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Exposure Draft ED/2020/2

Covid-19-Related Rent Concessions

Proposed amendment to IFRS 16

Comments to be received by 8 May 2020

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 IFRS[®]

Exposure Draft

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Exposure Draft ED/2020/2 *Covid-19-Related Rent Concessions* is published by the International Accounting Standards Board (Board) for comment only. Comments need to be received by 8 May 2020 and should be submitted by email to commentletters@ifrs.org or online at <https://www.ifrs.org/projects/open-for-comment/>.

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Introduction

Why is the Board publishing this Exposure Draft?

The International Accounting Standards Board (Board) has been informed that many lessors around the world have provided, or are expected to provide, rent concessions to lessees as a result of the covid-19 pandemic. Such rent concessions are particularly prevalent for leases of retail property and, in some cases, are encouraged or required by governments or jurisdictional authorities. Rent concessions include rent holidays or rent reductions for a period of time, possibly followed by increased rent payments in future periods.

IFRS 16 *Leases* contains requirements that specify the accounting for changes in lease payments, including rent concessions. However, the Board has been informed that applying those requirements to a potentially large volume of covid-19-related rent concessions could be practically difficult, especially in the light of the many challenges stakeholders face during the pandemic. In particular, lessees have identified potential difficulties in the current environment in assessing whether covid-19-related rent concessions are lease modifications and, for those that are, applying the required accounting.

In addition, many lessees are currently preparing their first annual financial statements applying IFRS 16. Any complexity arising as a result of the covid-19 pandemic therefore adds to the work being undertaken in implementing the new lessee accounting model in IFRS 16.

The objective of the proposal in this Exposure Draft is to provide lessees with practical relief during the covid-19 pandemic while enabling them to continue providing useful information about their leases to users of financial statements.

Proposal in this Exposure Draft

The Exposure Draft proposes an amendment to IFRS 16 to permit lessees, as a practical expedient, not to assess whether particular covid-19-related rent concessions are lease modifications. Instead, lessees that apply the practical expedient would account for those rent concessions as if they were not lease modifications. The Exposure Draft proposes no change for lessors.

Who would be affected by the proposal?

The proposal in this Exposure Draft would affect lessees that are granted rent concessions as a direct consequence of the covid-19 pandemic during 2020, and users of these lessees' financial statements.

Next step

The Board will consider the comments that it receives on the proposal in this Exposure Draft and will decide whether to proceed with the proposed amendment. The Board plans to complete any resulting amendment to IFRS 16 by the end of May 2020.

Invitation to comment

The Board invites comments on the proposal in this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

- (a) address the questions as stated;
- (b) indicate the specific paragraph(s) to which they relate;
- (c) contain a clear rationale;
- (d) identify any wording in the proposal that is difficult to translate; and
- (e) include any alternative the Board should consider, if applicable.

The Board is requesting comments only on matters addressed in this Exposure Draft.

Questions for respondents

Question 1—Practical expedient (paragraphs 46A and 46B of the [Draft] amendment to IFRS 16)

Paragraph 46A of the draft amendment to IFRS 16 proposes, as a practical expedient, that a lessee may elect not to assess whether a covid-19-related rent concession is a lease modification. A lessee that makes this election would account for any change in lease payments resulting from the covid-19-related rent concession the same way it would account for the change applying IFRS 16 if the change were not a lease modification.

Paragraph 46B of the draft amendment to IFRS 16 proposes that the practical expedient applies only to rent concessions occurring as a direct consequence of the covid-19 pandemic and only if all of the following conditions are met:

- (a) the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change;
- (b) any reduction in lease payments affects only payments originally due in 2020; and
- (c) there is no substantive change to other terms and conditions of the lease.

Do you agree that this practical expedient would provide lessees with practical relief while enabling them to continue providing useful information about their leases to users of financial statements? Why or why not? If you disagree with the proposal, please explain what you propose and why.

Question 2—Effective date and transition (paragraphs C1A and C20A of the [Draft] amendment to IFRS 16)

Paragraphs C1A and C20A of the draft amendment to IFRS 16 propose that a lessee would apply the amendment:

- (a) for annual reporting periods beginning on or after 1 June 2020. Earlier application is permitted, including in financial statements not yet authorised for issue at the date the amendment is issued; and
- (b) retrospectively, recognising the cumulative effect of initially applying the amendment as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the beginning of the annual reporting period in which the lessee first applies the amendment.

Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you propose and why.

Deadline

The Board will consider all written comments received by **8 May 2020** (14 days).

How to comment

The IFRS Foundation's offices are closed temporarily in line with government measures to stem the coronavirus pandemic. However, we are working and will consider your views in finalising this proposed amendment. Please submit your comments electronically.

Online <https://www.ifrs.org/projects/open-for-comment/>
By email commentletters@ifrs.org

Your comments will be on the public record and posted on our website unless you request confidentiality and we grant your request. We do not normally grant such requests unless they are supported by a good reason, for example, commercial confidence. Please see our website for details on this policy and on how we use your personal data.

[Draft] Amendment to IFRS 16 Leases

Paragraphs 46A, 46B, 60A, C1A and C20A are added. A new heading is added before C20A. For ease of reading these paragraphs have not been underlined.

Lessee

...

Measurement

...

Subsequent measurement

...

Lease modifications

...

46A As a practical expedient, a lessee may elect not to assess whether a covid-19-related rent concession (see paragraph 46B) is a lease modification. A lessee that makes this election shall account for any change in lease payments resulting from the covid-19-related rent concession the same way it would account for the change applying this Standard if the change were not a lease modification.

46B The practical expedient in paragraph 46A applies only to rent concessions occurring as a direct consequence of the covid-19 pandemic and only if all of the following conditions are met:

- (a) the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change;
- (b) any reduction in lease payments affects only payments originally due in 2020 (for example, a rent concession would meet this condition if it results in reduced lease payments in 2020 and increased lease payments that extend beyond 2020); and
- (c) there is no substantive change to other terms and conditions of the lease.

...

Disclosure

...

60A A lessee that applies the practical expedient in paragraph 46A shall disclose that fact.

Appendix C

Effective date and transition

Effective date

...

- C1A [Draft] *Covid-19-Related Rent Concessions*, issued in [Month] 2020, added paragraphs 46A, 46B and 60A. A lessee shall apply that amendment for annual reporting periods beginning on or after 1 June 2020. Earlier application is permitted, including in financial statements not yet authorised for issue at [date the amendment is issued].

Transition

...

Covid-19-related rent concessions for lessees

- C20A A lessee shall apply [Draft] *Covid-19-Related Rent Concessions* (see paragraph C1A) retrospectively, recognising the cumulative effect of initially applying that amendment as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the beginning of the annual reporting period in which the lessee first applies the amendment.

Approval by the Board of Exposure Draft *Covid-19-Related Rent Concessions* published in April 2020

The Exposure Draft *Covid-19-Related Rent Concessions*, which proposes an amendment to IFRS 16, was approved for publication by all 14 members of the International Accounting Standards Board.

Hans Hoogervorst Chairman

Suzanne Lloyd Vice-Chair

Nick Anderson

Tadeu Cendon

Martin Edelmann

Françoise Flores

Gary Kabureck

Jianqiao Lu

Darrel Scott

Thomas Scott

Chungwoo Suh

Rika Suzuki

Ann Tarca

Mary Tokar

Basis for Conclusions on Exposure Draft *Covid-19-Related Rent Concessions*

This Basis for Conclusions accompanies, but is not part of, the Exposure Draft Covid-19-Related Rent Concessions. It summarises the considerations of the International Accounting Standards Board (Board) when developing the Exposure Draft. Individual Board members gave greater weight to some factors than to others.

