

IN BRIEF

IFRS 16 Amendment COVID-19-Related Rent Concessions



IFRS 16 Amendment: COVID-19-Related Rent Concessions

1. Introduction

The IASB has issued an amendment to IFRS 16 *Leases* on 28 May 2020. The main purpose of this amendment is to provide a practical expedient for lessees in accounting for rent concessions received as a result of the COVID-19 pandemic (as reclassification and adjustment of lease liability requires a lot of time and effort) while still providing useful information about their leases to the readers of the Financial Statements.



Lessees may elect not to assess rent concession received as a direct consequence of the COVID-19 for lease modifications.



2. Reason for Amendment

Rent concessions that change the scope or overall consideration for a lease that was not part of the original conditions of an lease agreement is considered as lease modification. The lease modification treatment can be cumbersome for lessees with a large number of leases with different conditions and different rent concessions especially in the current difficult situation of the COVID-19 pandemic. Due to the concerns of lessees in assessing and accounting for the lease modification in this difficult time, the International Accounting Standards Board (IASB) issued an amendment to IFRS 16, *Covid-19-Related Rent Concessions*. The gist of the amendment is that you do not have to account for the rent concessions received as a result of COVID-19, as a lease modification.

3. Amendments

Lessees may elect not to assess rent concession received as a direct consequence of COVID-19 for lease modifications if the following conditions are met:

1. the change in lease payments must be substantially the same or less than the consideration before change;
2. any reduction in lease payments affects only payments originally due on or before 30 June 2021 (in other words, the change must not go beyond 30 June 2021); and
3. there is no substantive change to other terms and conditions of the lease.



Effective Date

Disclosures

- o Reporting periods beginning on or after 1 June 2020.
 - o Earlier application permitted for financial statements not authorised for issue on 28 May 2020.
- o Whether lessee has applied the practical expedient to all rent concessions that meet the conditions or, if not applied to all such rent concessions, information about the nature of the contracts to which it has applied the practical expedient; and
 - o the amount recognised in profit or loss for the reporting period to reflect changes in lease payments that arise from rent concessions to which the lessee has applied the practical expedient.

Adapting this change is voluntary, and therefore, businesses may still choose to account for lease modifications in accordance with the requirements before the amendment.



4. Accounting for Rent Concession

Lessees that received rent concessions that meet the conditions mentioned above can account for those rent concessions as if they were not lease modifications. The way the lessee accounts for rent concessions will be based on the type of concession received as follows:

∅ **Waiver of lease payments with no adjustments to future lease payments**

Rent concessions received in the form of a waiver of lease payments would generally be accounted as a variable lease payment. The lessee would derecognize the part of the lease liability that has been forgiven or waived with the corresponding entry to profit and loss account. However, the lessee shall recognise the interest component of the lease liability.

∅ **Deferment for certain periods followed by a proportionate increase in lease payments**

Deferred lease payments result in change in the timing of individual payments and do not extinguish the lessee's lease liability or change the consideration for the lease. Therefore, lessee would continue to both recognise interest on the lease liability and reduce that liability to reflect lease payments made to the lessor.

∅ **Both of Waiver and Deferment**

In some instances, the lessee might receive rent concessions in the form of both waiver and deferment of lease payments. This should be accounted for as explained above.



5. How it Applies in Practice

To make it easy to understand the treatment of rent concessions under the practical expedient we first look at how Lessee would initially recognise the lease transactions.

Case

A company enters into an agreement to lease a Guest House on an island for 2 years. The agreement was signed on 1 October 2019. Lease payments are MVR 150,000 per month payable at the beginning of each month. The annual interest rate implicit in the lease is 6%.

Here is how the lease should be accounted in the lessee's books.

Initial Recognition of the Lease Liability and Right-of-Use Asset (ROU Asset)

As the Lease payments are made monthly the present value of the lease payments should be calculated by using the monthly interest rate. The monthly interest rate can be computed as follows:

$$\begin{aligned}\text{Monthly Rate} &= (1 + \text{Annual Rate})^{1/12} - 1 \\ &= (1 + 6\%)^{1/12} - 1 = 0.49\%\end{aligned}$$

At commencement the company must record the lease liability at MVR 3,256,403 being the present value of the remaining 23 lease payments of MVR 150,000 discounted at 0.49% and the initial lease payment of 150,000 made at commencement date. In addition the company must record ROU Asset of 3,406,403 (3,256,403 + 150,000) being the PV of Lease Liability and the initial lease payment of 150,000 made at commencement date. These transactions will be recorded as follows:

Account	Dr (MVR)	Cr (MVR)
ROU Asset	3,406,403	
Bank/Cash		150,000
Lease Liability		3,256,403

Subsequent measurement of the Lease Liability would be to recognise the interest expense and record the lease payments. The depreciation expense should also be recognised for the ROU asset . Details of the amounts are shown in the table below.

