Shepherd Group

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International Accounting Standards Board

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Exposure Draft ED/2013/6, Leases

Dear Sir

We appreciate this opportunity to comment on the latest exposure draft on Leases.

Shepherd Group is a privately owned manufacturing and construction Group based in the UK, employing around 3,200 people and with consolidated Revenue of circa £700m. Within our Group is a company which manufactures modular buildings for hire and sale.

We are pleased to observe that the latest exposure draft has removed some areas of subjectivity and complexity from the proposals. However the new proposals introduce their own issues and our key observations are summarised as follows:

Short Term Leases
We welcome the proposal to permit short term leases to be accounted for in a similar manner to the existing operating lease rules. However as we commented in 2010 we believe that some lease arrangements, which have the ability to extend beyond 12 months, exhibit characteristics which warrant a similar treatment. We would therefore ask that, in the interest of avoiding increasing accounting complexity unnecessarily, the board consider widening this concession. In particular we would suggest that the abilty to extend a lease arrangement beyond 12 months should not in itself prohibit an arrangement being considered as "short term". In these circumstances there would clearly be no obligation for the lessee to extend. It would therefore appear to be inappropriate to treat this arrangement as a type A lease for no other reason than there is an ability to extend within the lease contract.

Type A and Type B leases
We agree with the board that a single accounting model for leases is not practical. However we do not believe that the proposed split between Type A and Type B leases draws the correct distinction and the wording is inconsistent.

Under paragraph 29 a lease would fall to be a Type B Lease if "*the lease term is for an insignificant part of the* ***total*** *economic life of the underlying asset*". However under paragraph 30 the lease would be classified as a type B lease if "*the lease term is for the major part of the* ***remaining*** *economic life of the underlying asset*". It is therefore extremely difficult to ascertain how an asset which has been leased a number of times during its life but is now reaching the end of its useful life would sit within these definitions. In a situation where one particular lease contract contained many individual homogenous assets, which could well be at different points in their life cycle, it would be impractical to treat some as Type A and some Type B leases simply due to their age profile. We would therefore recommend that the wording in paragraph 29 be retained and paragraph 30 be amended to be consistent.

Type B lease accounting
We welcome the P&L charge for Type B leases being allocated on a straight line basis. However we are concerned that the methodology used for accounting for Type B leases is conceptually unsound as the amortisation of the asset is a balancing figure leaving a meaningless valuation for the asset carrying value.

Lessor Accounting

We welcome the process of accounting under Type B leases but feel that there should be more clarity regarding the nature of Type B leases. Particularly in relation to assets approaching the end of their useful lives.

From a lessor perspective your proposals (in paragraph 30 as outlined above) would imply that the last time a particular asset is leased, the lease contract would have to be regarded as a Type A lease regardless of the class of asset or nature of the lease. This does not appear to be practical or sensible.

We are concerned that the proposals for accounting for Type A leases are extremely complex and therefore it is highly likely that companies and their auditors will be forced to be pragmatic about the level of accuracy with which calculations can be made for each and every lease transaction. In addition we are concerned that the impact of the proposals will be to accelerate revenue declaration, and therefore potentially tax payments, for lessor companies. We would also question whether the accounts of lessors will actually be more meaningful to users of the accounts following these changes.

Tax implications

We are concerned about the tax implications of the changes and the uncertainty which these fundamental accounting changes will create. Tax implications for lease arrangements can be extremely complex and are an important factor in lease pricing models. It is therefore vital that the transitional arrangements take this into consideration.

These requirements remain extremely complex and will place a significant extra burden on companies and we are concerned that there is a danger that if tax authorities do not adjust legislation to accommodate the changes companies will be required to prepare 2 sets of numbers in parallel, which will only add to this burden.

Conclusions

We very much appreciate the attempts to simplify the procedures and remove some of the areas of subjectivity in the previous proposals. However these proposals will place a burden on companies and we question whether the accounts will actually give any more useful information to readers as a result, particularly with regard to lessor accounting.

Yours faithfully

J Rose
Group Finance Controller