



DRAFT AMENDMENTS TO FRS 102 AND FRS 105 – COVID-19-RELATED RENT CONCESSIONS

Issued 28 August 2020

ICAEW welcomes the opportunity to comment on the FRED 76 *Draft amendments to FRS 102 and FRS 105 – COVID-19-related rent concessions* published by Financial Reporting Council in July 2020, a copy of which is available from this [link](#).

We support the proposed amendments to FRS 102 and FRS 105 for COVID-19-related rent concessions. We understand that different views have emerged in practice regarding how such arrangements should be accounted for under UK GAAP, primarily in relation to operating lease agreements. We agree, therefore, that clarifying the treatment within UK accounting standards will help reduce uncertainty and achieve greater consistency and comparability in reported results.

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KEY POINTS

Support for amendments

1. We support the proposed amendments to FRS 102 and FRS 105 for COVID-19-related rent concessions. We understand that different views have emerged in practice regarding how such arrangements should be accounted for under UK GAAP, primarily in relation to operating lease agreements. We agree, therefore, that clarifying the treatment within UK accounting standards will help reduce uncertainty and achieve greater consistency and comparability in reported results.
2. We broadly support mandatory application of the proposed accounting treatment, although we have noted below some potential complications for lessors reporting within IFRS groups.
3. We would welcome further illustrative examples within the standards, or guidance within Staff Educational Material, to demonstrate how the proposed accounting treatment for COVID-19-related rent concessions would be applied in practice. While lease arrangements vary between entities, there may be some common scenarios which could helpfully be used to demonstrate the FRC's intentions in developing the proposals. Throughout our response we have highlighted the specific areas where we believe further guidance would be helpful.

ANSWERS TO SPECIFIC QUESTIONS

Question 1

Do you agree with the proposed amendments to FRS 102 and FRS 105? If not, why not?

4. While we broadly agree with the proposed amendments to FRS 102 and FRS 105, we have set out some observations in the following paragraphs.

Time period over which lease payments are being compensated

5. Proposed paragraph 20.15C (and 20.25B for lessors) states that any change in lease payments arising from rent concessions meeting the relevant criteria should be recognised 'over the periods that the change in lease payments is intended to compensate'. We note the FRC's conclusion in paragraph 11 of the Basis for Conclusions that this would generally reflect the economic substance of the intended benefit of the concessions and their temporary nature.
6. While we agree with the rationale behind the proposal in paragraphs 20.15C and 20.25B, we do not find the proposed wording entirely clear. In our view, it would be simpler to refer to the 'period for which the lease payments are reduced.'
7. Notwithstanding our comments on the proposed drafting, we believe it would be helpful for the FRC to provide further guidance, or examples, to explain how an entity would determine the period in which the reduced lease payments should be recognised. In our view, there is scope for confusion on this matter. For example, when a rent concession has been agreed but does not come into effect until a later date, would the 'period' referred to in the proposed amendments start from the point at which the rent concession was agreed, or when the reduced payments come into effect? Further clarity on this point would be helpful.
8. We also believe that further guidance would be helpful to demonstrate how the benefit arising from the rent concession would be spread over the period to which it relates (as discussed above). This would help reduce uncertainty over its application, and avoid structuring opportunities.
9. To demonstrate the scope for different interpretations, some rent concessions may be graduated so that they decrease over time. In this instance, would the benefit arising from the rent concession be spread such that it reflects the pattern of the users' benefit from the concession (ie, to compensate the user for the asset being unavailable or unable to be used to its normal capacity due to COVID-19 restrictions), or on a straight line basis over the concession period?

10. We would expect the intention to be the spreading of the benefit of the rent concession on a straight-line basis unless there is another systematic basis. If this is the case, perhaps this could be made clear within the standard. For example, drawing on similar requirements for the accounting for grants and lease payments, it could be that the benefits are required to be 'recognised on a straight-line basis unless another systematic basis better reflects the time pattern of hardship of the lessee which the concession is intended to compensate.' If the FRC were to amend the standard in this way we suggest that the Basis for Conclusions should comment on the fact that entities would need to explain the basis of spreading period of concession if considered a key judgement, in accordance with FRS 102.8.6.

Criteria for applying the COVID-19 rent concession treatment

11. One of the criteria for applying the accounting treatment for COVID-19-related rent concessions is that 'the change in lease payments results in revised consideration for the lease that is less than the consideration for the lease immediately preceding the change' (proposed paragraph 20.15D(b)).
12. We note that this differs from the equivalent wording within the IFRS 16 Leases amendments, which refer to changes in lease payments that '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.' We understand from the Basis for Conclusions that this is because the amendments to UK GAAP are intended to cover rent concessions only, and not rent deferrals.
13. While we do not object to paragraph 20.15D(b), we suggest it may be helpful for the FRC to provide further guidance, or examples, to demonstrate how the criteria would be applied in different scenarios.
14. For example, there may be uncertainty around situations where rent reductions are compensated by rent increases beyond June 2021. If there is a net reduction in the lease payments, would the arrangement be within scope of the proposals, with only the net benefit recognised over the period to be compensated? Similarly, would a 3-month rent free period (perhaps to cover a lockdown period), with a 3-month extension of the lease at normal rent, be within the scope of the amendments? The latter situation is within the scope of the recent IFRS 16 amendments (BC205D) but it is not clear if that would be case with the proposed amendments to UK GAAP.

