in the contract and prevailing interest rates in the relevant market.</li> </ul> <p>A significant financing component does not exist if the timing of delivery is at the customer's discretion (for example, in the case of customer loyalty points) or the difference between the promised consideration and the cash selling price arises for reasons other than financing.</p> <p>As a practical expedient, a company need not assess whether a contract has a significant financing component if it expects at contract inception that the period between payment and the transfer of services will be one year or less.</p> <p>If a contract with a customer contains a significant financing component, the company should measure the amount of the financing by using a discount rate that reflects a separate financing transaction between the company and its customer, and that factors in the credit risk.</p>	<p>Discounting revenue to the present value is required when the arrangement effectively constitutes a financing transaction. The imputed rate of interest is the more determinable of either:</p> <ol style="list-style-type: none"> <li>1. the prevailing rate on a similar instrument of an issuer with a similar credit rating, or</li> <li>2. the rate that discounts the instrument to the current cash sales price of the goods or services.</li> </ol>



## 3. Determine transaction price (cont'd)

### **Potential impact:**

The new guidance related to a significant financing component differs from the current guidance on applying the time value of money. That said, we do not expect a significant change to the current practice for most transportation and logistics companies in connection with the time value of money because payment terms do not often extend over more than one year from the time of the contract performance.

#### **Example 3(a) – Demurrage claims in the transaction price**

**Facts:** A shipping company enters into a voyage charter contract with a customer to transport goods from point A to point B. The shipping company experiences delays in loading and unloading the cargo (referred to as demurrage), which are not the responsibility of the shipper. The additional amount to be paid to the shipping company is calculated in accordance with the terms of the contract. Demurrage claims are often negotiated, resulting in adjustments to the contract price, and can take a long time to resolve.

**Question:** When should the shipping company include the demurrage claim in the transaction price?

**Analysis:** Amounts for demurrage claims should not be included in the transaction price assessment prior to the occurrence of the delay as the company would not be entitled to claims prior to that point.

The amount of demurrage claims might be difficult to estimate and will vary depending on the counterparty and the type of delay. The shipping company may be familiar with the issues and have experience in successfully negotiating the claims. When a delay occurs, the company should estimate the expected amount of the claim to be received and determine whether it is highly probable that there will not be a significant reversal of revenue in a future period. Although some or all of the claim may not meet this threshold, the company is required to include in the transaction price any portion of the claim that meets the highly probable threshold. The time taken to resolve claims or the external factors involved are not factors that would allow the company to avoid including in the transaction price a minimum amount that meets the threshold.

The company should reassess its estimate of transaction price each reporting period.



## 3. Determine transaction price (cont'd)

### Example 3(b) – Volume rebates

**Facts:** A railway company enters into a contract to ship goods from point A to point B for \$1,000. The customer earns a rebate of \$100 for each load if the customer ships at least 10,000 loads annually. Based on past experience, management believes there is a 50% likelihood that the customer will ship 10,000 loads and earn the rebate of \$100 per load.

**Question:** How should the railway company determine the transaction price?

**Analysis:** The transaction price is \$900 per load, which reflects the amount to which the company expects to be entitled based on its estimate of loads to be shipped.

There are only two possible outcomes regarding the variable consideration (e.g., the rebate). The railway company will be entitled to either \$0 or an additional \$100 per load. It concluded that it would not be highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur if the incremental \$100 per load were included in the estimate of the transaction price at inception.

Any amounts collected in excess of \$900 per load (that is, the additional \$100 per load prior to earning the rebate) would be recorded as a liability. These estimates should be monitored and adjusted, as necessary, using a cumulative catch-up approach. For instance, should circumstances change and it becomes highly probable that the customer will not be entitled to the rebate, the extra \$100 per load would be included in the transaction price for the loads previously shipped at that point.

### Example 3(c) – Extended payment terms

**Facts:** A tour operator sells a refundable tour with a limited number of spaces to a customer with a deposit due at the time of booking, which is 13 months before the tour. The ticket price is \$1,000, with \$100 paid at booking and the remainder due 90 days in advance of the tour. Alternatively, customers have the option to pay 100% at the time of booking; however, there is no discount for paying in full at the time of booking.

**Question:** How should the tour operator measure the transaction price of this contract?

**Analysis:** The tour operator should consider the purpose of the payment terms to determine whether there is a significant financing component in the contract. In this example, the tour operator might conclude that the amount charged at booking is not charged for the primary purpose of obtaining financing, but to reserve and hold the booking and space for the customer and to ensure the customer is committed to the reservation. The tour operator would therefore consider the \$1,000 to be the transaction price, and not account for a financing component.



## 4. Allocate transaction price

Transportation and logistics companies may provide multiple goods or services to their customers as part of a single arrangement. Under the new standards, they will need to allocate the transaction price to the separate performance obligations in one contract based on the relative standalone selling price of each separate performance obligation.

### **Customer loyalty programmes – frequent flyer programmes**

Transportation and logistics companies often grant award credits (often called “points” or “miles”) as part of the sales transactions that can be redeemed for goods and services supplied either by the company itself or by other companies. The most common customer loyalty programmes in the industry are the frequent flyer programmes offered by airlines.

