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Application of the new IFRS standards continues to remain a key focus area at Higher Education institutions. Below are some overall considerations for IFRS 9, 15 and 16 specific to the sector, IFRS 9 & 15, effective to most higher education for the financial year ended 31 December 2018 as well as IFRS 16, effective for the financial year ended 31 December 2019.

Considerations on IFRS 9: Financial instruments for the higher education industry

IFRS 9 (financial instruments) is part of the International Accounting Standards Board’s (IASB) project to replace IAS 39 (financial instruments: recognition and measurement). IFRS 9 addresses classification and measurement of financial assets and replaces the multiple classification and measurement models in IAS 39 with a single model that has only two classification categories: amortised cost and fair value.

The classification category is firstly determined based on whether the instrument is a debt or equity instrument. For debt instruments, the classification is impacted by the institution’s business model for managing the financial asset and the characteristics of the contractual cash flows generated by the financial asset. IFRS 9 also includes an expected credit losses model that replaces the current incurred loss impairment model. The classification, measurement and presentation for financial liabilities and for the derecognising financial instruments has been relocated to IFRS 9 with limited changes.

Balances most likely impacted:

- Available for sale investments (classification and measurement)
- Money market instruments (classification and measurement)
- Bonds (classification and measurement)
- Student receivables (impairment)
- Other receivables (impairment)

Practical considerations for the year of adoption:

- Most institutions have significant funds under management by fund managers. The impact of IFRS 9 on classification is dependent on the terms of the fund agreements (as set out below).
- The institution’s election on the classification of equity instruments and its business model assumptions for classification of debt instruments should be documented in appropriate detail.
- Most institutions recognised an impairment provision based on debtors ageing in the past without considering credit risk for each type of counterparty. This may have resulted in an overprovision on balances owed by e.g. government Universities that pay, but pay late. The impact of IFRS 9 may therefore be a reduction in the provision for impairment.

Transition

The standard is to be applied retrospectively. Restatement of comparatives is not required, but the institution is permitted to restate comparatives if it can do so without the use of hindsight. If the institution does not restate comparatives, it should adjust the opening balance of its retained earnings for the effect of applying the standard in the year of initial application. The assessment of the impact on classification and impairment should therefore be performed and adjusted for on 1 January 2018, in retained earnings, as well as on 31 December 2018.
Classification and measurement of debt instruments

The institution recognises a financial asset when it first becomes a party to the contractual rights and obligations in the contract. It is, therefore, necessary to measure those contractual rights and obligations on initial recognition. Most universities make use of fund managers to manage their investment portfolios. It is important to understand the terms and conditions of the mandate with these fund managers in order to determine the impact IFRS 9 has on classification and measurement.

Questions to consider on funds invested by a fund manager:

• Are the underlying investments in the name of the institution?
• Does the fund invest in both equity and debt instruments?
• For equity instruments – what is the institution’s irrevocable election on initial recognition, on an instrument-by-instrument basis – fair value through profit/loss or fair value through other comprehensive income (OCI)?
• For debt instruments – what happens to investments when the contract with the fund manager terminates or the institution exits the contract?

If the fund manager liquidates the debt instruments and the institution only receives cash based on the fair value of the portfolio on liquidation, this indicates that the institution fails the ‘solely payments of principal and interest test’ and would need to account for the debt instruments at fair value through profit and loss.

Impairment

General impairment model:

The more onerous three-stage model applies to:

• investments in debt instruments measured at amortised cost
• investments in debt instruments measured at fair value through other comprehensive income (FVOCI)
• all loan commitments (e.g. intercompany loans) not measured at fair value through profit or loss
• financial guarantee contracts to which IFRS 9 is applied and that are not accounted for at fair value through profit or loss
• lease receivables that are within the scope of IAS 17 (accounting policies and disclosures applicable to leases), trade receivables and contract assets within the scope of IFRS 15 (revenue from contracts with customers) that give rise to a conditional right to consideration.

The model does not apply to investments in equity instruments.

Simplified approach for trade receivables, contract assets and lease receivables:

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 its life at an amount equal to lifetime expected credit loss. As a practical expedient, a provision matrix can be used to estimate expected credit loss for these financial instruments.

These are the steps to follow in calculating the impairment on the student and sundry receivable balances:

Step 1: Stratify the accounts receivable book.

The stratification should be based on the nature of the receivable and the possible impact that macroeconomic factors could have on the group of receivables. The stratification is judgmental and requires quantitative loss history. The institution should clearly document the rationale for its stratification.

Student receivables should be stratified based on payment terms (to the extent that the information is available and reliable) e.g. private students, students funded through the National Student Financial Aid Scheme and bursary students. Student receivables should further be stratified based on locations, if that makes sense for the institution.

