
IFRS® Interpretations Committee meeting

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| Date | March 2023 |
| Project | Potential annual improvements—Lessee accounting for lease payments forgiven (IFRS 9 and IFRS 16) |
| Topic | Initial consideration |
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Introduction

1. At its March 2022 meeting, the IFRS Interpretations Committee (Committee) discussed a request about a lessor's and a lessee's application of IFRS 9 *Financial Instruments* and IFRS 16 *Leases* in accounting for a rent concession in which the only change to the lease contract is the lessor's forgiveness of lease payments due from the lessee under the contract.
2. The Committee addressed a **lessor's** application of IFRS 9 and IFRS 16 in Agenda Decision [Lessor Forgiveness of Lease Payments \(IFRS 9 and IFRS 16\)](#) published in October 2022 (the Agenda Decision). In the Agenda Decision, the Committee concluded that the principles and requirements in IFRS Accounting Standards provide an adequate basis for a lessor to determine how to apply the expected credit loss model in IFRS 9 to an operating lease receivable and account for the rent concession described in the request.
3. With regard to **lessee** accounting, the Committee recommended in [March 2022](#) that the International Accounting Standards Board (IASB) consider undertaking a narrow-

scope standard-setting project—potentially in its next *Annual Improvements to IFRS Accounting Standards Cycle* (annual improvements).

4. The objective of this paper is:
- (a) to provide the Committee with background on the lessee accounting matter and our staff analysis; and
 - (b) to ask the Committee whether it agrees with our preliminary views:
 - (i) to propose that the IASB amend the definition of ‘lease modification’ in Appendix A to IFRS 16;
 - (ii) to propose that the IASB amend paragraph 2.1(b)(ii) of IFRS 9 to add a cross-reference to paragraph 3.3.3 of IFRS 9; and
 - (iii) to include these proposed amendments (see Appendix A to this paper) in the next annual improvements cycle.

Structure of this paper

5. This paper includes:
- (a) [Background information](#);
 - (b) [Staff analysis](#);
 - (c) [Question for the Committee](#);
 - (d) [Appendix A—recommended proposed amendments to IFRS 9 and IFRS 16](#);
and
 - (e) [Appendix B—Illustrative Example 19 accompanying IFRS 16](#).

Background information

The Committee's discussion in March 2022

6. At its March 2022 meeting, the Committee discussed lessee accounting for the rent concession described in the submitted fact pattern—see [Agenda Paper 4](#) for that meeting which sets out the request and staff analysis in more detail.

The fact pattern¹

7. The Committee received a request that described a rent concession agreed by a lessor and a lessee on the date the rent concession is granted. The rent concession changes the original terms and conditions of a lease contract. The lessor legally releases the lessee from its obligation to make specifically identified lease payments. No other changes are made to the lease contract, nor are there any other negotiations between the lessor and the lessee that might affect the accounting for the rent concession.
8. Until the date of being granted the rent concession, the lessee had recognised the payments forgiven as part of its lease liability. The lessee has not elected to apply the covid-19-related practical expedient in paragraphs 46A–46B of IFRS 16.²
9. The request asked whether the lessee applies the derecognition requirements in IFRS 9 or the lease modification requirements in IFRS 16 in accounting for the rent concession.

¹ The description of the fact pattern in this agenda paper omits information from the Agenda Decision that solely relates to the lessor's application of IFRS Accounting Standards.

² As stated in paragraph 46B of IFRS 16, the practical expedient in paragraph 46A of IFRS 16 applies only to rent concessions occurring as a direct consequence of the covid-19 pandemic and only if all of several conditions are met, including that any reduction in lease payments affects only payments originally due on or before 30 June 2022.