New guidance	Current PSAK
<p><b>Customer options that provide a material right</b></p> <p>A material right is a promise embedded in a current contract that should be accounted for as a separate performance obligation. If the option provides a material right to the customer, the customer, in effect, pays the entity in advance for future goods or services, and the entity recognises revenue when those future goods or services are transferred or when the option expires.</p> <p><b>Loyalty programmes</b></p> <p>Credits issued under customer loyalty programmes are separate performance obligations if they provide the customer with a material right that the customer would not receive without buying the initial product or service (for example, the original flight).</p> <p>The transaction price is allocated between the initial purchase and the awarded credits based on the actual or estimated standalone selling price of each performance obligation.</p> <p>The portion of the transaction price allocated to the award credits is not recognised as revenue until the credits are redeemed or expire.</p> <p>The standalone selling price of the award credits is not usually directly observable and will therefore need to be estimated. The estimate should reflect the discount achieved by customers when spending award credits, adjusted for the likelihood that the credits will be forfeited (breakage).</p> <p>The airline recognises revenue from the award credits on a gross basis when the customer redeems them for goods or services that the airline provides.</p>	<p>Customer loyalty programmes are accounted for as multiple-element arrangements. Consideration is allocated to the award credits based on their fair values, typically using the residual method, although the guidance also permits relative fair values. This amount is deferred and recognised as revenue when the award credits are redeemed or expire.</p> <p>The fair value of the award credits is adjusted for discounts available to other buyers, absent entering into the initial purchase transaction and for expected forfeitures (breakage).</p> <p>Management needs to determine whether the company is acting as a principal or an agent in the arrangement. A company may be acting as an agent if it issues award credits that are transferred to and redeemed by other companies.</p> <p>Revenue is recognised net of payments made to others to redeem award credits if the company is acting as an agent.</p>



## 4. Allocate transaction price (cont'd)

New guidance	Current PSAK
<p>An airline that operates a programme in which points can be redeemed with a third party needs to consider whether it is the principal or an agent in the arrangement. This requires management to first consider the nature of its performance obligation.</p> <p>The company should recognise revenue for the net fee or commission retained in the exchange if it is an agent in the arrangement.</p> <p><b>Tier status</b></p> <p>Customers can often obtain tier status on airlines due to frequent flyer programmes which allow them to receive certain benefits (e.g., free checked baggage, potential upgrades, expedited boarding rights, etc.). Airlines may also grant tier status to individuals who can demonstrate they are frequent travellers (e.g., demonstrate status on other airlines). Tier status will give rise to a separate performance obligation if the status benefits provide a material right to the customer.</p> <p>In evaluating whether a material right exists, a company should consider the extent to which status benefits would also be available to individuals who have not achieved tier status with it.</p>	<p>Airlines evaluate the value of status, if material, to determine whether it is a separate element for revenue considerations.</p>

### Potential impact:

The new guidance will require consideration to be allocated on a relative standalone selling price basis, which could have a different result than the residual approach sometimes applied today. Some companies might allocate less consideration to the award credits under the new guidance as a result.

Revenue allocated to award credits is recognised when the credits are redeemed or expire. Management will update its expectation of credits that will be redeemed each period to determine recognition of deferred amounts.

Entities that currently only recognise revenue from points when they expire will likely recognise revenue earlier (based on estimated redemptions) under the new standard.





## 4. Allocate transaction price (cont'd)

### Example 4(a) – Frequent flier programme

**Facts:** Airline A has a frequent flyer customer loyalty programme that rewards customers with award credits based on amounts paid for flights. A customer purchases a ticket for \$500 (the standalone selling price) and earns 2,500 award credits based on the price of the ticket. Award credits are redeemable at a rate of 50 award credits for \$1 (\$0.02 per credit). The award credits may only be redeemed for flights with Airline A.

**Question:** How should the consideration be allocated between the award credits and the ticket (ignoring breakage)?

**Analysis:** The transaction price of \$500 should be allocated between the ticket and award credits based on the relative standalone selling prices of \$500 for the ticket and \$50 (2,500 points x \$0.02) for the award credits as follows:

Ticket                      \$455 ( $\$500 \times \$500/\$550$ )

Award credits      \$ 45 ( $\$500 \times \$50/\$550$ )

Airline A would recognise revenue of \$455 when the flight occurs. It would defer revenue of \$45 and recognise it upon redemption or expiration of the award credits.

### Example 4(b) – Frequent flier programme and breakage

**Facts:** Assume the same facts as in Example 4(a), except that Airline A expects redemption of 80% of award credits earned (that is, 20% breakage) based on the history of redemptions. The airline estimates a standalone selling price for the credits of \$0.016 ( $\$0.02 \times 80\%$ ) based on the likelihood of redemption.

**Question:** How should the consideration be allocated between the award credits and the ticket (considering breakage)?

**Analysis:** The transaction price of \$500 should be allocated between the ticket and award credits based on the relative standalone selling prices of \$500 for the ticket and \$40 (2,500 points x \$0.016) for the award credits as follows:

Ticket                      \$463 ( $\$500 \times \$500/\$540$ )

Award credits      \$ 37 ( $\$500 \times \$40/\$540$ )

Airline A would recognise revenue of \$463 when the flight occurs. It would defer revenue of \$37 and recognise it when the 2,000 points (2,500 points x 80%) that are expected to be redeemed are redeemed by the customer or when the points expire.





## 4. Allocate transaction price (cont'd)

### Example 4(c) – Frequent flier programme - reassessing estimate of breakage

**Facts:** Assume the same facts as in Example 4(b). At the end of the first year, 1,000 points were redeemed out of the total 2,000 points expected to be redeemed, resulting in recognition of \$18.50 (50% of the \$37 deferred). In year 2, Airline A now expects redemption of 90% of award credits earned (that is, a total of 2,250 points). During the year, 500 points are redeemed.

**Question:** How much revenue should be recorded?

**Analysis:** Airline A should update the estimate of the number of awards that will be redeemed each reporting period and recognise revenue on a cumulative catch-up basis. Airline A should recognise revenue of \$6 in year 2, calculated as:  $[(1,500 \text{ points redeemed} / 2,250 \text{ points expected to be redeemed}) \times \$37 \text{ initial allocation}] - \$18.50 \text{ recognised in the first year}$ .





## 5. Recognise revenue

Transportation or freight services are generally provided over a period of time ranging from one day to multiple years. The new standards require that revenue be recognised, as a company satisfies a performance obligation by transferring control of a good or service. A performance obligation can be satisfied over time or at a point in time.

