

# MCA Notifies Amendments to Ind AS 116 to Provide Lessee Specific COVID-19 Relaxations

*The International Accounting Standards Board (IASB) on 28 May 2020 amended IFRS 16, Leases. The amendment makes it easier for lessees to account for covid-19-related rent concessions such as rent holidays and temporary rent reductions. The amendment exempts lessees from having to consider individual lease contracts to determine whether rent concessions occurring as a direct consequence of the covid-19 pandemic are lease modifications and allows lessees to account for such rent concessions as if they were not lease modifications. It applies to covid-19-related rent concessions that reduce lease payments due on or before 30 June 2021. Read on...*



CA. Amit B Bahl

The author is a member of the Institute. He can be reached at [amitbahl009@gmail.com](mailto:amitbahl009@gmail.com) and [eboard@icai.in](mailto:eboard@icai.in)

IFRS 16 specifies how lessees should account for changes in lease payments, including concessions. However, 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. This optional practical expedient gives timely relief to lessees and enables them to continue providing information about their leases that is useful to investors. The amendment does not affect lessors.

The Accounting Standards Board (ASB) of ICAI noted that Indian entities preparing Ind AS based financial statements could be facing similar challenges and situations like the International scenario. In addition, there is a need to remain converged with IFRS standards. Accordingly, the ASB of ICAI had issued the exposure draft of proposed amendments to Ind AS 116, *Leases*. After following due process, the amendments to Ind AS 116 were notified by the Ministry Corporate Affairs (MCA) on 24 July 2020 to incorporate lessee specific COVID-19 relaxations. A lessee



can apply the amendments to Ind AS 116 for annual reporting periods beginning on or after 1 April 2020. In case a lessee has not yet approved the financial statements for issue before the issuance of this amendment, then the same may be applied for annual reporting periods beginning on or after 1 April 2019. The amendments notified by MCA to Ind AS 116 are substantially converged with the amendments to IFRS 16.

### Overview of the amendments to Ind AS 116:

**A lessee falls within the scope of the amendment when it meets all the four conditions:**

Criteria 1: Did the rent concession occur as a direct consequence of the COVID-19 pandemic?

Criteria 2: Does the change in lease payments 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?

Criteria 3: Does the reduction in lease payments affect only payments originally due on or before 30 June 2021?

Criteria 4: Is there no substantive changes to other terms and conditions of the lease?

If the response to all the four questions above is "Yes", then a lessee can elect to apply the practical expedient to not account for the change in lease payments as a lease modification. In many cases, change in lease payments will then be accounted for as variable lease payment.

### Let us look at the four conditions in detail:

#### Criteria 1: Direct consequence of COVID-19

A lessee can apply the practical expedient, when a rent concession occurs 'as a direct consequence of the COVID-19 pandemic'. The amendments do not provide further guidance on how this criterion should

be assessed. Judgements needs to be applied. The rent concessions provided by lessor due to closure of offices and retail outlets pursuant to the government notified lockdown would generally meet the criteria of "direct consequence of COVID-19".

#### Criteria 2: Revised consideration

The second criteria for the expedient to apply is that the rent concession must result in revised consideration for the lease that is substantially the same, or less than, the consideration for the lease immediately preceding the change. For example, if the

concession compensates for the loss of time value of money due to deferral, for example, A lessor may defer the 3 months rental of a multiplex building amounting to INR 6 million for a period 9 months. Post deferral period, the lessee would pay INR 6.35 million to compensate for the loss of time value of money. So long as the increase in nominal cash flows reflects the time value of money, the lessee can still apply the expedient.

#### Criteria 3: Concession affects the lease payments originally due on or before 30 June 2021

The rent concession must reduce lease payments originally due on or before 30 June 2021. A rent concession that reduces lease payments after 30 June 2021 will disqualify the rent concession from the application of the practical expedient. The rent concession



A lessee can apply the amendments to Ind AS 116 for annual reporting periods beginning on or after 1 April 2020. In case a lessee has not yet approved the financial statements for issue before the issuance of this amendment, then the same may be applied for annual reporting periods beginning on or after 1 April 2019.

rent concession reduces the nominal cash flows by INR 5 million in comparison to the terms of the lease prior to the change, it would satisfy this criteria. The amendments are not explicit as to whether the 'revised consideration' should be assessed based on nominal or discounted cash flows. In certain cases, a lessor may defer rentals for certain period with increase in nominal rentals to



A lessee can apply the practical expedient, when a rent concession occurs ‘as a direct consequence of the COVID-19 pandemic’.

must be assessed for the whole of the period and cannot be subdivided.