Month	Period	Lease Liability b/f	Lease Payment	Interest	Lease Liability c/f	ROU Asset b/f	Depreciation	ROU Asset c/f
		A	B	C=(A-B) x Interest%	D=(A-B+C)			
Oct-19	1	3,256,403	-	15,851	3,272,254	3,406,403	141,933	3,264,470
Nov-19	2	3,272,254	150,000	15,198	3,137,452	3,264,470	141,933	3,122,536
Dec-19	3	3,137,452	150,000	14,542	3,001,994	3,122,536	141,933	2,980,603
Jan-20	4	3,001,994	150,000	13,882	2,865,876	2,980,603	141,933	2,838,669
Feb-20	5	2,865,876	150,000	13,220	2,729,096	2,838,669	141,933	2,696,736
Mar-20	6	2,729,096	150,000	12,554	2,591,650	2,696,736	141,933	2,554,802
Apr-20	7	2,591,650	150,000	11,885	2,453,535	2,554,802	141,933	2,412,869
May-20	8	2,453,535	150,000	11,213	2,314,748	2,412,869	141,933	2,270,935
Jun-20	9	2,314,748	150,000	10,537	2,175,285	2,270,935	141,933	2,129,002
Jul-20	10	2,175,285	150,000	9,858	2,035,143	2,129,002	141,933	1,987,068
Aug-20	11	2,035,143	150,000	9,176	1,894,319	1,987,068	141,933	1,845,135
Sep-20	12	1,894,319	150,000	8,491	1,752,810	1,845,135	141,933	1,703,201
Oct-20	13	1,752,810	150,000	7,802	1,610,612	1,703,201	141,933	1,561,268
Nov-20	14	1,610,612	150,000	7,110	1,467,722	1,561,268	141,933	1,419,335
Dec-20	15	1,467,722	150,000	6,414	1,324,136	1,419,335	141,933	1,277,401
Jan-21	16	1,324,136	150,000	5,715	1,179,851	1,277,401	141,933	1,135,468
Feb-21	17	1,179,851	150,000	5,013	1,034,864	1,135,468	141,933	993,534
Mar-21	18	1,034,864	150,000	4,307	889,171	993,534	141,933	851,601
Apr-21	19	889,171	150,000	3,598	742,769	851,601	141,933	709,667
May-21	20	742,769	150,000	2,885	595,654	709,667	141,933	567,734
Jun-21	21	595,654	150,000	2,169	447,823	567,734	141,933	425,800
Jul-21	22	447,823	150,000	1,450	299,273	425,800	141,933	283,867
Aug-21	23	299,273	150,000	727	150,000	283,867	141,933	141,933
Sep-21	24	150,000	150,000	-	-	141,933	141,933	-

For example, the entries for the month of June 2020 will be as follows:

Transaction	Account	Dr (MVR)	Cr (MVR)
Lease Payments	Lease Liability	150,000	
	Bank/Cash		150,000
Interest Expense	Interest Expense	10,537	
	Lease Liability		10,537
Depreciation Expense	Depreciation Expense	141,933	
	ROU Asset		141,933

Based on the above case, let us consider how the company should account for different rent concessions received due to the COVID-19 assuming all the conditions required under the amendment are met.

Scenario 1: Waiver of lease payments

The company received a waiver of the full lease payment for the month of June 2020 with no adjustment to future lease payments.

This should be recorded as follows:

Transaction	Account	Dr (MVR)	Cr (MVR)
Lease Payments	Lease Liability	150,000	
	Profit & Loss Account		150,000
Interest Expense	Interest Expense	10,537	
	Lease Liability		10,537

Scenario 2: Waiver of part of the lease payment

The company received a waiver of MVR 100,000 for the month of June 2020 lease payment with no adjustment to future lease payments.

This should be recorded as follows:

Transaction	Account	Dr (MVR)	Cr (MVR)
Lease Payments	Lease Liability	150,000	
	Bank/Cash		50,000
	Profit & Loss Account		100,000
Interest Expense	Interest Expense	10,537	
	Lease Liability		10,537

Scenario 3: Deferral followed by a proportionate increase in lease payments

The Company received a deferral of the June 2020 lease payment. The deferred lease payment is spread equally and is to be paid along with January and February 2021 lease payment.

	MVR	MVR
Deferred Amount relating to June 2020	150,000	
No. of month deferral to be paid in	2	
Additional amount payable in Jan and Feb 2021	75,000	
	Jan 2021	Feb 2021
Monthly amount payable	150,000	150,000
Additional amount relating to deferred amount	75,000	75,000
	225,000	225,000

This should be recorded as follows:

June 2020

Transaction	Account	Dr (MVR)	Cr (MVR)
Lease Payments	Lease Liability	-	
	Bank/Cash		-
Interest Expense	Interest Expense	10,537	
	Lease Liability		10,537

January 2021

Transaction	Account	Dr (MVR)	Cr (MVR)
Lease Payments	Lease Liability	225,000	
	Bank/Cash		225,000
Interest Expense	Interest Expense	5,715	
	Lease Liability		5,715

Note: In all the above scenarios there will be no impact to the depreciation expense of the ROU Asset. It has to be recorded as before.

6. Summary

The amendment to IFRS 16 *Leases* which deals with Covid-19-Related Rent Concessions will provide comfort for lessees, especially lessees with a large number of leases, during this challenging time as accounting for Covid-19-Related Rent Concessions are no longer required to be evaluated for Lease modification. The amendment does not bring any change for lessors' treatment of leases.

Further information

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