New guidance	Current PSAK
<p><b>Transportation revenue</b></p> <p>A performance obligation is satisfied over time if any one of the following criteria is met:</p> <ul style="list-style-type: none"> <li>• The customer simultaneously receives and consumes the benefits as the company performs</li> <li>• The company's performance creates or enhances an asset that the customer controls as the asset is created or enhanced</li> <li>• The company's performance does not create an asset with an alternative use, and the company has an enforceable right to payment for the performance completed to date.</li> </ul> <p>A company should recognise revenue over time only if the company can reasonably measure its progress toward complete satisfaction of the performance obligation.</p> <p>If a performance obligation is not satisfied over time, a company satisfies the performance obligation at a point in time. The standard provides indicators to determine the point in time at which control transfers.</p> <p><b>Transportation costs</b></p> <p>Costs to obtain or fulfil a contract are in the scope of the revenue guidance only if they are not addressed by other standards. Costs in the scope of other standards that are required to be expensed by those standards cannot be recognised as an asset under the revenue guidance.</p> <p>A company should recognise an asset for the incremental costs of obtaining a contract with the customer if the company expects to recover those costs. Incremental costs of obtaining a contract are those costs that the company would not have incurred if the contract had not been obtained (for example, sales commissions).</p> <p>A company should recognise an asset under the revenue guidance for costs to fulfil a contract when all of the following criteria are met:</p> <ul style="list-style-type: none"> <li>• The costs relate directly to a contract.</li> <li>• The costs generate or enhance resources of the company that will be used in satisfying performance obligations in the future.</li> <li>• The costs are expected to be recovered.</li> </ul> <p>Capitalised costs are amortised consistently with the pattern of transfer of control of the goods or services to which the asset relates. A company may elect, as a practical expedient, to expense the costs to obtain a contract as incurred when the expected amortisation period is one year or less.</p> <p>An impairment loss is recognised to the extent that the carrying amount of the capitalised asset exceeds the net amount of consideration to which the company expects to be entitled in exchange for the services to which the asset relates, less the remaining costs that relate directly to providing these services.</p>	<p>Revenue is recognised for service transactions, such as freight services, based on the stage of completion of the transaction. Costs are recognised as incurred.</p>



## 5. Recognise revenue (cont'd)

### Potential impact:

Transportation services will likely meet the criteria for revenue recognition over time as the customer simultaneously receives and consumes the benefit as the entity performs. The boards observed that the customer benefits from the entity's performance as it occurs if another entity would not need to substantially reperform the entity's performance (for example, distance already travelled) to date. An entity should disregard any contractual or practical limitations when it assesses whether the customer simultaneously receives and consumes the benefits and whether another entity would need to substantially reperform the performance completed to date. For example, the assessment would not consider contractual provisions that restrict an entity from transferring its obligations to another entity.

Freight fulfilment costs will continue to be expensed as incurred unless (1) they can be capitalised under another standard or (2) they relate directly to a contract or an anticipated contract, generate or enhance resources of the company that will be used in satisfying performance obligations in the future, and are expected to be recovered.

#### Example 5(a) – Transportation contract revenue

**Facts:** A shipping company enters into a contract with a customer to transport goods from point A to point B. The customer has an unconditional obligation to pay for the service when the service has been completed, which is when the goods reach point B.

**Question:** When should the shipping company recognise revenue from this contract?

**Analysis:** These types of contracts will typically meet the criteria for revenue recognition over time.

If the shipping company transports the goods halfway to the destination, another transportation company could fulfil the remaining obligation to the customer without having to reperform the services provided to date. The obligation to provide transportation services is therefore satisfied over time, and revenue should be recognised over the period of performance (generally the period from when transport of the goods begins from point A through delivery to point B).

#### Example 5(b) – Costs in inventory management services contract

**Facts:** A logistics company enters into a contract to perform inventory management services for its customer over a two-year period. Mobilisation costs are incurred in preparing to service the customer in accordance with the contract. These costs include leasehold improvements on warehouse space and internally developed software related to software enhancements and customisation required to perform under the contract.

**Question:** How should the logistics company account for these costs?

**Analysis:** The activities giving rise to these costs do not transfer a goods or service to the customer. Management will therefore need to evaluate if the costs incurred to fulfil the contract are in the scope of other standards to determine if other standards require them to be expensed or capitalised. The accounting for the software costs is in the scope of the guidance for internally developed software and should be evaluated in accordance with that guidance. Leasehold improvement costs fall under property, plant and equipment (PP&E) guidance and should be evaluated accordingly.



## 5. Recognise revenue *(cont'd)*

### Example 5(c) – Transportation costs

**Facts:** A shipping company has a vessel at point A and enters into a voyage charter contract with a customer to transport goods from point B to point C. The shipping company concludes that the contract does not contain a lease.

**Question:** Can the shipping company capitalise the costs to move the vessel from point A to point B?

**Analysis:** These costs do not fall under other guidance so the revenue standards would be applied. Judgment would be required to determine whether the costs to move the vessel (1) relate directly to a contract or to an anticipated contract that the company can specifically identify, (2) generate or enhance company resources that will be used in satisfying future performance obligations, and (3) are expected to be recovered. Assuming the costs meet these criteria, they would be capitalised.

### Example 5(d) – Portfolio approach versus individual revenue recognition

**Facts:** A container shipping company transports various customers' containers along a predetermined shipping route of around Port A, Port B, Port C, and back to Port A. The container shipping company concludes that the contract does not contain a lease. Different containers are loaded and unloaded at different ports. For example, one container is loaded at Port A and unloaded at Port C, another container is loaded at Port B and unloaded at Port C, and a third container is loaded at Port B and unloaded at Port A.

**Question:** Could the container shipping company recognise its transportation revenue from these three orders using a portfolio approach over the duration of the round-trip voyage or should it recognise revenue based on each individual voyage?

**Analysis:** The guidance may be applied to a portfolio of contracts (or performance obligations) with similar characteristics only if it reasonably expects that the effects of applying the portfolio approach would not differ materially from applying the new standards to the individual contracts. In the above example, we believe the container shipping company should account for its revenue based on the individual contracts with its customers.



