

To
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom
May 8th, 2020

Submitted electronically

Dear Sir/Madam

Subject: Exposure Draft on Covid-19-Related Rent Concessions: Proposed amendment to IFRS 16

I am pleased to respond to the call for comments on the Exposure Draft on Covid-19-Related Rent Concessions: Proposed amendment to IFRS 16.

I appreciate the IASB's efforts 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.

I thank you for the opportunity to provide comments on this exposure draft. Please do not hesitate to contact me should you wish to discuss any of my comments.

Yours sincerely,

Srivatsan Lakshminarayan
Professor of Accounting and Finance,
Centre for Financial Studies (CFS),
SPJIMR School of Management, Mumbai, India.
srivatsan.lakshminarayan@spjimr.org

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.

1. The condition imposed under para. 46B (b) restricts the benefit of the practical expedient to “payments originally due in 2020”. BC5(b) confirms that “if reductions in lease payments extend beyond 2020, the rent concession would not be within the scope of the practical expedient” and justifies this limitation on the basis of the need criterion i.e. when lessees “are expected to need it most”. It is not sufficiently evident that a concession that provides immediate relief over (say) two quarters within 2020 is better qualified to satisfy the need criterion compared to a concession of the same magnitude that staggers this relief over four quarters spread over 2020 and 2021, particularly if the latter arrangement is negotiated as mutually desirable from the cashflow standpoint of the lessor and lessee. So long as rent concessions arise as a direct consequence of the pandemic (already envisaged within 46B) the time restriction of 2020 appears impractical and

should be suitably modified. An alternative approach may be to limit the practical expedient to rent concessions **agreed** (instead of **originally due**) in 2020 or up to some reasonable date in 2021. This is also important to avoid having to re-visit amendments to IFRS 16 again due to situational developments during the remainder of 2020.

2. In the interest of comparability of financial statements (cross-border and within jurisdictions), it is submitted that paragraph 46A be either made mandatorily applicable or re-drafted as the preferred option for lessees instead of providing unqualified optionality as currently proposed in the Exposure Draft. Notwithstanding the undesirable connotation and on the assumption that a precedent is being set here (for future Covid-19 type situations e.g. pandemics, natural disasters etc., where consistent responses would be expected), the Board should be attentive to limiting options when undertaking IFRS amendments established through time-curtailed, rapid due-process exercises. Since balance sheet differences arising from the lessees' choice of options may, both, differ materially and persist, the lingering effects on leverage and other key financial metrics can be better obviated through convergence in treatment of rent concessions. This is particularly likely when the choice of lease modification accounting is not accompanied by impairment of Right of Use Assets as envisaged under BC9. This may be the case where for e.g. it is reasonably estimated that foregone benefits can probably be recouped through intensive use of leased assets in future. Material differences arising from current accounting choices (practical expedient vs modification accounting) may not be adequately appreciated upon a reading of financial statements in future periods when accompanying disclosures are either no longer required/available. Further, any requirement to enhance comparability of financial statements now between lessees who opt for the practical expedient and lessees who do not, will require additional current disclosures by the former category of lessees. This would have the consequence of undoing some of the benefits intended by the proposed amendments to IFRS 16.

3. Irrespective of optionality, it is submitted to the Board that lessees must not be allowed to choose to selectively account for rent concessions under some contracts through the practical expedient envisaged in this ED, while accounting for other concessions as modifications of original contracts. Therefore, where lessees opt to apply the practical expedient (or if it were made a preferred option as recommended in this comment letter), all rent concessions arising directly from Covid-19 and meeting the conditions specified in the proposed amendment to IFRS 16 must be accounted for using the practical expedient.

4. Based upon a reading of proposed paragraph 46B(a) with Basis for Conclusions BC7(a) and BC7(b), it is submitted that clarity in drafting be undertaken. Thus:

The conditionality in 46B(a) is confusing to the extent it pertains to situations in which changes in lease payment schedules result “in revised consideration...that **is substantially the same**”. This would most likely be covered by the situation contemplated in BC7(b) i.e. “change in lease payments” that result in offsetting inter-temporal adjustments over the period of the lease. The practical expedient in this Exposure Draft is primarily beneficial in cases where rent concessions take the form of waivers and/or forgiveness as opposed to deferrals or inter-period catch-up adjustments. In the latter case, since the accounting treatment would go through para. 36(b) of IFRS 16, it is not evident from the ED that the benefits of practical expedients apply, either through the need to avoid re-calculating lease liability (and right-of-use asset) or through beneficial effects on current period income statements. Consequently, a redrafting of 46B(a) may be undertaken to restrict reference to situations in which the revised consideration for the lease is **less (substantially or otherwise)** than the lease consideration preceding the change i.e. substantially representative of a rent concession as per the focus of this ED.

5. It is submitted that the conditionalities in 46B should be modified to explicitly specify that the scope of concessions **include** those arising either by voluntary contractual re-negotiation or through the impact of government policy action. Given the international reach of IFRS, such a

clarification will better accommodate the range of situations through which rent concessions are likely to affect lessees. This is also consistent with the original intent of the proposed amendment to IFRS 16 as outlined in para. 13(b) in Agenda Reference 32B (April 2020) to grant relief to lessees from assessments related to whether a proposed concession is a lease modification:

the assessment (of rent concessions during the pandemic) itself might be difficult. For example, a lease contract or applicable law or regulation may contain clauses, such as force majeure, which were developed without contemplating the covid-19 pandemic. It may be difficult to determine whether rent concessions offered—or mandated by government—are captured by the operation of such clauses.

6. With regard to disclosures under proposed para. 60A, it is submitted that the following additional aspects should be considered:

1. Where the rent concession pertains to a variable lease payment (dependant on an index or a rate or otherwise), the lessee should disclose this separately from concessions in normal lease payments. This would apply in cases where the waiver or forgiveness arises due to concessions from variable lease payments that the lessee would otherwise have been required to make under normal conditions.
2. In view of the recent transition of operating lease accounting to the Balance Sheet approach under IFRS 16, it is submitted that it may benefit future standard-setting by **recommending** that lessees quantify and disclose the effect of applying the practical expedient under para. 46A on leases that would otherwise have been recognized as operating leases, had the transition to IFRS 16 not been required. To the extent that the proposed amendment to IFRS 16 itself anticipates the fundamentally differing nature of relationship between lessors and lessees between operating and non-operating leases, such disclosures may highlight systemic differences that the Board may want to consider in future amendments to standard-setting on Leases.

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.

7. Regarding para. C1A relating to effective date, it is submitted that the draft be suitably reworded. At present the requirement that “A lessee shall apply that amendment for annual reporting periods beginning on or after 1 June 2020” is not sufficiently clear. If the intent is to ensure that the effect of the practical expedient should reflect in interim and annual financial statements authorized for publication on/after June 1, 2020 (as seems to be obvious), then this needs to be made clear and unambiguous.