Lessee: build two opening amounts

MODULE 1 / IFRS 16

1. **Check the contract**
   Identified asset + control of use + consideration.

2. **Determine the lease term**
   Include option periods only when the specified certainty test is met.

3. **Identify unpaid lease cash flows**
   Separate services unless the permitted expedient is elected.

4. **Discount the liability**
   Implicit rate if readily determinable; otherwise incremental borrowing rate.

5. **Build the right-of-use asset**
   Liability + prepayments - incentives + qualifying costs/restoration.

Remember	Why it matters
12 months or less is not enough	A short-term lease must have no purchase option.
Low value is assessed when new	An old expensive asset is not automatically low value.
Residual guarantee	Lessee includes the expected amount payable, not automatically the whole guarantee.
Variable payments	Index/rate and in-substance fixed amounts differ from pure usage/sales payments.
Payments made now	Add to the ROU asset; exclude from unpaid liability.

AASB 16 (December 2021), paragraphs 5-8, 9-28, Appendix A, B3-B33. Guide: Module 1, pp. 38-41.
standards.aasb.gov.au/aasb-16-dec-2021

Lessee: three payments in arrears

MODULE 1 / ORIGINAL WORKED EXAMPLE

Three annual payments of $12,000 at each year end; rate 6%; no services, incentives, guarantees, costs or options. Ownership does not transfer; useful life five years. Liability and initial ROU asset = **$32,076.14**. Depreciation period: three years.

Year	Opening	Interest	Cash paid	Closing
1	32,076.14	1,924.57	(12,000)	22,000.71
2	22,000.71	1,320.04	(12,000)	11,320.75
3	11,320.75	679.25	(12,000)	0.00

Entries at commencement and Year 1

Event	Debit	Credit
Commencement	ROU asset 32,076.14	Lease liability 32,076.14
Interest	Finance expense 1,924.57	Lease liability 1,924.57
Payment	Lease liability 12,000.00	Cash 12,000.00
Depreciation	Depreciation expense 10,692.05	Accumulated depreciation 10,692.05

Repeat interest and cash entries each year. Total interest = $36,000 - $32,076.14 = $3,923.86. Retain precision in schedules; adjust final cents when posting.

Advance-payment variation

Pay at times 0, 1 and 2 instead. Initial liability = **$22,000.71**; ROU asset = **$34,000.71**. Debit ROU asset $34,000.71; credit liability $22,000.71 and cash $12,000. Liability ends after Year 2, but use and depreciation continue through Year 3.

AASB 16 (December 2021), paragraphs 22-36. Guide: Module 1, pp. 39-42. Original calculations; no tax or lease modification assumed.

Lessor: separate the residual recovery

MODULE 1 / FINANCE AND OPERATING LEASES

For a finance lease, the net investment includes lease payments under lessor rules and the unguaranteed residual accruing to the lessor. That residual is not a debt owed by the lessee.

Original ordinary-lessor example: three year-end receipts of $10,000, unguaranteed residual $4,000 recovered at Year 3 end, implicit rate 8%. No direct costs or selling profit. Initial underlying carrying amount equals net investment.

Stage	Net investment
Initial: PV of receipts plus residual	28,946.30
After Year 1 cash receipt	21,262.00
After Year 2 cash receipt	12,962.96
After Year 3 cash receipt	4,000.00
After residual asset recovery at assumed value	0.00

Initially: debit net investment and credit underlying asset $28,946.30. Year 1: debit net investment and credit finance income $2,315.70; then debit cash and credit net investment $10,000. Recovering the residual is a separate asset recovery.

Finance lease	Operating lease
Substantially all risks and rewards transfer. Assess substance; no automatic 75% or 90% rule.	Underlying asset remains recognised.
Recognise net investment and a periodic finance return.	Recognise lease income; depreciate and assess impairment.
Manufacturer/dealer lessors have additional rules.	Qualifying initial direct costs are added and expensed over the lease term on the income basis.

AASB 16 (December 2021), paragraphs 61-97 and Appendix A. Guide: Module 1, pp. 42-44. Full-precision calculations; display rounding only.