# Other considerations

## **Principal versus agent (Gross versus net)**

Some arrangements involve two or more unrelated parties that contribute to providing a specified good or service to a customer. In these instances, management will need to determine whether the company has promised to provide the specified good or service itself (as a principal) or to arrange for those specified goods or services to be provided by another party (as an agent). This determination often requires judgment, and different conclusions can significantly impact the amount and timing of revenue recognition.

Management should first understand the relationships and contractual arrangements among the various parties. This includes identifying the specified good or service being provided to the end customer and determining whether the company controls that good or service before it is transferred to the end customer. It is not always clear whether the company obtains control of the specified good or service. The revenue standard provides indicators to help management make this assessment.

New guidance	Current PSAK
<p>A company is the principal and should report revenue on a gross basis if it controls the specified good or service before it is transferred to the customer.</p> <p>Conversely, a company is an agent and should report revenue on a net basis if its obligation is to arrange for another party to provide goods or services (i.e., the company does not control the specified good or service before it is transferred to the customer).</p> <p>Indicators to assist companies in determining whether it controls the good or service before it is transferred to the customer are:</p> <ul style="list-style-type: none"> <li>• The company is primarily responsible for fulfilling the promise</li> <li>• The company has inventory risk</li> <li>• The company has discretion in establishing the price</li> </ul> <p>Under the new standard, no single indicator is determinative or weighted more heavily than others. However, some indicators may provide stronger evidence, depending on the circumstances.</p> <p>The principal versus agent assessment is performed at the performance obligation level, not at the contract level. A company may act as a principal with respect to certain performance obligations in the contract and an agent with respect to others.</p>	<p>A company is acting as a principal when it is exposed to the overall risks and rewards of the transaction. It presents revenue gross if the gross economic benefit from the business activity results in an increase in the company's equity. Alternatively, the company presents revenue net if the gross economic inflows include amounts collected on behalf of the principal.</p> <p>The following are indicators to assess in determining whether gross or net revenue presentation is appropriate:</p> <ul style="list-style-type: none"> <li>• Primary responsibility for providing the goods or services</li> <li>• Inventory risk</li> <li>• Latitude in establishing price</li> <li>• Credit risk</li> </ul>



## Other considerations *(cont'd)*

### **Potential impact:**

Although the indicators in the new standard are similar to those in the current guidance, the purpose of the indicators is different. The new standard requires a company to assess whether it controls the specified good or service, and the indicators are intended to support the control assessment.

In contrast, the existing guidance is focused on assessing whether the company has the risks and rewards of a principal. Companies will therefore need to reassess their arrangements through the lens of the control principle.

The new standard also provides more guidance on the unit of account that should be used in the gross versus net assessment, which could result in changes to the assessment as compared to current guidance.

### **Example 6(a) – Principal versus agent assessment**

**Facts:** A customer purchases a ticket to fly from point A to point C from Airline Y, with a stop at point B. Airline Y will operate the flight from point A to point B and Airline Z will operate the flight from point B to point C. At the time of booking, the customer is aware that Airline Z will operate the second segment of the flight, and while Airline Y has latitude to price the entire ticket, it does not bear any inventory risk over seats on Airline Z's plane. Airline Y has concluded that each flight segment is a separate performance obligation.

**Question:** Should Airline Y record revenue as a principal or as an agent in this transaction?

**Analysis:** For each performance obligation, Airline Y should determine whether its promise is to provide a service (as a principal) or to arrange for a third party to provide services (as an agent).

For the first flight segment, Airline Y concluded that revenue should be recorded on a gross basis as it is the only company involved in providing the flight service from point A to point B.

Conversely, for the second flight segment, Airline Y may conclude that it has merely arranged for Airline Z to provide the flight and should report revenue on a net basis (e.g., reflecting only its fee from Airline Z as revenue for arranging the carriage). If Airline Y has no inventory risk and is not primarily responsible for fulfilling the promise to fly the customer from point B to point C, it may indicate that Airline Y does not control the service before it is transferred to the customer.





↑  市區的士  
Urban Taxi

↑  新界的士  
New Territories Taxi

↑  大嶼山的士  
Lantau Taxi  
→  停車場 3  
Car park 3

→ T2 二號客運大樓  
Terminal 2  
→  往內地交通  
Transport to Mainland China

二號客運大樓  
Terminal 2

登機手續辦理  
Check-in aisle

離港  
Departures

P 停車場 3  
Car park 3

往內地交通  
Transport to Mainland China

# PSAK 73

## Leases

*In 2017, DSAK-IAI issued PSAK 73. Under the new guidance, lessees will be required to bring substantially all leases onto their balance sheets. It is expected that the transportation and logistics sector will be significantly impacted by the new guidance given the high volume and dollar amounts of leases that will be reflected on the balance sheet.*



# At a glance

The new lease accounting standard will fundamentally change the accounting for lease transactions and is likely to have significant business implications.

Almost all leases will be recognised on the balance sheet, with a right of use of the asset and financial liability that recognise more expenses in the profit or loss during the earlier life of a lease.

This will have an associated impact on key accounting metrics, and clear communication will be required to explain the impact of changes to stakeholders.

## ***Why the new standard matters to the industry?***

For decades, financing aircraft through off-balance lease models has been a well-established practice in the airline industry. In addition, airport facilities, which are essential to run airline operations, are typically rented from the respective airport owner.

Under PSAK 73, substantially all lease contracts will be on the balance sheet of the lessee. Estimates suggest this change will mean that trillions of additional lease obligations will be added to the balance sheets of airlines worldwide. As most lease obligations are denominated in US Dollar, many airlines will also be exposed to additional foreign currency volatility into their profit or loss.

The PwC Global Lease Capitalisation study performed in 2016 concludes that the airline sector will be the second most impacted after the retail industry. The median increase in on-balance debt is projected to be +47%. About 50% of airlines are expected to increase debts by more than 25%. Due to the respective change in the profit or loss geography (with interest and depreciation presented instead of rental expenses), the median increase in EBITDA is projected with some +33%.