Other receivables could be stratified between government receivables, large corporates, medium-sized corporates and individuals depending on the characteristics of the receivables.

Step 2: Determine how much data is available when collating the write-off history

The more data the better. Seven years is considered an average economic cycle.

Another method that could be applied is to infer the credit rating of specific organisations, such as universities with listed debt or government universities, and to apply the credit spread relating to the inferred credit rating to the specific debtor or class of debtors. (e.g. various levels of government).

Step 3: Identify the reasons for the write-offs identified in Step 2.

Exclude write-offs from the history if they were isolated and not recurring. Consider the impact of a write-off because of students not enrolling or for other reasons. If the write-off event is isolated, it should be excluded from the historical information to ensure that it does not taint the data.
Step 4: Consider the correlation of macroeconomic factors to write-off history.

The assessment of macroeconomic factors should include both a qualitative and quantitative assessment. Matters that could impact on student receivables include changes in legislation, the impact of government assistance and many others. It is important that the institution assess the causes of prior year write-offs and determine if there was a lag between the change in the macroeconomic factor and the subsequent write-offs.

Step 5: Incorporate forward-looking information

The institution should assess if the impact of forward-looking information can be determined internally, as well as what information is needed to make such an assessment. It is not appropriate to automatically conclude that the impact is immaterial.

Key impairment reminders:

- One key difference in student receivables that should be considered is that, at reporting date, most of the student receivables are significantly overdue.
- Consider write-offs as far back as possible.
- It is unlikely that a single model can be applied to the entire debtors’ book, e.g. government receivables may just be paid late, but may not be impaired.
- Impairment on students funded by government should be separately considered.
- Forward-looking information is not automatically immaterial.
- More than one macroeconomic factor may impact write-offs.
- No write-off history does not preclude the application of IFRS 9.
- Consider a possible lag when considering write-offs.
- All the judgements and estimates made as part of calculating impairment should be documented.
- IFRS 9 has extensive disclosure requirements that should be considered.
Considerations on IFRS 15: Revenue from contracts with customers for the higher education industry

IFRS 15 (revenue from contracts with customers) has resulted in a single and comprehensive revenue-recognition model for all contracts with customers, to achieve greater consistency in the recognition and presentation of revenue. Revenue is recognised based on the satisfaction of performance obligations, which occur when control of goods or services transfers to a customer. In addition, the standard calls for more disaggregated and entity-specific disclosure of revenue.

The main sources of revenue for higher education institutions includes:

- Tuition fee income
- Residence income
- Research funding
- Miscellaneous income from sales of products

### Practical considerations for the year of adoption

- What is the transition method selected by the higher education institution – full retrospective or modified retrospective? Based on a limited poll, most institutions are applying the modified retrospective approach.
- How will the institution disaggregate its revenue streams in its disclosure? Not all the revenue streams referred to above are material. This is a key consideration in splitting revenue. Also, some revenue might be accounted for based on other standards, e.g. IAS 20 (government grants) for research funding or government subsidies. If material, the revenue streams should not be disclosed as part of revenue from contracts with customers.
- Has an analysis been performed to determine the impact of IFRS 15 on each source of revenue? The biggest impact is expected on income from research contracts.

### Key considerations on transition:

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| **Retrospective transition method**    | Universities are permitted to adopt the revenue standard by restating all prior periods (that is, full retrospective adoption) following IAS 8 (changes in accounting estimates). Universities electing retrospective application are permitted to use any combination of the following practical expedients:  
  - Disregard completed contracts that begin and end within the same annual reporting period (therefore begin and end in 2017), or are completed contracts at the beginning of the earliest period presented (contracts completed before 1 January 2017).  
  - Consider modifications before the beginning of the earliest period presented to form a part of the original contract.  
  - Do not disclose the amount of the transaction price allocated to the remaining performance obligations for the comparative period. |
| **Modified retrospective approach**    | Universities electing this approach will recognise the cumulative effect of initially applying the revenue standard as an adjustment to the opening balance of retained earnings (or other appropriate component of equity) in the period of initial application. Comparative prior year periods would not be adjusted. The institution would recognise the cumulative effect adjustment of applying the revenue standard in the opening balance of retained earnings as at 1 January 2018. Universities that choose to use this approach should provide the following additional disclosures in the reporting period that includes the date of initial application (that is, in the year of adoption):  
  - The amount by which each financial statement line item is affected in the current year as a result of applying the revenue standard (as compared to the previous revenue guidance).  
  - A qualitative explanation of the significant changes between the reported results under the revenue standard and the previous revenue guidance. |
Research funding contract considerations

After extensive consultation, a decision tree was developed to assist institutions to distinguish between research contracts in the scope of IAS 20 or IFRS 15. The following are the key questions to answer in assessing the impact of the new revenue standard on each research funding contract:

- Is the contract in the scope of the new revenue standard, or is it a government grant?