A rent concession would meet this condition if it results in reduced lease payments before 30 June 2021 and increased lease payments that extend beyond 30 June 2021.

*Criteria 4: No substantive changes to other terms and conditions*

The rent concession must not contain substantive changes to other terms and conditions of the lease. Extensions to the lease term, the introduction or modification of lessee and/or lessor options, or other changes in the scope of leases would disqualify the rent concession from the application of the practical expedient. Instead, the lessee would be required to apply the requirements applicable to lease modifications, if the change meets the definition of a lease modification. For example, if a lessor offered to reduce the lessee’s monthly rent for office space by 50% for a period of six months due to COVID-19, but only on the condition that the lessee reduced its office space from 10,000 square feet to 5,000 square feet, then such concession would not be eligible for the practical expedient.

## How will the practical expedient benefit the lessee?

If a rent concession satisfies all conditions discussed above, the practical expedient is available to be applied, however, its application is not mandatory, i.e., a lessee can elect not to apply the practical expedient. All accounting policies relating to leases in the scope of Ind AS 116 are subject to the requirement in paragraph 2 of Ind AS 116, which requires an entity to apply Ind AS 116 consistently to contracts with ‘similar characteristics and in similar circumstances’. The same principle should be followed by applying the practical expedient to similar leases.

If the lessee elects to apply the practical expedient, the lessee does not account for a rent concession as a lease modification.. In many situations, a lessee would account for the rent concession applying the requirements of Ind AS 116 para 38(b) i.e. as a negative variable lease payment.

Let’s consider an example below to explain the impact of the amendment:

### Example 1: Forgiveness of lease payments -Impact of amendment

*ABC Limited leases a property from a lessor. As at 1 June 2020, Lessor grants ABC Limited rental waiver of 3 months due to the COVID-19 pandemic. This rent waiver was not part of the original terms and conditions of the lease. There are no conditions attached to the waiver.. Apart from the rent waiver, there is also a non-substantive change to terms of the lease contract. Assume that*

*all the four criteria to apply the COVID-19 practical expedient discussed above are met.*

*Query: How should ABC Limited account for the rent waiver?*

### Response:

Ind AS 116 defines 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(for example, adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual lease term”.

The rent concession provided to ABC Limited meets the definition of a lease modification (because it is a change in consideration for a lease that it not part of the original terms) and it would be accounted for as a lease modification, if the practical expedient is not elected by ABC Limited.



For example, A lessor may defer the 3 months rental of a multiplex building amounting to INR 6 million for a period 9 months. Post deferral period, the lessee would pay INR 6.35 million to compensate for the loss of time value of money. So long as the increase in nominal cash flows reflects the time value of money, the lessee can still apply the expedient.



A rent concession that reduces lease payments after 30 June 2021 will disqualify the rent concession from the application of the practical expedient. The rent concession must be assessed for the whole of the period and cannot be sub-divided.

### Example 2 : Accounting treatment of rent forgiveness based on illustrative numbers

Lessee ABC Limited enters into contract with Lessor LMQ to lease a retail space for 5 years . The lease commenced on 1 April 2018 and rental payments are INR 100,000 per month payable in advance. ABC Limited's incremental borrowing rate at commencement of lease was 5% per annum. There are no initial direct costs.

ABC Limited's business is significantly impacted by COVID-19 and both ABC Limited and Lessor LMQ negotiate a rent concession. On

31 May 2020, Lessor agrees to provide a concession whereby the Lessor forgives the rentals of the Lessee for next three months provided the retail space is closed due to lockdown.

Assuming that there are no other changes to the lease and lock down continues till August 2020, ABC Limited shall recognize the credit of INR 100,000 in each month of June 2020, July 2020 and August 2020 with corresponding adjustment to the lease liability because the waiver is granted on condition that retail space is closed due to lockdown.