Another sector that is likely to be one of the most affected by the new standard is the shipping industry, given that bareboat, time-charter contracts and other arrangements will typically fall under the definition of a lease. The PwC study on the impact of lease capitalisation indicated that there would be a median debt increase of 24% and a 20% median increase in EBITDA for the transport and infrastructure industry.

Whilst the new standard leaves lessor accounting substantially unchanged, it will have a significant impact on the shipping industry's customer base, its charterers (lessees). Historically, most charter contracts have been considered as operating leases and have, therefore, not had any impact on the balance sheets of charterers. Charter-in hires were typically recognised in the income statement on a straight-line basis over the lease term and classified, in their entirety, as operating expenses. Under the new lease standard, these contracts will be recognised on the balance sheet and the income statement charge will need to be allocated between operating expenses (depreciation) and finance costs. The impact of the new standard on the charterers' financial reporting is, therefore, significant and may lead to a change in the behaviour of the charterers when negotiating new contracts. This will have a business impact on ship owners (lessors) as well.

Our in-depth publication "[PSAK 73 – Leases, A new Era for Lease Accounting](#)" provides a comprehensive analysis of the new standard. This publication summarises the main aspects of the standard, highlighting some key challenges and matters to consider in a transition.

# Overview

The new standard covers every lease except for rights to explore non-regenerative resources, rights held under licencing arrangements, leases of biological assets and service concession arrangements. For lessors, leases of intellectual property are excluded from PSAK 73; lessees are not required to apply PSAK 73 to certain rights held under licensing arrangements.

PSAK 73 requires lessees to capitalise all leases, except for short-term leases and leases of low-value assets. This is a significant change from PSAK 30, where operating leases were off balance sheet.

The accounting model for lessors is substantially the same as under existing PSAK. Lessors will classify leases as operating or financing. A lease that transfers substantially all risks and rewards incidental to ownership is classified as a finance lease. All other leases are classified as operating leases.

## **Effective date and transition**

The new standard is effective for annual reporting periods beginning on or after 1 January 2020.

Earlier application is permitted, but only in conjunction with adopting PSAK 72, 'Revenue from contracts with customers'. This means that an entity is not allowed to apply PSAK 73 before applying PSAK 72. The date of initial application is the beginning of the annual reporting period in which an entity first applies PSAK 73.

The new standard is required to be adopted using either a full retrospective approach under PSAK 25, 'Accounting policies, changes in accounting estimates and errors', or a simplified approach. Under the simplified approach, lessees do not need to restate comparative information, but they should instead recognise the cumulative effect of applying the standard as an adjustment to the opening retained earnings at the date of initial application.

If a lessee chooses the 'simplified approach' for its leases that are currently classified as operating leases, it can choose whether to recognise the right-of-use assets retrospectively or the lease liability on transition. Right-of-use assets based on the lease liability will typically be bigger than those calculated retrospectively, resulting in more depreciation and reduced profitability in future.

The simplified approach provides various practical expedients, including being allowed to use hindsight.

Lessees calculating right-of-use assets retrospectively under the 'simplified approach' have a choice of using hindsight (which is not available under the full retrospective application). Hindsight relates to areas of estimation and judgement (for example, whether the lessee was reasonably certain to extend a lease). Hindsight should not be applied to areas that do not involve judgement or estimation (for example, leases that have been modified or would have been reassessed).

All lessees calculating a right-of-use asset retrospectively (under either transition approach) will have to retrospectively calculate how the right-of-use asset would have changed each time there was a modification (such as a renegotiation) or a reassessment (such as a market rent review or inflationary increase).

# Overview (cont'd)

## Impact on key accounting metrics

The new accounting treatment for lessees will immediately affect a range of key metrics monitored by stakeholders, including net debt and gearing (increase as lease liability included in net debt), net assets (decrease as the right of use asset amortises on a straight-line basis while the lease liability is unwound more slowly in early years) and EBITDA (increase as the rental expense is replaced by interest and amortisation).

Many airlines use Return on Capital Employed (ROCE) to measure the amount of value generated. The above-mentioned implications will most likely also affect the individual ROCE calculations. Cost of Available Seat Kilometres (CASK), which is an important non-GAAP measure used in the industry, will be affected by changes to EBITDA. Additionally, any lump sum adjustments used by analysts to calculate the comparable level of debt from aircraft financing will probably not concur with numbers calculated under PSAK 73. Therefore, listed airlines will also need to communicate this to analysts appropriately.

In the shipping space, all types of vessel charterers will likely see the most significant impact on their financial reporting. Companies that are involved solely in vessel owning are effectively lessors and will likely have the least impact on their financial reporting from the new standard. However, it is possible that the impact of the standard on charterers will be such as to change the behaviour of charterers towards particular types of charter arrangements, as companies try to manage the impact of the new accounting treatment of these contracts on their financial performance and accounting metrics. In this case, lessors would likely face business implications.

The new accounting standard may also have the wider potential business impacts for lessees:

- Debt covenants – covenants might need to be renegotiated.
- Share-based payments – performance metrics might need renegotiation.
- Dividend policy – the revised profile of the profit or loss expense might affect the ability to pay dividends.
- Lease negotiations – although accounting should not be the key driver in commercial negotiations, market behaviour might change towards shorter lease tenures or a change of other terms to minimise lease liabilities. This will also impact lessors.
- Future transactions – Decisions such as (re)financing or raising capital to fund growth, acquisitions and mergers and lease versus buy options are expected to be affected. Also, for anticipated capital market transactions any specific regulatory requirements regarding the presentation of historical information should be considered.

For transportation and logistics companies with a significant portfolio of leases, the ability to gather the required information on existing leases, and to capture data on new leases at the outset, will be critical to an orderly and smooth transition to the new standard. This might result in the need for new systems, controls and processes, which will take time to identify, design, implement and test.

# Is the contract a lease?

Lease accounting guidance applies to any arrangement that conveys control over an identified asset to another party. An arrangement is a lease, or contains a lease, if an underlying asset is explicitly or implicitly identified and use of the asset is controlled by the customer.

