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28 April 2023

Dear Sirs

Response to consultation on FRED 82: Draft Amendments to FRS 102 and other FRSs (December 2022)

Buzzacott is pleased to respond to the FRC's consultation on FRED 82. Please find our response to certain questions below:

Question 6: Leases:

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? If not, why not?

Response:

We agree with the proposals and support the enhanced comparability between UK GAAP and IFRS that they bring.

However, we note that there will be implications for public benefit entities where properties are often leased at discounted rates where donors support the entity's activities. Recognising these right of use assets, the corresponding liabilities and non-exchange transaction to reflect the market value of the rent may significantly alter the picture presented in the financial statements. There is often considerable public (and donor) interest in the financial statements for this sector, especially in relation to costs. We therefore consider that an exemption to allow not for profit entities to recognise the balance sheet asset and liability based on the actual lease payments, and to disclose details of the donated or discounted element of leases in the notes would be appropriate. This would allow the sector to achieve a balance between transparency and the accessibility of the financial statements to their users.

In addition, where public benefit entities are given the use of a property at no charge or at a peppercorn rent, we consider that an exemption to allow this to be recognised as a 'donation in kind' with no associated debt on the balance sheet would be appropriate.

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

Response:

Although we debated if we would support more simplifications in recognition and measurement of leases for small companies (as these could prevent disproportionate costs), we have concluded that we agree that having additional "tiers" of recognition and measurement (where we already have three – FRS 105, FRS 102 and IFRS) is not desirable in principle. Therefore, we agree that there should be no recognition or measurement differences for small companies applying FRS 102 and that FRS 102 should align with IFRS.

That being said, we do note that, following Brexit, there may now be an opportunity for the FRC to look at changing FRS 105 (which is not a 'true and fair' framework) and replace this with a proportionate 'true and fair' standard for smaller UK entities (perhaps with higher thresholds than the current Micro thresholds). This would allow more smaller UK entities access to a proportionate regime without adding an additional recognition and measurement "tier".

Question 7: Revenue

Question: Do you agree with the proposals to revise Section 23 of FRS 102 and Section 18 of FRS 105 to reflect the revenue recognition model from IFRS 15, with simplifications? If not, why not?

Response:

We agree with this approach, but we note that the wording in the revenue recognition model within paragraph 23.3 is slightly different from that in IFRS 15, for example step 2 of the model refers to identifying the promises in the contract whereas IFRS15 paragraph 22 refers to identification of performance obligations. We appreciate that the intention is to simplify the language, but we consider it is possible that this may cause confusion, especially for subsidiaries of groups reporting under IFRS.

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

Response:

We would like to see examples included in the standard, especially in cases where there may be accrued/deferred income or timing differences between transfer of risks/rewards and control. Without clear examples, there may be interpretation issues when applying the terminology to a common activity. We would suggest the examples cover the following areas:

- software as a service;
- revenue for professional practices (for example of lawyers, accountants and architects);
- sale of a property (exchange vs completion).

We would also welcome additional guidance, outside the standard, to be prepared by the FRC which covers the areas where there may be a difference in revenue recognition between the existing and revised versions of FRS 102.

Question 8: Effective Date and Transitional Provisions

Question: FRED 82 proposes to permit an entity to use, as its opening balances, carrying amounts previously determined in accordance with IFRS 16. Do you agree with this proposal? If not, why not?

Response:

Yes, we agree.

Question: 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?

Response:

Our interpretation of paragraph 35.10(x) was that this allowed an accounting policy choice as to whether a lease existed based on the facts and circumstances at the transition date or at the date of the commencement of the contract. We believe that this could lead to non-comparable financial statements across the sector where entities choose different options so we would welcome additional clarity in this area.

However, we feel that the provisions in paragraphs 35.10(x)(I-iv) provide a pragmatic approach to setting discount rates and treatment of short-term leases which we welcome.

We acknowledge that the FRC's usual policy is to publish on its website all responses to formal consultations issued by the FRC and therefore that this letter may be made publicly available.

Yours faithfully