Background

- BC1 IFRS 16 *Leases* sets out requirements for how to account for changes in lease payments during the term of a lease. The Standard contains specific requirements for some changes in lease payments—for example, those arising from changes in an index or rate used to determine lease payments. Otherwise the accounting IFRS 16 requires for a change in lease payments depends on whether that change meets the definition of a lease modification. IFRS 16 defines a lease modification as 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. If a change in lease payments results from a lease modification, then unless the change meets particular criteria to be accounted for as a separate lease, a lessee is required to remeasure the lease liability by discounting the revised lease payments using a revised discount rate.
- BC2 Many lessors have provided, or are expected to provide, rent concessions to lessees as a result of the covid-19 pandemic. The Board understands that lessees may have difficulty assessing whether a potentially large volume of covid-19-related rent concessions are lease modifications and, for those that are, applying the required accounting in IFRS 16, especially in the light of the many challenges entities face during the pandemic.
- BC3 The proposal in this Exposure Draft provides lessees with a practical expedient in accounting for particular covid-19-related rent concessions. The proposal does not address lessor accounting because lessors are not expected to face the same practical challenges as lessees in accounting for covid-19-related rent concessions. For many lessors with a large volume of leases, leasing is a core part of their business. In addition, the consequences for users of a lessor's financial statements are different from those for a lessee. In particular:
- (a) IFRS 16 carried forward the lessor accounting model in IAS 17 *Leases*. Therefore, unlike lessees, lessors have not recently implemented a new accounting model for their leases.
 - (b) Lessor accounting for modifications to operating leases requires no remeasurement of amounts recognised in a lessor's statement of financial position, whereas lessees are required to remeasure lease liabilities using a revised discount rate for all lease modifications. Many of the real estate leases for which covid-19-related rent concessions are being provided would be operating leases for the lessor.

- (c) In the case of a finance lease, lessors apply the requirements in IFRS 9 *Financial Instruments* to modifications. The information this accounting provides is considered useful for users of a lessor's financial statements and is consistent with the required accounting for other financial instruments in the scope of IFRS 9.

Proposed amendment to IFRS 16

- BC4 The proposal in this Exposure Draft permits lessees, as a practical expedient, not to assess whether particular covid-19-related rent concessions are lease modifications and, instead, account for those rent concessions as if they were not lease modifications. Lessees would apply the practical expedient consistently to contracts with similar characteristics and in similar circumstances, as already specified by paragraph 2 of IFRS 16. In the Board's view, this practical expedient would relieve lessees of the practical challenges described in paragraph BC2 while enabling lessees to continue providing useful information about their leases to users of financial statements.
- BC5 The Board was mindful of the risk of the practical expedient being applied too broadly, which could result in unintended consequences. Therefore, the Board is proposing to limit the scope of the practical expedient so that it applies only to rent concessions that occur as a direct consequence of the covid-19 pandemic and:
- (a) result in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change. The Board is of the view that a change that results in more than an insubstantial increase in total payments for the lease could not result solely from a covid-19-related rent concession (as described in this Exposure Draft), except to the extent the increase reflects the time value of money.
 - (b) reduce only lease payments originally due in 2020. A related increase in lease payments that extends beyond 2020 would not prevent a rent concession from meeting this condition. In contrast, if reductions in lease payments extend beyond 2020, the rent concession would not be within the scope of the practical expedient. In developing this condition, the Board observed that the economic effects of the covid-19 pandemic could continue for some time. If the practical expedient is not limited to a particular timeframe, a lessee could conclude that many future changes to lease payments are a result of the covid-19 pandemic. Limiting the practical expedient to reductions in lease payments originally due in 2020 provides relief to lessees when they are expected to need it most, while avoiding lessees applying the exemption beyond when it is needed.
 - (c) there is no substantive change to other terms and conditions of the lease. This condition reflects the Board's view that lessees should not apply the practical expedient to lease modifications that are unrelated to the covid-19 pandemic but are negotiated at the same time as a covid-19-related rent concession (although, for example, a three-month

rent holiday in 2020 followed by three additional months of substantially equivalent payments at the end of the lease would not prevent a rent concession from being within the scope of the practical expedient).

- BC6 The practical expedient is a departure from the requirements in IFRS 16 and is proposed only to provide lessees with practical relief during the covid-19 pandemic. The Board decided that lessees should not be required to depart from the requirements in IFRS 16—some lessees (for example, those with systems to address changes in lease payments) may prefer to apply the existing requirements to all changes in lease contracts throughout the pandemic. The Board therefore proposes to permit, but not require, a lessee to apply the practical expedient. As described in paragraph BC4, if a lessee chooses to apply the practical expedient to a lease, it would apply the practical expedient consistently to all lease contracts with similar characteristics and in similar circumstances.