In contrast, if the ABC Limited was forgiven the lease payments at 31 May 2020 for payments due in June, July and August 2020 without a condition attached to the forgiveness (that is, irrespective of the closure of retail space due to lockdown), the lessee should recognise a gain for the portion of the lease liability that is forgiven (that is, for the present value of INR 300,000) on 31 May 2020.



For example, If a lessor offered to reduce the lessee's monthly rent for office space by 50% for a period of six months due to COVID-19, but only on the condition that the lessee reduced its office space from 10,000 square feet to 5,000 square feet, then such concession would not be eligible for the practical expedient.

	<b>Practical expedient applied (variable lease payment accounting as per para 38 of Ind AS 116)</b>	<b>Practical expedient is not applied (lease modification accounting)</b>
<b>Lease liability</b>	Reduced for the impact of revised consideration. Reduction is accounted when the waiver is granted. There are no conditions attached to the waiver. s	Reduced for the overall impact of revised consideration on the date of modification
<b>Right-of-use asset</b>	No impact	Impact of lease liability reduction is adjusted with the right-of-use asset
<b>Discount rate</b>	No change	The revised remaining consideration is discounted using a <i>revised discount rate</i> determined on the date of lease modification
<b>Effect on profit or loss</b>	Impact of reduction in lease liability is recognized in profit or loss when the waiver occurs	No impact on lease modification. Future amortization of right-of-use asset and interest expense on lease liability will change



If the lessee elects to apply the practical expedient, the lessee does not account for a rent concession as a lease modification.. In many situations, a lessee would account for the rent concession applying the requirements of Ind AS 116 para 38(b) i.e. as a negative variable lease payment.

## Accounting treatment of rent deferral

A change in lease payments that only reduces payments in one period but proportionally increases payments in another does not extinguish the lessee's liability or substantially change the consideration of the lease. A lessee should recognise in profit or loss the present value effect that would result from discounting the revised payments using an unchanged discount rate at the time when the deferral is granted.

## Disclosure

An entity that applies the practical expedient must disclose:

- (a) that it has applied the practical expedient to all rent concessions that meet the criteria, 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
- (b) the amount recognised in profit or loss to reflect changes

in lease payments that arise from COVID-19-related rent concessions. Accordingly, rent concessions accounted for as negative variable lease payments in profit or loss must be disclosed separately from the effect of other variable lease payments included in profit or loss.

## Transition and effective date

Lessees will apply the practical expedient 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. In the reporting period in which a lessee first applies the amendment, the lessee is not required to disclose the information required by paragraph 28(f) of Ind AS 8 Accounting Policies, Changes in



A lessee can apply the amendments to Ind AS 116 for annual reporting periods beginning on or after 1 April 2020. In case a lessee has not yet approved the financial statements for issue before the issuance of this amendment, then the same may be applied for annual reporting periods beginning on or after 1 April 2019.

Accounting Estimates and Errors.

A lessee can apply the amendments to Ind AS 116 for annual reporting periods beginning on or after 1 April 2020. In case a lessee has not yet approved the financial statements for issue before the issuance of this amendment, then the same may be applied for annual reporting periods beginning on or after 1 April 2019.

## Key takeaway

The amendment to Ind AS 116 will provide relief to lessees for accounting for rent concessions from lessors specifically arising from the covid-19 pandemic. While lessees that elect to apply the practical expedient do not need to assess whether a concession constitutes a modification, lessees still need to evaluate the appropriate accounting for each concession as the terms of the concession granted may vary. The practical expedient is not available for lessors. ■■■

Reference:

[http://www.mca.gov.in/Ministry/pdf/Rule\\_24072020.pdf](http://www.mca.gov.in/Ministry/pdf/Rule_24072020.pdf)

<https://www.ifrs.org/news-and-events/2020/05/iab-issues-amendment-to-ifrs-standard-on-leases/>

<https://cdn.ifrs.org/-/media/project/ifrs-16-covid-19/covid-19-related-rent-concessions-amendment-to-ifrs-16.pdf?la=en>

<https://resource.cdn.icai.org/59845asb48675.pdf>

<https://indasaccess.icai.org/download/2019/asb0719/264/264asb-cias-2019-20-vol1-16.pdf>

<https://www.ifrs.org/news-and-events/2020/04/amendment-to-leases-standard-to-help-companies-with-covid-19-related-rent-concessions/>