Lessee application of IFRS 9 and IFRS 16

10. The Committee agreed with the staff conclusion, summarised in paragraphs 68–69 of [Agenda Paper 4](#) for the March 2022 meeting, that there is more than one way for a lessee to read the principles and requirements in IFRS Accounting Standards in accounting for the rent concession in the submitted fact pattern. The lessee could:
- (a) apply paragraphs 3.3.1 and 3.3.3 of IFRS 9 to the part of the lease liability that is extinguished and paragraphs 45–46 of IFRS 16 in accounting for the lease modification (after having applied the derecognition requirements in IFRS 9 to the part of the lease liability extinguished). Such an approach would result in the lessee recognising the effect of the forgiveness of lease payments in profit or loss at the date on which the rent concession is granted.
 - (b) account for the forgiveness of lease payments by applying the lease modification requirements in IFRS 16. Such an approach would result in the lessee recognising the effect of the forgiveness of lease payments as a decrease in the carrying amount of the right-of-use asset.

Potential amendments to IFRS 16

11. The Committee agreed with the staff recommendation that the IASB consider a narrow-scope standard-setting project, potentially as an annual improvement, to clarify whether a lessee applies IFRS 9 or IFRS 16 in accounting for a rent concession such as the one described in the submitted fact pattern.
12. The Committee agreed with the staff's preliminary view that the IASB amend IFRS 16 to exclude from its scope a change to a lease contract that results *only* in the extinguishment of the lessee's lease liability (or a part of it) as described in paragraph 3.3.1 of IFRS 9. As a result of such an amendment:
- (a) the lessee would apply the derecognition requirements in IFRS 9 for a change to a lease contract that solely results in a lease liability (or a part of it) being extinguished; and

- (b) the lessee would apply the lease modification requirements in IFRS 16 for all other changes to a lease contract that meet the definition of a lease modification.

Potential amendments to Illustrative Example 19 accompanying IFRS 16

13. Some Committee members suggested that if the IASB considers amending IFRS 16 as described in paragraph 12 of this paper, it should also reconsider Illustrative Example 19 accompanying IFRS 16 (Illustrative Example 19). Illustrative Example 19, reproduced in Appendix B to this paper, illustrates a lease ‘modification that is a change in consideration only’. In the example fact pattern in Illustrative Example 19, the lessee accounts for a decrease in lease consideration as a lease modification applying IFRS 16; it remeasures the lease liability and recognises a corresponding adjustment to the right-of-use-asset.
14. A few Committee members said Illustrative Example 19 describes the change in consideration under the lease contract as a lease modification (in accordance with IFRS 16) but could also be viewed as—or is economically the same as—a partial extinguishment (in accordance with IFRS 9) of the lessee’s lease liability. Those Committee members suggested that the IASB clarify the application of IFRS 9 and IFRS 16 in the fact pattern in that example.

Potential amendments to IFRS 9

15. Some Committee members suggested that if the IASB considers amending IFRS 16 as described in paragraph 12 of this paper, it should also consider amending paragraph 2.1(b)(ii) of IFRS 9 to add a cross-reference to paragraph 3.3.3 of IFRS 9. Those Committee members suggested such a cross-reference to paragraph 3.3.3 of IFRS 9 to clarify the corresponding adjustment a lessee is required to make when accounting for an extinguishment of a lease liability.
16. Those Committee members noted that paragraph 2.1(b)(ii) of IFRS 9 states that lease liabilities recognised by a lessee are subject to the derecognition requirements in

paragraph 3.3.1 of IFRS 9. Applying paragraph 3.3.1 of IFRS 9, a lessee ‘removes a financial liability (or a part of a financial liability) from its statement of financial position when, and only when, it is extinguished ...’. Those Committee members said a lessee could make a corresponding adjustment to profit or loss applying paragraph 3.3.3 of IFRS 9—but is not required to do so because paragraph 2.1(b)(ii) of IFRS 9 does not refer to paragraph 3.3.3 of IFRS 9. Those Committee members said a lessee could instead make a corresponding adjustment to its right-of-use asset recognised applying IFRS 16. They were therefore of the view that it would be helpful for the IASB to resolve this lack of clarity for a lessee.