If an arrangement explicitly identifies the asset to be used, but the supplier has a substantive contractual right to substitute the asset, the arrangement does not contain an identified asset. A substitution right is substantive if (a) the supplier can practically use another asset to fulfil the arrangement throughout the term of the arrangement, and (b) it is economically beneficial for the supplier to do so. The supplier's right or obligation to substitute an asset for repairs, maintenance, malfunction or technical upgrade does not preclude the customer from having the right to use an identified asset.

An identified asset must be physically distinct. A physically distinct asset might be an entire asset or a portion of an asset. A capacity portion of an asset is not an identified asset if (1) the asset is not physically distinct (for example, the arrangement permits the lessor to allocate a different space to the lessee), and (2) a customer does not have the right to substantially all of the economic benefits from the use of the asset.

Arrangements will need to be assessed to identify whether there is an identified asset. There is no identified asset where the supplier has a substantive right to substitute the asset.

## **Example 1 – Aircraft owner with substitution rights**

**Facts:** Airline enters into a two-year contract with an aircraft owner (Supplier). Every Monday, Wednesday, Friday, Saturday and Sunday, the Supplier will exclusively transport passengers of the Airline from Paris to Mallorca at 10am and at the same day from Mallorca to Paris at 6 pm. The type of aircraft is specified by the Airline. The Supplier owns more than one aircraft of this type. The Supplier is permitted to substitute the aircraft at any time during the contract period and must substitute the aircraft if it is not working. Furthermore, the Supplier is responsible for operating the aircraft, and using its own crew.

**Question:** Does the contract contain a lease?

**Analysis:** The contract does not contain a lease.

There is no identified asset. The Supplier owns several aircrafts of the same type to fulfil its contractual obligations and can exchange the aircrafts without the permission of the Airline. Even if the aircraft will be specified in the contract there is no identified asset because the Supplier will benefit from using the aircraft for example on Tuesday and Thursday to carry out service for other customers. In addition, the Airline wouldn't have the right to obtain substantially all of the economic benefits from the use of the aircraft.

## Is the contract a lease? *(cont'd)*

### **Example 2 – Check-in space with substitution rights**

**Facts:** The Airline enters into a contract with an airport operator (the Supplier) to use a space in the airport to deploy its check-in machines and other equipment. The contract states the exact amount of space and that the space must be located in the entrance hall. However, the Supplier has the right to change the location of the space allocated to the Customer at any time during the contractual term. There are minimal costs to the Supplier associated with changing the space for the Customer and there are several unoccupied places in the entrance hall of the airport that would meet the specifications for the space to be used by the Customer.

**Question:** Does the contract contain a lease?

**Analysis:** The contract does not contain a lease.

The space where the check-in machines and the other equipment will be located is specified in the contract. However, fulfilment of the contract does not depend on the use of an identified space. The Supplier has a substantive right to substitute the space the Customer uses because the Supplier has the practical ability to change the space used by the Customer. There are several unoccupied places in the entrance hall that meet the specifications of the space used by the Customer, and the Supplier has the right to change the location of the space at any time without the Customer's approval. In addition, the Supplier would benefit economically from substituting the space. Besides the fact, there would be minimal cost associated with changing the space used by the Customer, and substitution allows the Supplier to make the most efficient cost.

A customer controls the use of the identified asset by possessing the right (1) to obtain substantially all of the economic benefits from the use of such asset ('economics' criterion), and (2) to direct the use of the identified asset throughout the period of use ('power' criterion). A customer meets the 'power' criterion if it holds the right to make decisions that have the most significant impact on the economic benefits derived from the use of the asset.

For example, the 'right to control the use' of the ship might be evidenced by the exclusive use of the ship by the charterer, where they have the ability to decide whether and what cargo will be transported and when and to which ports the ship will sail to throughout the period of use, even if protective rights exist. Moreover, the 'right to control the use' of the ship might be evidenced even in cases where the charterer does not have the exclusive use of the ship but the charterer's cargo occupies substantially all of the capacity of the ship, thereby preventing other parties from obtaining economic benefits from the ship. In these cases, the charterer shall also have the ability to make decisions about how and for what purpose the ship is used to conclude that he has the 'right to control the use' of the ship.

The new model differs, in certain respects, from today's risks and rewards model, and it might result in the identification of fewer embedded leases compared to current guidance. However, under current lessee guidance, embedded leases are often off-balance sheet operating leases and, as such, application of lease accounting might not have had a material impact on the income statement. Determining whether to apply lease accounting to an arrangement under the new guidance is likely to be far more important, since virtually all leases will result in recognition of a right-of-use asset and lease liability.



# Is the contract a lease? *(cont'd)*

## **Example 3 – Right to control the use of the asset in the shipping industry**

According to the new standard, bareboat charters in the shipping industry will typically meet the new definition of a lease as, under these agreements, the charterer controls the use of the ship. Whilst voyage charters are not likely to meet the new definition of a lease, as the charterer typically does not have the right to direct the use of the ship, i.e. how and for what purpose the ship is used.



# Components, contract consideration, and allocation

An arrangement might contain lease and non-lease components that are subject to different accounting models. Components are those items or activities that transfer a good or service to the lessee. For example, time charters and pool arrangements are likely to contain both a lease (i.e. right to use the ship) and service components (i.e. operation and maintenance of the ship by the ship owner). At the same time, contracts of affreightment are unlikely to meet the definition of a lease, since they are contracts for the provision of a service rather than the use of an identified asset.

Arrangements might also contain multiple lease components. The right to use an underlying asset is a separate lease (from other leases within the contract) where the lessee can benefit from using the underlying asset on its own, or together with resources readily available to the lessee, and the underlying asset is not highly dependent on, or highly interrelated with, other underlying assets in the contract.

A lessee might elect to apply the practical expedient of accounting for a lease and the associated non-lease component as a single lease component. If the practical expedient is applied, the cash flows associated with the non-lease component will increase the liability and right-of-use asset recognised on the balance sheet. This is an election by asset class. Companies are likely to consider the significance of the increase in the right-of-use asset and liability relative to the effort and complexity required to obtain reliable information to separately account for the lease and non-lease components.

