To whom it may concern,

Thank you for the opportunity to comment on the proposals within FRED 82 and for giving interested parties the opportunity to shape UK GAAP.

Firstly, I would like to state that the following observations are my solely my personal views and are in no way connected to any employer I currently work with or have previously worked within.

Background: I am a qualified FCCA, particularly interested within the area accounting for leases having exposure to SSAP 21, IAS 17 and more latterly IFRS 16 during my career.

As my interest (and specialism) is within IFRS 16 Leases, it is that area I shall be commenting upon in this invitation. I shall therefore be commenting on Question 6 and Question 8 (but with reference to leases only)

With regard to Question 6:

Question: Do you agree with the proposals to revise Section 20 of FRS 102 to reflect the on-balance sheet lease accounting model from IFRS 16, with simplifications?

Answer: **I do**. I am in agreement with the principles as outlined within IFRS 16 and with the concept of capturing all non low value/short term leases on balance sheet. Ever since the IASB former chairman, Sir David Tweedie, made his now famous and revered comment to The Empire Club of Canada in Toronto in 2008, I have agreed that as leasing is a form of financing (and organisations are able to generate revenue from its existence) leases should be accounted for on balance sheets (subject to the recognition practical exemptions)

Question: Have you identified any further simplifications or additional guidance that you consider would be necessary or beneficial?

Answer: **Please see below**

My comments below reflect the fact that the audience for FRED 82 is the SME community and any suggestions I make herein are to help an easier transition (and subsequent reporting) from IAS 17 aligned Section 20 to IFRS 16 for such organisations.

My only comment with regards to IFRS 16 within FRED 82 is with regard to the discount rate.

My observations are as follows:

- *Order of application*

One of the most complex areas of IFRS 16 is the determination of the discount rate to be used when calculating the initial measurement of the lease liability. Paragraph 20.52 specifies 4 separate notions (2 aligned to full IFRS 16 and 2 new concepts) as to what discount rate should be used.

1) Implicit interest rate in the lease as calculated as that rate of interest which causes the present value of:

a) the lease payments and b) the unguaranteed residual value* to equal i) the fair value of the underlying asset*+ ii) any initial direct costs of the lessor*

*-subjective assessment or requires information from the lessor

2) the lessee incremental borrowing rate (if i) is not "*readily obtainable*")

3) the lessee obtainable borrowing rate (new in FRED 82)

4) The Gilt Rate (new in FRED 82)-if those in ii) & iii) above is not "*readily obtainable*")

As FRED 82 suggests 4 options I read paragraph 20.52 as a ranking of the various discounts rates to use in the order they are written (It is simpler in IFRS 16 as there are only 2 options). However, I am uncertain whether the lessee's incremental borrowing rate takes precedence over the lessee's obtainable borrowing rate ("middle 2 options"). For clarity, I would suggest the paragraph needs to indicate definitively the precedence requirements or if in the case of the aforementioned "middle" 2 options it should be stated that either could apply i.e. there is no specific requirement in the application order of these 2 options.

- *The implicit rate in the lease*

The IASB believes that organisations should specify a discount rate that reflects how the contract is priced and therefore a lessee should use the implicit rate in the lease (if readily obtainable) (BC160). But it has been widely commented that determining the implicit interest rate in a lease is a difficult exercise principally because:

- It is lessor specific e.g. it requires the lessor's initial direct costs

- It depends on the initial fair value of the underlying asset and the ***lessor's*** expectation of the residual value of the asset at the end of the lease. Unless the underlying asset is acquired by the lessor at lease inception and conveyed to the lessee at the end of the lease term a lessee will often not have the required information to determine both of these amounts.

Therefore,

- The implicit rate requires resource to obtain the information which, as FRED 82 will be applied to SMEs, such organisations may not have.

- To request information of a lessor may breach commercial boundaries within the lease contract (if not specified during lease negotiations at the outset).

Given the complexity regarding sourcing the information required to calculate the implicit interest rate, there is an argument to be made that the use of the implicit interest rate should be less prescriptive ie more of an encouragement rather than a requirement.

- *The notion of "readily available"*

Organisations that would be applying FRED 82 may have differing views as to what "readily obtainable" actually means or may not be able to obtain necessary guidance as to form a view as to exactly what is "readily obtainable" (as, of course, not all SMEs are may not have auditors to advise for example).

This notion of "readily available" could be argued as ambiguous and open to interpretation and has, in my opinion, a negative connotation in that the IASB had a suspicion that lessors would not be too forthcoming in supplying the required information to calculate the implicit rate in the lease and therefore used the term as a "get out" without actually specifying what it meant.

If the implicit rate is to remain as a 1st instance requirement, I would therefore propose for greater clarity and simplicity that the notion of "readily available" is defined somewhat (ie how many attempts to get information from a lessor is sufficient if not forthcoming; suggest what reasons would be sufficient from a lessor to not to supply information to define that it would be deemed not readily available e.g. commercial confidentiality/contract re-negotiation difficulties). However, I realise that this would become a "charter" of the ways to avoid using the implicit rate in the lease (as I believe it is a more onerous task to obtain than the other 3 options) Failing that, I would propose that the FRC would omit the term "readily available" and mandate something akin to "the lease payments shall be discounted using the interest rate implicit in the lease, *in the 1st instance*, *and therefore make a demonstrable and reasonable attempt to obtain such information as required to calculate the implicit rate*. *If that information is not forthcoming,* then the lessee shall use the incremental borrowing rate or the lessee's obtainable borrowing rate etc."

- *The gilt rate in the lease*

Paragraph 20.52 uses the term "in exceptional circumstances" that the gilt rate shall be used without appearing to give any indication as to what circumstances would be considered "exceptional". Therefore, greater clarity may be required to define this term.

With regard to Question 8:

Question: *The proposed effective date for the amendments set out in FRED 82 is accounting periods beginning on or after 1 January 2025, with early application permitted provided all amendments are applied at the same time. Do you agree with this proposal? If not, why not?*

Answer: **I do not** (not for IFRS 16 in any case) as I don't believe this would be sufficient time preparation time- I would suggest a further 1 year to 1 January 2026.

Given that some SMEs may have extensive leasing activities organisations may need more time than given for an effective implementation date of 1 January 2025.

There potentially is a big data gathering exercise that is required to get all the information required (the actual lease contracts (which may or may not be easily locatable), lease term, discount rates etc) as well as make business decisions as to whether to extend or to re-negotiate expiring leases.

Furthermore, any finance leases that SMEs may currently have (which maybe few and far between) may be accounted for on spreadsheets and given that current operating leases will have to be incorporated (which are probably greater in number) they may need accounting software to be installed-this will take time in itself.

The IASB gave a lead in time of 3 years from announcement (January 2016) to effective date (January 2019), I would suggest @ least a 2 year lead in time for Section 20 to be updated.

Question: FRED 82 proposes transitional provisions (see paragraphs 1.35 to 1.60 of FRS 102 and paragraph 1.11 of FRS 105). In respect of leases, FRED 82 proposes to permit an entity to use, as its opening balances, carrying amounts previously determined in accordance with IFRS 16. This is expected to provide a simplification for entities that have previously reported amounts in accordance with IFRS 16 for consolidation purposes, promoting efficiency within groups. Do you agree with this proposal? If not, why not?

Answer: **I do**

Question: Otherwise, FRED 82 proposes to require the calculation of lease liabilities and right-of-use assets on a modified retrospective basis at the date of initial application. Do you agree with this proposal? If not, why not?

Answer: **I would agree with this proposal as an alternative**

Yours faithfully

Stephen Bowen FCCA