

## Amendments of Leases as a Result of COVID-19-Related National and International Measures

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**Abstract:** *The spread of the dangerous, contagious human disease COVID-19 has dampened the economies of all countries since the end of 2019. Governments, as well as international organisations and bodies, operating in the various COVID-19-affected areas have taken measures to mitigate the impact of COVID-19 of the crisis on economic and social life. This paper examines and compares the measures influencing accounting theory and practice taken by the Slovak government, the European Union, and the International Accounting Standards Board to maintain the "going concern" assumption of accounting entities. One of the measures taken caused amendments to leases, particularly in the part of rent concessions.*

**Keywords:** COVID-19, leases, IFRS 16, IASB, Slovak Republic

JEL codes: M41, M48

### 1 Introduction

The spread of the dangerous, contagious human disease COVID-19 since the end of 2019 has caused a slowdown of economies in all countries and thus the emergence of probably one of the greatest economic crises of the 21st century. This phenomenon has been called the COVID-19 pandemic. It hit full force in the year 2020 and has also taken the form of a society wide crisis spreading worldwide. According to Caballero-Morales (2021) the COVID-19 pandemic has had a deeper impact on small and medium enterprises (SMEs) in emerging economies because they have very limited resources and vulnerable supply chain and business-to-business/business-to-clients relationships. Different policy decisions e.g. travel restrictions, inter-state travel restrictions, occupation restrictions, full lockdowns, and reopening scenarios (Killian et al., 2020) to slow the dynamics of the spread of the disease have enforced changes in the behaviour of the household, as well as business, sectors. Although SMEs are considered as a backbone of the economy, the negative impact of the COVID-19 pandemic was reflected clearly in large companies, and varied by sector. Liu (2021), in his study focused on the Chinese stock markets, found that, simultaneously, higher uncertainty due to COVID-19 was significantly associated with greater volatility in stock returns for both the composite index and sector indices. Carracedo et al. (2021) stated that companies have been forced to adopt new managerial guidelines to adapt to the difficult conditions and to survive in this "new normal". For instance, the impact of COVID-19 pandemic on the restaurant and bar sector has resulted even in already undergoing structural change (Neise et al., 2021; Zięba, 2021). Alongside the development of the COVID-19 pandemic, the role of governments changed. Governments in many European countries started to introduce numerous regulations, limitations, and restrictions intended to keep the spread of the virus under control (Zięba, 2021). The administration of governmental limitations and regulations has also had a devastating impact on many businesses, although many legal regulations should help business to survive. It was also noted in the USA, with three quarters of small businesses having enough cash to last no more than two months, the small business sector proved to be financially fragile and significantly dependent on government actions helping them to endure this difficult period (Bartik et al., 2020). Although many authors (e.g. Caballero-Morales, 2021; Donthu & Gustafsson, 2020; Killian et al., 2020; Liu, 2021; Niese et al., 2021; Zięba, 2021) identify a number of negative impacts of the pandemic, there are also bright sides e.g. it proves

that markets are dynamic (Jaworski, Kohli, & Sahay, 2000). Despite the fact that market dynamics did exist during the COVID-19 outbreak, we should take into consideration the factor of government regulation. Severe economic and social consequences of the current outbreak mean that no country will be unaffected, including the Slovak Republic. In this context, this paper is focused on the measures taken by the Slovak government, the European Union and the International Accounting Standards Board to influence accounting theory and practice as regards leases to maintain the "going concern" assumption of accounting entities.

## 2 Methodology and Data

This research paper focuses on regulations applied in the Slovak Republic between March 2020 and July 2021 to help businesses to survive during the time of specific governmental limitations of consumers' ordinary behaviour. The focus is also on the international impact connected with the support of businesses during the COVID-19 pandemic period. In this case, it monitors the work of the European Union and the International Accounting Standard Board. The research is based on a qualitative descriptive design. Data used in this paper was collected mainly through the available secondary sources.