Transportation and logistics lessees with material leases will need additional processes, controls and documentation to ensure appropriate and consistent application of the guidance. For example, the guidance requires an appropriate allocation based on relative stand-alone prices that maximises the use of observable prices.



# Lease classification and initial measurement

Lessees will recognise a right-of-use asset and lease liability for virtually all of their leases (other than short-term leases or leases of low-valued assets for which they elect to apply an exemption). There will be no distinction between finance and operating leases for lessee accounting, as is the case under PSAK 30. However, lessors will continue to classify leases as operating or finance leases.

Short-term leases are leases with a lease term of 12 months or less. The lease term also includes periods covered by an option to extend, or an option to terminate, if the lessee is reasonably certain to exercise the extension option, or not to exercise the termination option. A lease that contains a purchase option is not a short-term lease.

For lessees, due to the nature of assets commonly leased in the transportation and logistics sector, the above recognition and measurement exception is unlikely to have a practical effect for the aviation and shipping industries.

At the commencement date, the lessee measures the lease liability at an amount equal to the present value of the lease payments during the lease term that are not paid at that date. Lease payments consist of the following components:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable;
- variable lease payments that depend on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option (if the lessee is reasonably certain to exercise that option); and
- payments of penalties for terminating the lease (if the lease term reflects the lessee exercising the option to terminate the lease).

Variable lease payments that do not depend on an index or a rate are not included in the lease liability and would be recognised in the period the obligation is incurred.

The lessee will also recognise a right-of-use asset to an equal amount plus initial direct costs.

## Example 4 – Rental payments that depend on a rate

**Facts:** As of 1 January 2016, Airline enters into three-year lease agreement with rentals, which vary based on the 3M-Euribor rate. The rentals will be paid monthly and amount to 10 CU at lease commencement. Every six months the rentals are adjusted to the then-prevailing 3M-Euribor plus 150 bpts. The incremental borrowing rate at lease commencement is 2.8%.

**Analysis:** At commencement, the Airline measures the present value of the lease liability and the right-of-use asset by discounting 36 months of lease payments (i.e. 360 CU) using 2.8%.

As of 1 July 2016 the rentals have been increased to 11 CU due to a change in the 3M-Euribor. At that date the Airline remeasures the lease liability to reflect this change. The new carrying amount of the lease liability is calculated as the present value of the outstanding 30 months of rentals (i.e. 330 CU). As the change in the lease payments results from a change in a floating interest rate (3M-Euribor), the Airline must also use a revised discount rate which reflects the change in the interest rate.

The difference between the carrying amount of the lease liability before and after the remeasurement results in a corresponding adjustment to the right-of-use asset.



# Lease classification and initial measurement *(cont'd)*

The existence of renewal options or lessee rights to extend are a common feature of leases. Periods covered by an option to extend the lease term are included in the lease term if the lessee is reasonably certain to exercise that option. Hence, at initial recognition, lessees should include lease payments in future periods if the lessee is 'reasonably certain' to exercise the extension option.

PSAK 73 lists various factors to consider, but it does not prescribe how to weight the individual factors when determining whether it is 'reasonably certain' that a lessee will exercise an option. A number of factors should be considered to assess if it is reasonably certain that the lessee will renew the lease, such as lease term, location, termination penalties and magnitude and expected useful life of any leasehold improvements.

Non-monetary aspects are included in the analysis, provided that they reflect economic incentives and not irrational behaviour. Examples of non-monetary aspects include the time and business disruption to find a replacement asset and to enter into a new contract.

A lessee's past practice might provide information that is helpful in assessing whether the lessee is reasonably certain to exercise, or not to exercise, an option. It is, however, key to understanding the economic reasons for that past practice. Those economic reasons, if any, must be taken into account in the lease term assessment.

Our common observation is that measurement of the lease liabilities will be highly judgmental and is going to be affected by the different terms, including:

- Contingent/variable hire, renewal and/or purchase options and other services received under the agreements – these might all affect the measurement of the lease liability. Given the volatility of the market, the calculation of the lease liability is likely to be challenging, as lessees will need to assess whether it is reasonably certain to exercise the renewal and/or purchase options both initially and subsequently at each reporting date. Also, lease payments may be fixed, indexed, performance based or might include minimum guaranteed consideration.
- The lease payments shall be discounted using the interest rate implicit in the lease, and whenever that rate cannot be readily determined, the lessee's incremental borrowing rate adjusted to reflect the terms and conditions of the lease.
- Remeasurements of the lease liability will also be required whenever cash flows under the lease change. For example, in the shipping industry in cases where the charters are linked to an index, this need for remeasurement will likely be challenging due to the volatility of the charter rates. Any remeasurements would require a relevant adjustment to right-of-use asset or might affect the income statement, depending on the circumstances. In addition, income statement volatility might also arise through foreign exchange differences on the translation of the lease liability and right-of-use asset to the lessee's functional currency, if applicable.

The lessee might be obliged to return the underlying asset to the lessor in a specific condition or to restore the site on which the underlying asset has been located. The accounting for these obligations is comparable to the current accounting. The lessee continues to recognise a provision in accordance with PSAK 57, 'Provisions, contingent liabilities and contingent assets', to reflect this obligation. The initial carrying amount of any provision is included in the measurement of the right-of-use asset. Obligations incurred during the term of the lease (such as wear and tear) are recognised as an expense as incurred.

# Lease classification and initial measurement *(cont'd)*

## Example 5 – Maintenance expenses

**Facts:** The Airline will incur maintenance expenses before returning the aircraft back to the lessor due to contractually-agreed return conditions.

**Question:** How PSAK 73 impact the accounting for maintenance?

**Analysis:** In many situations, PSAK 73 will not change the current practice in accounting for maintenance. However, if the maintenance costs relate to contractually-agreed return conditions, PSAK 73 requires those costs to be included as part of the measurement of the right-of-use asset when the obligation is recognised. At the same time, the airline would account for a provision in accordance with PSAK 57. Subsequent accounting for the provision and the portion of the right-of-use asset that belongs to those future maintenance costs will be in accordance with ISAK 9, Changes in Existing Decommissioning, Restoration and Similar Liabilities.