- If the contract is in the scope of the new revenue standard, how many performance obligations can be identified in the contract?

- If performance obligations are satisfied over time, what is the best measure of progress?

- Is there a process in place to determine the measure of progress at year-end, and is the measure of progress reliable and verifiable?

- How does the institution account for assets acquired in a research contract that it keeps after completion of the research project?

Determining whether an arrangement is in the scope of the revenue standard can be complex and requires significant judgement. Arrangements may contain elements of both a customer and collaborator relationship or may represent a government grant. Both collaboration relationships and government grants are scoped out of the revenue standard.

A contract may be entered into with a government or similar entity where the amount is awarded unconditionally without regard to the institution’s future actions, or requirement to incur further costs. Such grants may be given for the institution’s immediate financial support, or assistance, or for the reimbursement of costs previously incurred. They may also be given to finance an institution’s general activities over a specified period, or to compensate for a loss of income. Grants awarded on such a basis are recognised in the income statement in the period in which they become receivable and would also not be accounted for in terms of the new revenue standard.

Contracts where the government is acting as a customer to whom the institution is delivering research services, would be in the scope of IFRS 15.

Where contracts are in the scope of IFRS 15, the institution should consider how many distinct performance obligations are in the contract and if these are satisfied over time or at a point in time.

Most of the performance obligations are satisfied over time as the research is performed based on the assumption that the research is owned by the institution’s customer.

An appropriate measure of progress should be used to accurately depict how the institution progresses towards satisfaction of each of the performance obligations. Determining the measure of progress appears to be complex for higher education institutions and the following considerations are relevant:

- An appropriate output measure could be a survey of work performed. The department or individuals directly involved in the research project would be best placed to provide these as most research contracts require periodic reporting on progress to the customer.

- Cost incurred may be an appropriate input measure of progress. This method is problematic if the cost incurred includes costs that should be excluded from the measure of progress, such as the purchase of assets that the institution keeps after the contract is completed, or other uninstalled materials.
Considerations on IFRS 16: Leases for the higher education industry

The International Accounting Standards Board (IASB) published IFRS 16 (Leases) in January 2016 with an effective date of 1 January 2019, therefore applicable for the first time to most higher education (HE) institutions for the 31 December 2019 year-end. Under the previous guidance in IAS 17 (accounting policies and disclosures applicable to leases), a lessee had to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). The new standard requires lessees to recognise nearly all leases on the balance sheet, which will reflect their right to use an asset for a period of time and the associated liability for contractually agreed payments.

Many higher education institutions lease a vast number of high-value assets such as cars, buildings and land, including the rental of parking bays. Therefore, lessees will be greatly affected by the new standard. The lessors’ accounting largely remains unchanged.

Practical considerations in application of the new standard

• Are all the operating lease contracts identified? It may take a while to identify all existing operating lease contracts, especially in decentralised finance functions.

• Are all the policy decisions and judgements documented in sufficient detail? This will ensure consistency in applying these policies going forward, e.g. what assets are considered to be low-value assets for the HE institution.

• There are a number of expedients and decisions that are made in the initial adoption of the standard. Ensure that these elections and decisions are documented in sufficient detail and approved by the appropriate bodies within the HE institution.

Transition

IFRS 16 can be applied either fully retrospectively or through one of the simplified approaches. There is no impact on transition for the lessee in a finance lease as the lease liability and carrying amount of the leased asset is carried forward.

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| Fully retrospective approach | • The financial statements are presented as if IFRS 16 has always been applied since the inception of the lease.  
• Comparative amounts are restated for each prior period presented (opening balance sheet 31 December 2017, 31 December 2018).  
• The implication? A lessee goes back to the point in time it entered into every lease and gathers information on the terms and conditions of the leases. This is complicated and could have significant cost implications. |
| Simplified approach (two options) | • This approach is also applied retrospectively, but the impact of adoption is adjusted against the opening balance of retained earnings on the date of initial application (that is 1 January 2019).  
• Comparatives are not restated.  
• Calculate the Right Of Use asset either (lease-by-lease choice):  
• Retrospectively from the inception of the lease, depreciated up until 1 January 2019 (straight-lining asset/liability derecognised against retained earnings)  
• At the same value as the lease liability at transition date, therefore on 1 January 2019 (straight lining lease asset/liability derecognised against Right Of Use asset) |
What else is new?

New definition of a lease

• IFRS 16 defines a lease as a contract, or part of a contract, that conveys the right to use an asset for a period of time in exchange for payments. In practice, it can be challenging to assess whether a contract conveys the right to use an asset or is, instead, a contract for a service that is provided, using the asset.