## 3 Results and Discussion

Since the beginning of the COVID-19 pandemic, two waves were detected so far in the Slovak Republic. The first wave resulted in the adoption of restrictive measures to prevent the COVID-19 outbreak and caused the first declaration of emergency from March 2020 until June 2020. One of the first analyses of the economic situation at that time was provided by Finstat in April 2020. This analysis showed that 15 660 businesses - generating annual sales totalling approximately 8.8 billion euros - were placed at risk by the COVID-19 crisis (Finstat, 2020). The slow-down of the Slovak economy was accompanied by stimulus packages provided by the Slovak government. On 2nd April 2020, the act No 67/2020 Coll. on certain emergency financial measures in relation to the spread of the dangerous, contagious human disease COVID-19 was issued to regulate the emergency measures in the field of taxation, customs and accounting. Most importantly, this act regulates tax administration, motor vehicle tax, administrative fees, accounting in relation to the act No. 431/2002 on Accounting, income tax, the area of the financial market, and the area of budgetary rules. In order to support businesses and employment, all Ministries have introduced aids. The one connected with leases has its legislative background only partially in the act No. 67/2020 Coll. in the third part "Moratorium on repayments of loans". Leases have some features of loans (Blahušiaková, 2016; Vašeková, 2018). The Ministry of Finance of the Slovak Republic has brought in lease payment holidays in its LEX KORONA 3 stimulus package. This package is intended for consumers and small and medium-sized enterprises. In the case of a financial leasing agreement, the lessee may request an adjustment of the lease amortisation schedule which will be implemented by a deferral of payments for a maximum of 3 months - during the pandemic only. It is possible to request a further extension, for a maximum of another three months, before the end of the first deferral. The lessee is obliged to pay the interest and insurance agreed in the instalments also during the deferral of the principal instalments according to the lease amortisation schedule. The leasing company may not charge any fee for the deferral of payments (FINinfo, 2020).

Internationally, measures have been taken by the International Accounting Standards Board (IASB) - the IFRS Foundation's standard-setting body of IFRS Standards (Hornická, 2017; Kordošová, 2019). The IASB, and also the US's Financial Accounting Standards Board (FASB), decided to give relief to lessees in response to the COVID-19 pandemic by amendments to the IASB's IFRS 16 Leases and FASB's ASC 842 Leases. This relief from the requirements in IFRS 16 or ASC 842 casts doubt on their necessity. Teixeira (2021) highlights weaknesses in how the IASB and FASB developed their leases Standards, and why those Standards are not robust enough to cope with a shock to the economic system. Considering the pandemic situation, the IASB published its first amendments to IFRS 16

titled "Covid-19-Related Rent Concessions" on 28 May 2020. As governments or jurisdictional authorities required, or encouraged, lessors around the world to provide rent concessions to lessees in the form of rent holidays or rent reductions, the IASB decided to specify the accounting treatment for changes in lease payments, including rent concessions. On the other hand, there was also the need for faithful disclosure. Hence, the amendment to IFRS 16 provides optional, temporary COVID-19 related operational relief for lessees benefitting from lease payments holidays without undermining the relevance and usefulness of financial information reported by companies (Commission Regulation, 2020). The amendment permitted lessees not to assess whether particular - rent concessions occurring as a direct consequence of the COVID-19 pandemic are lease modifications and instead to account for those rent concessions as if they are not lease modifications (IFRS 16, 2020). According to the IASB decision, these amendments are effective as from 1 June 2020 and did not affect lessors. The IASB proposed to extend the application period of the COVID-19 related amendments to IFRS 16 in February 2021. Due to the urgent nature of this proposal the IASB issued an official amendment "Covid-19-Related Rent Concessions beyond 30 June 2021", which extended the availability of this practical expedient by one year already in March 2021. This amendment has an effective date for annual reporting periods beginning on or after 1 April 2021.