Lessors

15. We support the FRC's decision to extend the proposed accounting treatment for COVID-19-related rent concessions to lessors.
16. We note, however, that similar amendments have not been made for lessor accounting under IFRS. As the accounting treatment outlined in FRED 76 will be mandatory, there may be tensions for IFRS group reporters that are lessors where a different treatment will be applied in the group accounts compared to any subsidiary accounts prepared under FRS 102 or FRS 105. It is not clear from the Basis for Conclusions whether the FRC has fully considered this matter, and whether it would result in useful information in these situations.

Non COVID-19-related rent concessions

17. FRS 102 does not specify how to account for changes in lease payments that result from rent concessions, or indeed, for significant changes to other terms and conditions of a lease arrangements. We note that the FRC does not wish entities to analogise the COVID-19 guidance for other rent concessions and, for this reason, has placed limitations on the proposed accounting treatment in FRED 76.
18. However, in our view, accounting for modifications to lease arrangements is a matter that could be helpfully addressed within FRS 102. While we do not suggest that this should be considered as part of the current proposals, we believe it should be revisited at the next Triennial Review of FRS 102.

Other

19. Paragraph 16 of the Basis for Conclusions notes that “The proposed amendments also apply only to rent concessions that introduce no significant change to other terms and conditions of the lease. Therefore, a concession that incorporates significant changes to a lease agreement which are unrelated to the COVID-19 pandemic but negotiated at the same time as those related changes, would not meet this condition.” We believe the word ‘also’ at the start of this paragraph is contradictory and may cause confusion. We would suggest it is removed to avoid any potential confusion to readers.

Question 2

Do you agree with the proposed effective date for these amendments? If not, what difficulties do you foresee?

20. Yes, we agree that the proposed amendments should be effective for periods beginning on or after 1 January 2020, with early application permitted.
21. We also urge the FRC to expedite, where possible, the timetable for finalising and publishing the amendments. This will help reduce uncertainty over the accounting for COVID-19-related rent concessions, particularly for any entities with a short reporting period.

Question 3

The proposed amendments to FRS 102 require a lessee to disclose those changes in lease payments recognised in accordance with paragraph 20.15C.

The Basis for Conclusions describes the reasons for this proposal and the existing disclosures required by FRS 102 relevant to this transaction.

Do you consider that these disclosure requirements are sufficient to meet the needs of users?

22. We agree with the need for disclosure of the changes in lease payments arising from COVID-19-related rent concessions in the accounts. However, in our view, it is not entirely clear that proposed paragraph FRS 102.20.16(c) requires disclosure of the profit or loss effect of any COVID-19-related rent concessions accounted for in accordance with proposed paragraphs 20.15C and 20.15D. We suggest that the disclosure requirement is clarified to add ‘recognised in profit or loss’ to avoid any confusion.
23. We also believe it would be helpful to require entities to disclose the nature of the COVID-19-related rent concessions which are being accounted for in accordance with proposed paragraphs 20.15C and 20.25D. We acknowledge that a general description of lease arrangements is not required by lessees for operating leases (although perhaps this is another matter that could be addressed in the next Triennial Review of FRS 102). Nevertheless, we believe that disclosure of the nature of the COVID-19-related rent concession would appear to be important and relevant information to users of the accounts.
24. We note that there are no specific disclosure requirements outlined for lessors applying the accounting treatment for COVID-19-related rent concessions. Paragraph 18 of the Basis for Conclusions refers to the existing requirement for lessors to provide a general description of leasing arrangements, and the FRC’s expectation that this would include details of the nature of any rent concessions. We question whether this will provide sufficient information to meet the needs of users. Section 20 of FRS 102 does not require lease income to be disclosed (although, if material, some disaggregation of revenue/other income would be expected). For rental companies, lease income would be included in revenue. For other companies, it may be included in ‘other operating income’ and if material, disclosure in the notes may be required. We believe it would be appropriate to require lessors to give the same disclosures as lessees in respect of the impact on profit or loss of COVID-19-related rent concessions (as well as the nature of concessions).
25. We suggest that an exemption should be given from the requirement in FRS 102.10.13(b) to disclose the amount of adjustment for each financial statement line item affected in the

current and prior periods as a result of the amendment to FRS 102. As noted in the Basis for Conclusions, the accounting treatment for rent concession is not entirely clear under current FRS 102 which would make providing this disclosure difficult. A similar exemption has been provided in the recent amendments to IFRS for COVID-19-related rent concessions.

Question 4

In relation to the Consultation stage impact assessment, do you have any comments on the costs and benefits identified? Please provide evidence to support your views?

26. We have no comments on the costs and benefits identified by the FRC at this stage