Staff analysis

Potential amendments to IFRS 16

17. Appendix A to IFRS 16 defines ‘lease modification’ as [bold font omitted]:

A change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease (for example, adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual lease term).

18. We recommend amending the definition of ‘lease modification’ to exclude from that definition, for a lessee, a change that solely results in a lease liability (or a part of it) being extinguished in accordance with IFRS 9 (see Appendix A to this paper). In our view, this proposed amendment is in line with the preliminary view we previously discussed with the Committee.

Potential amendments to Illustrative Example 19 accompanying IFRS 16

19. Paragraph B3.3.1 of IFRS 9 states:

A financial liability (or part of it) is extinguished when the debtor either:

- (a) discharges the liability (or part of it) by paying the creditor, normally with cash, other financial assets, goods or services; or
- (b) is legally released from primary responsibility for the liability (or part of it) either by process of law or by the creditor. (If the debtor has given a guarantee this condition may still be met.)

20. In the fact pattern in Illustrative Example 19 (reproduced in Appendix B to this paper), at the beginning of year 6 of a 10-year lease, a lessee and a lessor agree to amend the lease contract for the remaining five years to reduce the lease payments from CU100,000 per year to CU95,000 per year—a reduction of CU5,000 per year. No other changes are made to the lease contract.
21. For the lessee's lease liability in that example, the requirements in paragraph B3.3.1 of IFRS 9 for extinguishment of that liability have not been met. For the CU5,000—the reduction per year in lease payments under the lease contract—the lessee has not discharged that liability by paying the lessor, and therefore paragraph B3.3.1(a) has not been met. The lessor has not legally released the lessee from primary responsibility for that liability, and therefore paragraph B3.3.1(b) has not been met. Instead, the change to consideration under the lease contract is a lease modification applying IFRS 16, as illustrated in that example.
22. If we consider our recommended amendment to the definition of a lease modification as described in paragraph 18 of this paper, the change in lease consideration illustrated in Illustrative Example 19 would continue to be a lease modification. The change in lease consideration in that example does not solely result in the lessee's lease liability (or a part of it) being extinguished in accordance with IFRS 9. We therefore recommend retaining Illustrative Example 19 as it is currently written.

Potential amendments to IFRS 9

23. Paragraph 2.1(b)(ii) of IFRS 9 states that ‘lease liabilities recognised by a lessee are subject to the derecognition requirements in paragraph 3.3.1’ of IFRS 9.
24. Paragraph 3.3.1 of IFRS 9 states that ‘an entity shall remove a financial liability (or a part of a financial liability) from its statement of financial position when, and only when, it is extinguished ...’.
25. Paragraph 3.3.3 of IFRS 9 states that [emphasis added] ‘the difference between the carrying amount of a financial liability (or part of a financial liability) extinguished ... and the consideration paid, including any non-cash assets transferred or liabilities assumed, *shall be recognised in profit or loss*’.
26. As we stated in paragraph 51 of [Agenda Paper 4](#) for the March 2022 meeting, we would expect that a lessee that has applied paragraph 3.3.1 of IFRS 9 would apply paragraph 3.3.3 of IFRS 9 to determine the amount to be recognised in profit or loss. In our view, the IASB intended a lessee to apply, in sequence, paragraphs 3.3.1 and 3.3.3 of IFRS 9, and the lack of a cross-reference to paragraph 3.3.3 in paragraph 2.1(b)(ii) of IFRS 9 was an oversight.
27. We therefore recommend, as suggested by some Committee members, to amend paragraph 2.1(b)(ii) of IFRS 9 to add a cross-reference to paragraph 3.3.3 of IFRS 9 (see Appendix A to this paper).

Does this matter meet the annual improvements criteria?