As many accounting entities have had to cease their business, the repayment of lease payments has become an issue that has been addressed at the level of individual countries, but also at the level of the European Union. The European Union has also taken steps to emphasize the need to apply measures to mitigate the adverse effects of this situation on the citizens of the European Union as well as on the accounting entities. The main aim was to prevent the bankruptcy of companies and the consequent loss of jobs. This, caused both the Member States and the European Union to take measures to provide financial aid including payment holidays based on private or public moratoria. For this reason, the document amending IFRS 16 (Covid-19-Related Rent Concessions) issued by the IASB was also expressly adopted by the European Commission. Following the consultation with the EFRAG, the European Commission published its Regulation (EU) 2020/1434 amending Regulation (EC) No 1126/2008 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council as regards International Financial Reporting Standard 16 on 9 October 2020. These amendments are effective also in act No 431/2002 on Accounting specified accounting entities. The Act No 431/2002 on Accounting is affected by the accounting legislation implemented by the European Union (Hunyady and Domaracká, 2016). Amendments to IFRS 16 are related to lessee in part to subsequent measurement (lease modifications) and disclosure. IFRS 16 (2020) permits lessees, as a practical expedient, not to assess whether particular COVID-19-related rent concessions are lease modifications. Instead, lessees that apply the practical expedient would account for these rent concessions as if they were not lease modifications. This practical expedient applies only to rent concessions occurring as a direct consequence of the COVID-19 pandemic and only if all three conditions stated in IFRS 16 are met. If a lessee applies the practical expedient, the disclosure requirements are for the group of all rent concessions to which the practical expedient was applied to confirm that all conditions were met. If the practical expedient was not applied to all such rent concessions, a lessee shall disclose information about the nature of the contracts to which it was applied. In addition, the lessee shall disclose 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 (Commission Regulation, 2020). The European Commission has not yet issued a new regulation in connection with the recently published amendments to IFRS 16 (Covid-19-Related Rent Concessions beyond 30 June 2021) by the IASB.

If we compare the national and international measures on leases, we can identify some differences. The national measures are designed for small and medium sized enterprises, if they meet some criteria and also ask for changes in their lease amortization schedule. According to the Slovak measures, there is no disclosure requirement to inform that the business is having three or six months of the lease payment holidays after the request is

accepted by a leasing company. Lease payment holidays relate only to the repayment of principal and not to the interest and insurance agreed in the instalments. The international measures applied by the IASB and EU are designed for all accounting entities which apply IFRS for disclosure of their financial information. The international measures do not set the form or the length of the COVID-19 related rent concessions, but alter the measurement (subsequent measurement – lease modification) and disclosure by a lessee.

## Conclusions

The spread of the dangerous, contagious human disease COVID-19 since the end of 2019 has caused a slowdown of economies in all countries. Restrictions applied by governments had an impact on each business, entity or individual. As the COVID-19 pandemic crisis has not been overcome yet, it is expected that many enterprises (primarily SMEs) will disappear as the "new normality" will require changes in business or working conditions. SMEs are a pillar of the Slovak economy, accounting for 99.9% of the total number of business entities, providing employment opportunities in the corporate economy for almost 75% of the active workforce and contributing more than 50% to gross production and added value (Monitoring podnikateľského prostredia, 2021). In this context, the Slovak government has decided to provide stimulus packages. In order to support SMEs, it introduced a moratorium on repayments of loans in the act No 67/2020 Coll. Although this part of the act does not directly apply to leases, it is used as a base by leasing companies if they are asked to provide rent concessions. The IASB, FASB and EU also adopted measures on COVID-19 related concessions. After a comparison of national and international measures, differences were identified. The national measures are designed for small and medium sized enterprises, which have to officially ask for a change in the lease amortization schedule from their leasing company. The change consists of three- or six-months lease payment holidays and relates only to the repayment of principal and not to the interest and insurance agreed in the instalments. According to the Slovak measures, there is no disclosure requirement for lease payment holidays. The international measures, applied by the IASB and EU set the measurement and disclosure by a lessee, but do not set the form or the length of the COVID-19 related rent concessions. It is difficult to estimate if work done by government or international bodies is enough and how long the impact will continue, but it should be emphasized that amendments to IFRS 16 and ASC 842 have raised questions of whether the leasing standards have some underlying weaknesses and if new amendments are needed before another crisis starts.

## Acknowledgments

This article is an output of the project APVV no. APVV-16-0602 "Enhancement of the relevance of the accounting data in the SR - from expenses to value".

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