IFRS Accounting

Staff paper

Agenda reference: 12D

IASB® meeting

Date	**October 2022**
Project	**Lessor Forgiveness of Lease Payments (IFRS 9 and IFRS 16)**
Topic	**Finalisation of agenda decision**
Contacts	**Jenifer Minke-Girard** (jminke-girard@ifrs.org)

Purpose of meeting

1. At its September 2022 meeting, the IFRS Interpretations Committee (Committee) decided not to add a standard-setting project to the work plan in response to a request on Lessor Forgiveness of Lease Payments (IFRS 9 *Financial Instruments* and IFRS 16 *Leases*). The Committee instead decided to finalise an agenda decision.

2. The purpose of this meeting is to ask International Accounting Standards Board (IASB) members whether they object to the agenda decision, as required by paragraph 8.7 of the IFRS Foundation *Due Process Handbook*.

Background

3. The Committee received a request about a lessor's application of IFRS 9 and IFRS 16 in accounting for a particular rent concession. The rent concession is one for which the only change to the lease contract is the lessor's forgiveness of lease payments due from the lessee under that contract. The request asked:

    a. how the lessor applies the expected credit loss (ECL) model in IFRS 9 to the operating lease receivable before the rent concession is granted if it expects to forgive payments due from the lessee under the lease contract; and

    b. whether the lessor applies the derecognition requirements in IFRS 9 or the lease modification requirements in IFRS 16 in accounting for the rent concession.

4. In March 2022, the Committee discussed the request and decided to publish a tentative agenda decision, having concluded that the principles and requirements in IFRS Accounting Standards provide an adequate basis for a lessor to determine how to apply the ECL model in IFRS 9 to an operating lease receivable and account for the rent concession described in the request.

Overview of the feedback on the tentative agenda decision

5. The Committee received 23 comment letters on its tentative agenda decision by the comment deadline.

6. As reported in Agenda Paper 4 for the Committee's September 2022 meeting, seven respondents agreed with all the Committee's analysis and conclusions for the reasons explained in the tentative agenda decision. Four respondents agreed with aspects of the Committee's analysis and conclusions and requested clarification about other aspects or raised additional questions they suggested the Committee analyse.

7. Eleven respondents disagreed with some or all of the Committee's analysis and conclusions. These respondents said:

    a. they either (i) disagree with the approach described in the tentative agenda decision for application of the ECL model to the operating lease receivable in the fact pattern described; or (ii) view that approach as only one possible interpretation of IFRS 9;

    b. on the date a rent concession is granted, it remains unclear whether IFRS 9 or IFRS 16 takes precedence;

    c. the tentative agenda decision is not persuasive in concluding that forgiven lease payments recognised as an operating lease receivable are not accrued lease payments or lease incentives applying IFRS 16; and

    d. the conclusions in the tentative agenda decision could affect a wider population of transactions than the narrow fact pattern submitted.

8. One respondent did not express a view on the Committee's technical analysis and conclusions and asked for clarity about the application of the ECL model in IFRS 9.

9. Some respondents suggested that, rather than publishing an agenda decision, the Committee ask the IASB to either (a) consider the questions as part of the post-implementation review (PIR) of IFRS 9's impairment requirements or the PIR of IFRS 16; or (b) undertake a standard-setting project to address the questions submitted.

10. At its September 2022 meeting, the Committee considered the feedback and staff analysis of that feedback. The Committee affirmed its technical analysis and conclusions in the tentative agenda decision on the lessor's application of IFRS 9 and IFRS 16 to the rent concession in the fact pattern described. The Committee discussed wording in the agenda decision that clarifies that the rent concession described is one for which the only change to the lease contract is the lessor's forgiveness of lease payments due from the lessee under that contract—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.

11. Ten of the 14 Committee members voted to finalise the agenda decision.

12. The appendix to this paper includes the wording of the agenda decision approved by the Committee.

Questions for the IASB

Do you object to the Committee’s:

(a) decision not to add a standard-setting project to the work plan; or

(b) conclusion that the agenda decision does not add or change requirements in IFRS Accounting Standards?

Appendix—The Agenda Decision

A1. The Agenda Decision below was approved by the Committee at its meeting in September 2022.

Lessor Forgiveness of Lease Payments (IFRS 9 *Financial Instruments* and IFRS 16 *Leases*)

The Committee received a request about a lessor's application of IFRS 9 and IFRS 16 in accounting for a particular rent concession. The rent concession is one for which the only change to the lease contract is the lessor's forgiveness of lease payments due from the lessee under that contract.

The fact pattern

The request 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 classified by the lessor—applying IFRS 16—as an operating lease. The lessor legally releases the lessee from its obligation to make specifically identified lease payments:

a. some of these lease payments are amounts contractually due but not paid. Paragraph AG9 of IAS 32 states that 'a lessor does not regard an operating lease as a financial instrument, except as regards individual payments currently due and payable by the lessee'. Therefore, the lessor has recognised these amounts as an operating lease receivable. Applying paragraph 81 of IFRS 16, the lessor has also recognised the amounts as income.

b. some of these lease payments are not yet contractually due.