• Universities can elect not to reassess existing lease contracts but to apply the new definition of a lease only to contracts entered into (or changed) on or after the date of initial application (this is commonly referred to as ‘grandfathering’). If an entity chooses this expedient, it shall be applied to all of its existing contracts on 1 January 2019.

• Service arrangements are more frequently identified for communication-related services such as storage capacity, networks etc.

Additional disclosure requirements

• For both, lessees and lessors, IFRS 16 adds significant new and enhanced disclosure requirements, which include a reconciliation between the operating lease commitments disclosed for 31 December 2018 and lease liabilities initially recognised under IFRS 16. Therefore, for the 31 December 2018 year-end, it is vital that the contingencies and operating lease commitments note is accurate and complete.

Measurement

Lease term and short-term leases

Lease term

Renewal and cancellation clauses in lease agreements may make it complex to determine the lease term.

IFRS 16 defines a lease term as the non-cancellable period for which the lessee has the right to use an underlying asset, including optional periods when an entity is reasonably certain to exercise an option to extend (or not to terminate) a lease.

Key questions to consider when assessing the lease term of the lease agreement:

• What are the contractual lease terms (i.e the minimum term defined in the contract)?

• Is there any option to extend the lease? (Implicit or explicit). An option to extend means any option to increase the lease term as defined above.

• Is it reasonably certain that management will exercise their option to extend at commencement date/date of initial application?

• Are there circumstances that have led to the lease terms being re-assessed? (Only applicable for subsequent measurement not relevant on date of initial application or lease commencement date).

• Does the lessor have any termination options which might indicate a shorter lease term?

• How long is the lease term, as determined above, after the effective date?
Short-term leases

The institution may potentially identify leases that will have a lease term of less than 12 months after 1 January 2019. The institution (as a lessee), may elect not to apply IFRS 16 to those specific leases. In such cases a lessee recognises the lease payments in profit or loss on a straight-line basis over the lease term. To be able to apply this exemption, the institution should determine the lease term on 1 January 2019. The determination of a short-term lease is consistent with the definition of a lease term as discussed above, and therefore the lease term considerations noted should also be taken into account.

Key considerations for the short-term lease exemption:

- A lease that contains a purchase option is not a short-term lease.
- The exemption is required to be applied by class of underlying assets.
- If the university applies the short-term lease exemption, it shall treat any subsequent modification or change in lease term as resulting in a new lease.

Low-Value Assets

The university may lease items such as lab equipment, office furniture and IT equipment, which may be considered to be low-value assets.

Take the following considerations into account when developing an accounting policy that determines what is a low-value asset:

- The IASB considered assets of a value of $5,000 or less when new. The value threshold is applied per asset.
- There is however no specific quantitative threshold. The $5,000 was used to illustrate a general principle.
- It is more important to focus on what the nature of the asset is. Cars would not qualify as low value assets because a new car would typically not be of low value. However cell phones would be examples of low-value assets for the university.
- Lab equipment may need to be stratified, and the nature of the equipment assessed, before concluding that it is of low value.
- The low-value exemption can be applied on an asset-by-asset and lease-by-lease basis.
- An asset is a low-value asset on its own if the lessee can obtain separate benefit from the asset, and the asset is not dependent or highly interrelated with other assets in the contract.

Therefore it may be appropriate for the institution to stipulate a value in its low value asset policy that it would use to assess whether an asset is a low-value asset. Both the value and the nature of the asset will play a role when determining if the asset is a low value asset.

Additional Key Measurement Reminders

Discount rate

The interest rate implicit in the lease is the discount rate used. If this rate cannot be readily determined, the lessee should instead use its incremental borrowing rate. The incremental borrowing rate would be complex to determine as most HE institutions do not have external borrowings. The borrowing rate should be based on an estimated rate applied to secured debt with a similar term of repayment to the lease term.

Separating lease components

IFRS 16 requires the identification of lease components and to be accounted for separately from non-lease components. A lease component is a separate component if there is separate benefit from the use of the asset or service for the lessee, and the underlying asset is not highly dependent on, or highly interrelated with, other assets in the contract.

For example, in vehicle leases, the contract for the car lease may be combined with a vehicle maintenance plan. Property leases could include the rental of premises and the rental of parking bays. Non-lease components could include operating costs incurred by the landlord in respect of maintaining and running the building, or could include property taxes and insurance payments.

Separate lease components practical expedient

Lessees have an accounting policy choice, applied by class of underlying asset, to not separate lease and non-lease components but rather account for these components as a single lease component. The result is a higher Right-Of-Use asset and a higher lease liability.

Variable lease payment

Variable lease payments, based on an index or rate, are part of the lease liability (e.g. CPI). Variable payments that are not based on a rate or index are recognised in the income statement when the event of conditions that triggers payment occurs (e.g. property rates based on government set rates and the value of the property). The existence of in-substance lease payments require judgement.
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