Linda Feeney

From: Edward Beale <Edward.Beale@city-group.com>
Sent: 01 December 2016 14:08
To: UKFRS
Subject: Triennial Review

Dear Jenny

I am responding on behalf of Western Selection plc to the FRC's consultation document on its triennial review of accounting standards.

Western Selection is an investment company which prepares its own accounts under IFRS, and as such our comments on UK standards are from an investor perspective.

Accounts are a tool for the communication of information by boards to shareholders and other stakeholders. Changes to accounting standards should only be contemplated where they will improve the quality of this communication. IFRS are not perfect and, the FRC should demonstrate thought leadership in diverging from IFRS where this will promote better communication. Conversely requiring accounting treatments that impair or impede effective communication damages the reputation of the FRC and diminishes respect for UK GAAP.

Many of the users of accounts will not be experts in financial accounting and therefore communication needs to be pitched in a manner that is understandable to the target audience. While I can unpick (with some effort) financial accounting adjustments to reveal the underlying cash generation and the quantum and timing of future committed cash inflows and outflows, which we use to assess a business, many of my colleagues struggle with this complexity and we waste valuable time.

Our responses to your questions are as follows:

Question 1
The principles need to be examined in the light of the objective.

The FRC's stated objective is "to enable users of accounts to receive high-quality understandable financial reporting...". "High-quality" is not defined and there is a suspicion that the FRC understands this to mean "consistent with IFRS". It would be useful if the FRC could clearly set out what it understands by the term "high-quality". An objective of "easily understandable financial reporting" would in our view be clearer. The FRC's focus should not waver from the quality of communication.

We think that the principles need to be extended to acknowledge that the target audience for accounts are not expert accountants, and that standards will need to lead to the presentation and disclosure of information in a manner that is understandable by this target audience.

Question 2
IFRS, while in theory principles based, include many rules, a considerable number of which are designed to restrict opportunities for abuse. The FRC should as a matter of principle be promoting principles based accounting and should not include such anti-abuse rules in its standards. The FRC should rely on the other extensive checks and balances in the system of accounts preparation to minimise abuse. If these other checks and balances are not deemed to be sufficient then the FRC should be seeking to strengthen these checks and balances, or replace them with more effective ones, rather than distorting accounting standards. Accounting standards should not be the mechanism for restricting impropriety.

As a matter of policy the FRC should not seek to amend IFRS 2 for changes to IFRS before there has been a post implementation review of those IFRS changes. Earlier implementation could result in changes being made to FRS102, that then require further amendment following post implementation review changes to IFRS.

Our comments on specific IFRS are as follows:
IFRS 3 – agree no changes
IFRS 9 – see response to Qu. 3 below
IFRS 10 & 11 – see response to Qu. 6 below
IFRS 12 – agree no changes
IFRS 13 – The FRC should review the use of fair values which are not directly or indirectly based on market values to determine whether such fair values communicate useful information in a proportionate manner. In our opinion marking to model is rarely informative, as small changes to model inputs usually result in large changes to model outputs. The use of marking to model complicates our identification of cash generation, and our assessment of the quantum and timing of future committed cash inflows and outflows.
IFRS 15 – agree no changes
IFRS 16 – see response to Qu. 5 below.

Question 3
The expected loss model is overly complex for businesses that are not financial institutions. Ideally the FRC should revert to a system of general and specific provisioning which will be a clearer method of achieving similar outcomes. If current impairment requirements in FRS 102 are functioning effectively, the FRC should not be seeking to change them, so we favour option (c).

Question 4
Sections 11 & 12 of FRS 102 are overly complex and inhibit the communication of high-quality information regarding the cash generation of a business and the quantum and timing of future committed cash inflows and outflows. Rather than tinkering, these two sections need a total re-write.

Question 5
The objective of increasing visibility of future cash outflows relating to leases can be achieved in a more proportionate manner by better disclosure of the quantum and timing of such cash flows, as opposed to bringing a net present value onto the statement of financial position.

The FRC will be justified in assuming that users of accounts will read disclosures in the accounts as well as examining the primary statements. Presenting information solely in note disclosures should not be assumed to mean that this information will be overlooked, or that the primary statements are in some way less technically complete.

Question 6
The FRC should not make changes to better align FRS 102 with IFRS 10 and IFRS 11 unless these meets its principle of balancing improvements with stability.

Question 7
Share option accounting currently relies on the use of complex mathematical models. **None of these models have been validated in the real world for the size and nature of companies applying FRS 102. Output from such models is therefore as valid as a wild guess.** The current approach is potentially misleading and certainly ineffective. The FRC should not be allowing (let alone encouraging) the use of such models unless and until they have been suitably validated. A disclosure only approach for share options will reduce the number of non-cash adjustments required to get from PBT to cash generation, while presenting a complete information set to users. Presenting information solely in note disclosures should not be assumed to mean that this information will be overlooked.

Question 8
The proposed dates appear manageable but will need to be reviewed in the light of the actual changes proposed by the FRC.

Questions 9 & 10
No comment.

I will be happy to discuss any of these responses in more detail .

Kind regards
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