The effects on information provided to users of financial statements

- BC7 The Board considered the accounting for changes in lease payments applying the practical expedient for three types of change:
- (a) A lessee applying the practical expedient would generally account for a forgiveness or waiver of lease payments as a variable lease payment applying paragraph 38 of IFRS 16. The lessee would also make a corresponding adjustment to the lease liability—in effect, derecognising the part of the lease liability that has been extinguished by the forgiveness or waiver of lease payments.
 - (b) A change in lease payments that reduces payments in one period but proportionally increases payments in another does not extinguish the lessee’s lease liability or change the consideration for the lease—instead, it changes only the timing of individual payments. In this case, a lessee would continue to reduce the lease liability for payments made to the lessor applying paragraph 36(b) of IFRS 16.
 - (c) Some covid-19-related rent concessions reduce lease payments, incorporating both a forgiveness of payments and a change in the timing of payments.
- BC8 The Board observed that the lease liability recognised by a lessee applying the practical expedient would represent the present value of future lease payments owing to the lessor. In the Board’s view, this accounting provides a faithful representation of a lessee’s obligations under the lease contract, so lessees applying the practical expedient would provide useful information to users of financial statements.
- BC9 The proposal in this Exposure Draft could however affect comparability between lessees that apply the practical expedient and those that do not. Notably, the effects of covid-19-related rent concessions on a lessee’s right-of-use asset and profit or loss could differ depending on whether a lessee applies

the practical expedient. For example, a lessee applying the practical expedient would generally recognise the effects of forgiveness of lease payments in profit or loss in the period in which the event or condition that triggers that forgiveness occurs. A lessee applying the lease modification requirements would, instead, make an adjustment to the carrying amount of the right-of-use asset and generally recognise the effects of the rent concession through depreciation of the right-of-use asset. This potential loss of comparability might be somewhat mitigated because the circumstances giving rise to covid-19-related rent concessions are likely to indicate that right-of-use assets may be impaired. Any impairment would reduce the potential difference between accounting—or not accounting—for a rent concession as a lease modification.

- BC10 Recognising the possible effects of the practical expedient on comparability, the Board decided to propose that a lessee that applies the exemption should disclose that fact. A lessee is also required to apply the other disclosure requirements in IFRS 16 and other IFRS Standards, such as IAS 1 *Presentation of Financial Statements*, in providing useful information to users of financial statements about the lessee's leasing activities.

Transition and effective date

- BC11 Lessees were already facing challenges as a result of the covid-19 pandemic when the Board developed the proposal in this Exposure Draft. Acknowledging the urgency of the matter, the Board proposes an effective date of annual reporting periods beginning on or after 1 June 2020, with earlier application permitted. By choosing to apply the amendment early, lessees would be able to apply the practical expedient immediately in any set of financial statements not yet authorised for issue at the date the amendment is issued. However, by setting the effective date for annual reporting periods beginning on or after 1 June 2020 the Board is enabling, rather than requiring, immediate application—thereby ensuring lessees have the opportunity to obtain the information needed if they wish to apply the practical expedient.
- BC12 The Board also proposes to require lessees to apply the amendment retrospectively. The scope of the practical expedient (see paragraph BC5) means that retrospective application would not capture rent concessions that affect payments due before January 2020. However, retrospective application may benefit lessees that authorise annual or interim financial statements for issue after receiving covid-19-related rent concessions but before the amendment is issued. For example, a lessee that does not apply the practical expedient in its 31 March 2020 financial statements would be able to apply the amendment retrospectively to particular covid-19-related rent concessions that affect payments due before 31 March 2020 in its 31 March 2021 financial statements, thus accounting for similar covid-19-related rent concessions consistently. Retrospective application would also benefit lessees applying the practical expedient during their first year of applying IFRS 16. For example, a lessee that applies IFRS 16 retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* and applies the practical

expedient to covid-19-related rent concessions would not determine a revised discount rate for those leases. Instead, the lessee would use a discount rate determined as if IFRS 16 had always been applied (for example, a rate determined at the commencement date).

- BC13 Nonetheless, restatement of comparative information would provide little benefit, and requiring this may be costly for lessees. The Board therefore proposes to require lessees to recognise the cumulative effect of initially applying the amendment as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at the beginning of the annual reporting period in which the lessee first applies the amendment.



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