Triennial review of accounting standards

Submission from the Association of Investment Companies

The Association of Investment Companies (AIC) welcomes the opportunity to respond to the Financial Reporting Council's (FRC) consultation document on the triennial review of UK and Ireland accounting standards.

The AIC represents 345 closed-ended investment companies with assets under management of over £144 billion. Investment companies have their shares admitted to trading on public stock markets.

The AIC's members include UK investment trusts, Venture Capital Trusts, UK REITs and non-EU companies. Our non-EU members are primarily Channel Islands domiciled.

Approximately half our members, by number, use UK GAAP. The majority of our remaining members use IFRS.

Question 1 - The FRC has reviewed its principles for developing succinct financial reporting standards for the UK and Republic of Ireland. As a result, limited changes have been made to the principles, to emphasise the need to balance improvement with stability and the need for proportionate solutions (see paragraph 1.11). Do you agree with the principles? If not, why not?

The AIC **agrees** with the limited changes that have been proposed.

Question 2 - Significant changes in IFRS have been considered against the FRC's principles for developing succinct financial reporting standards for the UK and Republic of Ireland; see Section 3 Changes in IFRS – Detailed analysis. Do you agree with the proposals for updating FRS 102 as result of changes in IFRS as part of this triennial review? If not, please provide alternative suggestions.

The AIC **agrees** with proposals for updating FRS 102.

Question 3a - In relation to the impairment of financial assets, the FRC proposes to amend FRS 102 in order to incorporate an expected loss model. Paragraph 3.13 sets out three options for how this may be achieved, with the FRC favouring option (b). Which option would you prefer, and why?

The AIC **recommends** that the FRC adopts option (b) for the reasons it states in the discussion paper.

Additionally, the AIC **recommends** that it is applied only to a sub-set of financial institutions.

IFRS 9 was developed to rectify the weaknesses of IAS 39 in the wake of the financial crisis. The AIC agrees that large financial institutions, particularly banks, should have recognised larger credit losses than they did, quicker than they did.

IFRS 9 was written with banks and building societies in mind, it is not appropriate to use the expected loss model for other companies.

In amending FRS 102, the FRC should follow its objective to develop standards "*proportionate to the size and complexity of the entity and user's information needs".* Therefore, the amendments in relation to impairment of financial assets, should apply only to certain categories of large financial institutions.

This should not include investment trusts and VCTs which are defined as financial institutions under FRS 102.

To deliver proportionate standards, and focus on financial institutions that present systemic risk, the FRC should exclude funds. The AIC **recommends** that companies specified in paragraph g[1] of the definition of financial instruments under FRS 102 are specifically excluded.

Question 3b - Do you have any suggestions for how the simplified approach to impairment losses for trade receivables, contract assets and lease receivables in IFRS 9 might be developed into a suitable model for entities applying FRS 102 (other than financial institutions, or a sub-set such as banks and building societies)?

See response to question 3a.

Question 4 - Presently, in paragraph 11.2 (and paragraph 12.2), FRS 102 permits an accounting policy choice in relation to financial instruments, allowing an entity to choose the recognition and measurement requirements of FRS 102, IAS 39 Financial Instruments: Recognition and Measurement or IFRS 9 Financial Instruments (and elements of IAS 39 as amended by IFRS 9). The FRC proposes to retain the option to choose IAS 39 until the requirements for the impairment of financial assets have been amended in FRS 102 (i.e. for all accounting periods beginning before 1 January 2022). From 1 January 2022 the FRC proposes that the available options will be the requirements of FRS 102 or IFRS 9. Do you agree? If not, why not?

The AIC **agrees** with these proposals.

Question 5 - Do you have any suggestions for how the requirements of IFRS 16 Leases might be developed into a suitable model for entities applying FRS 102? In particular, do you have any suggestions relating to the application of the short-term lease exemption or the exemption for leases when the value of the underlying asset is low?

The AIC does not have any comment on this question.

Question 6 - The FRC proposes to makes changes to FRS 102 to incorporate the control model of IFRS 10 Consolidated Financial Statements. Company law specifies

[1] FRS 102 defines a financial institution as any of the following…g) an investment trust, Irish Investment Company, venture capital trust, mutual fund, exchange traded fund, unit trust, open-ended investment company (OEIC)

when consolidated financial statements are prepared, and any changes would supplement these existing requirements by providing further guidance on what is meant by 'control'. Are you aware of any legal barriers to incorporating the control model of IFRS 10 alongside the existing legal requirements?

In most situations, any changes to the definition of control in FRS 102 will have no impact in practice. However, in other cases entities may be consolidated for the first time or cease to be consolidated. Do you have any information about how significant the practical impact may be and the circumstances in which it might occur?

The AIC does not have any comment on this question.

Question 7 - Do you have any comments on the cost-effectiveness of the requirements for share-based payments, currently set out in Section 26 Share-based Payment of FRS 102? If you consider that alternative requirements would be more cost-effective, please provide details of how you would adapt the current requirements whilst still providing useful information to users.

The AIC does not have any comment on this question.

Question 8 - Do you agree with the proposed effective dates for the amendments arising from the triennial review, with incremental improvements and clarifications effective from 1 January 2019 and more fundamental changes effective from 1 January 2022?

The AIC **recommends** that proposed effective dates are consulted on as part of the FREDs that will be issued for phase 1 and phase 2 of this review. Until companies are able to see these exposure drafts they cannot fully assess how long a period will be required to make the necessary changes to their accounting systems.

In any event, the AIC **recommends** this should be effective no earlier than the dates suggested by the FRC.

Question 9 - Do you have any other comments on the approach to keeping FRS 102 up-to-date as part of the triennial review?

Given the significant changes required by companies when they adopted to FRS 102 for the first time, updates in this triennial review should be kept to a minimum. This will allow companies time to fully embed the new accounting standard with minimal disruption.

Question 10 - The FRC will be preparing consultation stage impact assessments to accompany the FREDs arising from the triennial review. At this stage do you have any comments on the costs and benefits likely to arise from the outline proposals in this Consultation Document that will help inform those impact assessments? Please provide evidence to support your views of any quantifiable costs or benefits.

The AIC does not have any comment on this question.

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To discuss the issues raised in this paper please contact:

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