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. Before the date the rent concession is granted, the lessor applies the expected credit loss model in IFRS 9 to the operating lease receivable.

The question

The request asked:

a. how the lessor applies the expected credit loss model in IFRS 9 to the operating lease receivable before the rent concession is granted if it expects to forgive payments due from the lessee under the lease contract; and

b. whether the lessor applies the derecognition requirements in IFRS 9 or the lease modification requirements in IFRS 16 in accounting for the rent concession.

Applying the expected credit loss model in IFRS 9 to the operating lease receivable

Paragraph 2.1(b)(i) of IFRS 9 states that 'operating lease receivables recognised by a lessor are subject to the derecognition and impairment requirements' in IFRS 9. Therefore, a lessor is required to apply the impairment requirements in IFRS 9 to the gross carrying amount of an operating lease receivable from the date on which it recognises that receivable, taking into account applicable derecognition requirements in IFRS 9.

IFRS 9 defines credit loss as 'the difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (ie all cash shortfalls)…'. Paragraph 5.5.17 of IFRS 9 states that 'an entity shall measure expected credit losses … in a way that reflects (a) an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes; (b) the time value of money; and (c) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions'.

Consequently, in the fact pattern described in the request, the lessor applies the impairment requirements in IFRS 9 to the operating lease receivable. The lessor estimates expected credit losses on the operating lease receivable by measuring any credit loss to reflect 'all cash shortfalls'. These shortfalls are the difference between:

a. all contractual cash flows due to the lessor in accordance with the lease contract (and included in the gross carrying amount of the operating lease receivable); and

b. all the cash flows the lessor expects to receive, determined using 'reasonable and supportable information' about 'past events, current conditions and forecasts of future economic conditions'.

Therefore, the Committee concluded that, before the rent concession is granted, the lessor measures expected credit losses on the operating lease receivable in a way that reflects 'an unbiased and probability-weighted amount …', 'the time value of money', and 'reasonable and supportable information …' (as required by paragraph 5.5.17 of IFRS 9). This measurement of expected credit losses includes the lessor considering its expectations of forgiving lease payments recognised as part of that receivable.

Accounting for the rent concession—IFRS 9 and IFRS 16

Applying the derecognition requirements in IFRS 9 to the operating lease receivable

Paragraph 2.1(b)(i) of IFRS 9 states that operating lease receivables recognised by a lessor are subject to the derecognition requirements in IFRS 9. Consequently, on granting the rent concession, the lessor considers whether the requirements for derecognition in paragraph 3.2.3 of IFRS 9 are met.

In the rent concession described in the request, the lessor legally releases the lessee from its obligation to make specifically identified lease payments, some of which the lessor has recognised as an operating lease receivable. Accordingly, on granting the rent concession, the lessor concludes that the requirements in paragraph 3.2.3(a) of IFRS 9 have been met—that is, its contractual rights to the cash flows from the operating lease receivable expire—because it has agreed to legally release the lessee from its obligation and thus has given up its contractual rights to those specifically identified cash flows. Therefore, on the date the rent concession is granted, the lessor remeasures expected credit losses on the operating lease receivable (and recognises any change to the expected credit loss allowance in profit or loss) and derecognises the operating lease receivable (and associated expected credit loss allowance).

Applying the lease modification requirements in IFRS 16 to future lease payments under the lease

The rent concession described in the request meets the definition of a lease modification in IFRS 16. The rent concession is 'a change in … the consideration for a lease … that was not part of the original terms and conditions of the lease'. Therefore, the lessor applies paragraph 87 of IFRS 16 and accounts for the modified lease as a new lease from the date the rent concession is granted.

Paragraph 87 of IFRS 16 requires a lessor to consider any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease. The Committee observed that lease payments contractually due from the lessee that the lessor has recognised as an operating lease receivable (to which the derecognition and impairment requirements in IFRS 9 apply) are not accrued lease payments. Consequently, neither those lease payments nor their forgiveness are considered—applying paragraph 87 of IFRS 16—as part of the lease payments for the new lease.

In accounting for the modified lease as a new lease, a lessor applies paragraph 81 of IFRS 16 and recognises the lease payments (including any prepaid or accrued lease payments relating to the original lease) as income on either a straight-line basis or another systematic basis.

The Committee concluded that the lessor accounts for the rent concession described in the request on the date it is granted by applying: (a) the derecognition requirements in IFRS 9 to forgiven lease payments that the lessor has recognised as an operating lease receivable; and (b) the lease modification requirements in IFRS 16 to forgiven lease payments that the lessor has not recognised as an operating lease receivable.

Conclusion

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. Consequently, the Committee decided not to add a standard-setting project to the work plan.