28. Paragraphs 6.10–6.13 of the [Due Process Handbook](#) include the criteria for annual improvements. To meet these criteria, the proposed solution would need to be limited to:
 - (a) clarifying the wording in an Accounting Standard, which involves either replacing unclear wording in existing Accounting Standards or providing requirements where an absence of requirements is causing concern; or

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- (b) correcting relatively minor unintended consequences, oversights or conflicts between existing requirements.
29. In our view, our proposed solution to amend the definition of ‘lease modification’ in Appendix A to IFRS 16 and to amend paragraph 2.1(b)(ii) of IFRS 9 to add a cross-reference to paragraph 3.3.3 of IFRS 9 (see Appendix A to this paper) meets these criteria. Such amendments would:
- (a) efficiently resolve the conflict between the derecognition requirements in IFRS 9 and the lease modification requirements in IFRS 16 that arise when a lessee accounts for the rent concession in the submitted fact pattern;
 - (b) correct an unintended oversight in cross-referencing between paragraphs within IFRS 9 and resolve potential confusion for a lessee applying the derecognition requirements in IFRS 9; and
 - (c) not propose a new principle or change an existing principle.

Summary of staff preliminary views

30. Based on our staff analysis, our preliminary views are:
- (a) to propose that the IASB amend the definition of ‘lease modification’ in Appendix A to IFRS 16;
 - (b) to propose that the IASB amend paragraph 2.1(b)(ii) of IFRS 9 to add a cross-reference to paragraph 3.3.3 of IFRS 9; and
 - (c) to include these proposed amendments (see Appendix A to this paper) in the next annual improvements cycle.

Question for the Committee

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Do Committee members agree with our preliminary views as summarised in paragraph 30 of this paper? If 'no', do you have any other suggestions?

Appendix A—recommended proposed amendments to IFRS 9 and IFRS 16

Proposed amendment to IFRS 9

- A1. Our proposed amendment to paragraph 2.1(b)(ii) of IFRS 9 would add a cross-reference to paragraph 3.3.3 of IFRS 9. New text is underlined.

2.1 This Standard shall be applied by all entities to all types of financial instruments except:

...

(b) rights and obligations under leases to which IFRS 16 *Leases* applies. However:

...

(ii) lease liabilities recognised by a lessee are subject to the derecognition requirements in paragraphs 3.3.1 and 3.3.3 of this Standard; and

...

Proposed amendment to Appendix A to IFRS 16

- A2. Our proposed amendment to the definition of ‘lease modification’ in Appendix A to IFRS 16 would exclude from that definition, for a lessee, a change that solely results in a lease liability (or a part of it) being extinguished in accordance with IFRS 9. New text is underlined.

lease modification

A change in the scope of a **lease**, or the consideration for a lease, that was not part of the original terms and conditions of the lease (for example, adding or terminating the right to use one or more **underlying assets**, or extending or shortening the contractual **lease term**). For a lessee, a change

that results solely in a lease liability (or a part of it) being extinguished in accordance with IFRS 9 is not a lease modification.

Appendix B—Illustrative Example 19 accompanying IFRS 16

- B1. The text of Illustrative Example 19 accompanying IFRS 16 is reproduced below for reference.

Example 19—Modification that is a change in consideration only

Lessee enters into a 10-year lease for 5,000 square metres of office space. At the beginning of Year 6, Lessee and Lessor agree to amend the original lease for the remaining five years to reduce the lease payments from CU100,000 per year to CU95,000 per year. The interest rate implicit in the lease cannot be readily determined. Lessee's incremental borrowing rate at the commencement date is 6 per cent per annum. Lessee's incremental borrowing rate at the beginning of Year 6 is 7 per cent per annum. The annual lease payments are payable at the end of each year.

At the effective date of the modification (at the beginning of Year 6), Lessee remeasures the lease liability based on: (a) a five-year remaining lease term, (b) annual payments of CU95,000 and (c) Lessee's incremental borrowing rate of 7 per cent per annum. Lessee recognises the difference between the carrying amount of the modified liability (CU389,519) and the lease liability immediately before the modification (CU421,236) of CU31,717 as an adjustment to the right-of-use asset.