## Subleases

IFRS 73 requires the lessor to evaluate a sublease with reference to the right-of-use asset. Intermediate lessors must now classify subleases based on the right-of-use asset from the head lease, rather than the underlying lease asset (as under PSAK 30). Therefore, subleases are now more likely to be classified as finance leases.

For example, the term of a vessel sublease would be compared to the term of the head lease when assessing whether the lease is for the major part of the economic life. Similarly, the present value of lease payments is compared to the fair value of the right-of-use asset, instead of the underlying asset, when assessing whether it is for substantially all of the fair value. The change to sublease guidance must be considered both on transition to PSAK 73 for existing subleases and for all new subleases entered into once PSAK 73 applies.

## Practical impact:

Transportation and logistics companies may find themselves in a situation where they act as a lessee in relation to the head lease and an intermediate lessor in the sublease, required to apply guidance in PSAK 73.

The lessor of a sublease will have to recognise an asset on its balance sheet – a right-of-use asset with respect to the head lease (if the sublease is classified as an operating lease) or a lease receivable with respect to the sublease (if the sublease is classified as a finance lease). For a sublease that results in a finance lease, the intermediate lessor is not permitted to offset the remaining lease liability (from the head lease) and the lease receivable (from the sublease). The same is true for the lease income and lease expense relating to head lease and sublease of the same underlying asset.

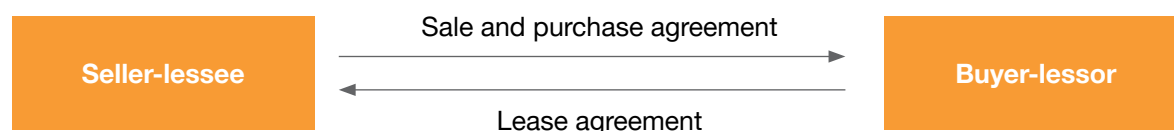
This will have an impact on all companies chartering-in vessels that are subsequently sub-chartered out.

# Sale and leaseback transactions

## ***Determining whether the transfer is a sale***

Aside from lessee accounting, the accounting for sale and leaseback transactions is one of the main areas in which the new lease standard changes the current guidance. The accounting for sale and leaseback transactions under PSAK 30 mainly depended on whether the leaseback was classified as a finance or an operating lease. Under PSAK 73 the determining factor is whether the transfer of the asset qualifies as a sale in accordance with PSAK 72. An entity should apply the requirements for determining when a performance obligation is satisfied in PSAK 72, to make this assessment.

*Structure of a sale and leaseback*



## ***Transfer of the asset is a sale***

If the buyer-lessor has obtained control of the underlying asset and the transfer is classified as a sale in accordance with PSAK 72, the seller-lessee measures a right-of-use asset arising from the leaseback as the proportion of the previous carrying amount of the asset that relates to the right of use retained. The gain (or loss) that the seller-lessee recognises is limited to the proportion of the total gain (or loss) that relates to the rights transferred to the buyer-lessor.

If the consideration for the sale is not equal to the fair value of the asset, any resulting difference represents either a prepayment of lease payments (if the selling price is below market terms) or an additional financing (if the selling price is above market terms). The same logic applies if the lease payments are not at market rates. The buyer-lessor accounts for the purchase in accordance with applicable standards (such as PSAK 16 if the underlying asset is an item of property, plant and equipment), and for the leaseback in accordance with PSAK 73.

# Sale and leaseback transactions

## *(cont'd)*

### Example 5 – Maintenance expenses

**Facts:** Airline sells a ten-year old airplane (book value of 50 CU) to Lessor for 100 CU and immediately leases it back for eight years. The lease agreement contains no repurchase obligation or any call or put option. There is a renewal option to extend the lease term for a further five years. However, at lease inception extension of the lease has been assessed as to not be reasonably certain. The present value of the eight-year leaseback rentals amount to 70 CU.

**Question:** How is the profit or loss for sale and leaseback transactions determined?

**Analysis:** The rentals for the leaseback represents 70% of the airplane's fair value. This means that the Airline has sold 30% of the airplane's residual value. In accordance with the sale and leaseback provisions of

PSAK 73, the seller-lessee (the Airline) recognises a right-of-use asset of 35 CU, which represents 70% of the former book value (i.e. the portion retained). There is a gain of 15 CU, which represents 30% of the difference between the fair value of the airplane (30 CU) and the book value of the portion sold (15 CU).

### **Transfer of the asset is not a sale**

If the transfer is not a sale (that is, the buyer-lessor does not obtain control of the asset in accordance with PSAK 72), the seller-lessee does not derecognise the transferred asset, and it accounts for the cash received as a financial liability. The buyer-lessor does not recognise the transferred asset, and instead it accounts for the cash paid as a financial asset (receivable).



# Glossary

AFS	Available for sale
DSAK-IAI	<i>Dewan Standar Akuntansi Keuangan – Ikatan Akuntan Indonesia</i> or “Financial Accounting Standards Board – Indonesian Institute of Accountants”
ECL	Expected credit loss
FOB	Free on Board
FVPL	Fair Value through Profit or Loss
FVOCI	Fair Value through Other Comprehensive Income
IFAS	Indonesian Financial Accounting Standards
IFRS	International Financial Reporting Standards
IP	Intellectual Property
ISAK	<i>Interpretasi Standar Akuntansi Keuangan</i> or “Interpretation of Financial Accounting Standards”
OCI	<i>Other comprehensive income</i>
PSAK	<i>Pernyataan Standar Akuntansi Keuangan</i> or “Statement of Financial Accounting Standards”
SAK	<i>Standar Akuntansi Keuangan</i> or “Financial Accounting Standards”
SPPI	Solely Payments of Principal and Interest





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