15 January 2014

Hans Hoogervorst
Chairman
IFRS Foundation
30 Cannon Street
London
EC4M 6XH

Dear Hans

A REVIEW OF THE CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING - DISCUSSION PAPER

IMA represents the asset management industry operating in the UK. Our members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of £4.4 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles. In particular, IMA members manage holdings amounting to just over 30% of the domestic equity market.

In managing assets for both retail and institutional investors, IMA members are major investors in companies whose securities are traded on regulated markets. Therefore, they have an interest in the standards governing how such companies prepare their financial statements and the information disclosed to them as users.

IMA supports the development of high quality accounting standards that are applied consistently internationally. This should maximise the transparency and comparability of financial statements for our members. We very much welcome the IASB revisiting the Conceptual Framework (CF) and bringing it up-to-date so that consistent concepts are applied when IFRS are developed or revised. The overall focus of the CF should be to ensure that financial statements prepared under the IFRS accounting framework give a true and fair view.

We also agree with a number of the proposals in the DP, for example:

- **The mixed attribute model.** We support the mixed attribute model and two measurement bases of amortised cost and fair value where the latter, mark to market or

65 Kingsway London WC2B 6TD
Tel:+44(0)20 7831 0898 Fax:+44(0)20 7831 9975

www.investmentuk.org

mark to model, is applied to financial instruments that are not held for the long-term. A single measurement basis would not necessarily provide relevant information.

- **A sub-total for profit or loss.** We welcome a sub-total for profit and loss being retained. This should give a clear indication to investors of the return management has made on the economic resources entrusted to it in the period.

- **The current definition of equity.** We support the current definition of equity as this is consistent with a proprietary perspective. As set out below, we believe the primary users of financial statements are the equity shareholders. Thus as opposed to the "entity perspective" which looks top-down at the entity, we believe accounting should be based on the "parent entity perspective". The latter is where the assets and liabilities of an entity, even if that entity is not fully owned, are consolidated in full, and non-controlling interests are separately identified such that the financial statements reflect what the shareholders of the consolidated parent company own.

There are other of the proposals, however, where we have certain reservations. Our key reservations are set out below and our comments on the detailed questions in the attached Annex.

- **Primary users and the concept of stewardship or accountability**. The 2010 CF states that "the objective of general purpose financial reporting is to provide financial information that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to an entity".

We consider this too broad and firmly believe that the primary audience should be the holders of ordinary shares. These are the ultimate owners of a company, the providers of the risk capital and bearers of the residual risk. Financial statements should provide them with the information they need, not only for the purposes of deciding to buy, sell or hold their shares, but also to fulfill their responsibilities as owners – assessing company management and the strategies adopted for the longer term.

In particular, investors tend to base investment decisions and their assessment of future prospects on various sources of information; much of which is produced outside the annual reporting framework - via analyst briefings, investor meetings, strategy presentations, stock exchange announcements and certain non-financial information. Moreover, financial statements are published some time after the events to which they relate and in looking backwards and focusing on past performance, they are essentially confirmatory. Investors value them in so far as they demonstrate management's accountability – it is entrusted with the assets of the entity and financial statements should show how effectively it put those assets to use and the performance derived from those assets. This is the concept of accountability or stewardship. Whilst the objectives of financial reporting in Chapter 1 encompass this concept, we believe it should be equal in prominence to that of providing information that is decision useful.

- **Profit and loss should be defined.** It is important that the IASB develops a robust definition of profit and loss in the CF. This should accord with what investors really want to know, i.e. what management has generated from its operations and the resources allocated to it in the period. Management's accountability for its performance includes, but is by no means limited to, the link between executive remuneration and how the reporting entity creates, delivers, and captures value. In the absence of a clear definition, changes in net assets that do not represent business activity or result in cash flows can be reported as part of performance. There also needs to be a closer alignment between reporting and the business model to enable shareholders to hold management accountable for the execution of its business model and the creation of true shareholder value.

- **Prudence.** The concept of prudence, which was removed in 2010, should be specifically written into the CF. Investors want companies to err on the side of caution, i.e. be prudent, at an individual item level in the face of uncertainty, such that:

    - There is later rather than earlier recognition of revenues and assets;
    - There is earlier rather than later recognition of costs (incl. impairments) and liabilities; and
    - Assets and income are not overstated and liabilities and costs are not understated.

    We believe prudence should be a fundamental qualitative characteristic for guiding preparers (and auditors) when recognition involves estimates. We do not consider the prudence is necessarily incompatible with neutrality in that the former should prevail when there is uncertainty. It should also be possible for the CF to refer to it without it being used for income smoothing. Moreover, IFRS already requires prudence in that:

    - Revenue is recognised over time, but losses are recognised up front if the contract is onerous (i.e. at unfavourable terms).
    - Liabilities must be recorded for guarantees or warranties, even when they have not yet been called in.
    - Inventory is typically carried at lower of cost or net realisable value; again a prime example of exercising caution.
    - Both assets and liabilities measured at fair value are adjusted for risk. This reflects the effect of uncertainty by increasing the measure of a liability or decreasing the measure of an asset.
    - Asset impairment tests are required to ensure that the carrying amount in the statement of financial position is not greater than the [market] value of the asset and the IASB is moving to an expected from an incurred loss model.
    - Strict rules about balance sheet presentation give as complete a picture of an entity's exposure as possible to the investor.
    - Limited netting of derivatives and other financial instruments.
    - Consolidation rules are based on the principle of control rather than a "50%+1" bright line.
    - The IASB is proposing that entities should recognise all leases on the balance sheet.

- **Each primary statement should be of equal importance**. The current approach whereby the key defined elements are assets and liabilities and changes in those assets and liabilities are income and expense gives too much priority to the statement of financial position. Each of the primary statements should be of equal importance.

- **Reliability as a qualitative characteristic.** Financial statements will always contain estimates that have a degree of uncertainty. Investors want to trust the information reported and these estimates should be the best in the circumstances in that a certain level of precision is necessary. We do not consider that "freedom from material error" which is in the definition of "faithful representation" necessarily captures this. Unreliable estimates should not be included in financial statements and "reliability" should be a separate qualitative characteristic.

- **Substance over form**. Similarly substance over form is no longer a component of faithful representation. This is a well understood concept and we consider that "economic substance over accounting and legal form" is an essential qualitative characteristic of financial reports and should be re-introduced.

- **Going Concern.** The DP refers to the going concern concept in the existing CF but it is unclear what is proposed. We consider that this should continue to be one of the fundamental concepts that underlie financial reporting and it is important it is retained.

I trust that the above and the attached are self-explanatory but please do contact me if you require any clarification of the points in this letter or if you would like to discuss any issues further.

Yours sincerely

Liz Murrall
Director, Corporate Governance and Reporting

IMA'S ANSWERS TO THE DETAILED QUESTIONS RAISED

IMA's answers to the detailed questions raised are set out below.

Section 1 Introduction

> 1. *Paragraphs 1.25-1.33 set out the proposed purpose and status of the Conceptual Framework. The IASB's preliminary views are that:*
>
> *(a) the primary purpose of the revised Conceptual Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs; and*
> *(b) in rare cases, in order to meet the overall objective of financial reporting, the IASB may decide to issue a new or revised Standard that conflicts with an aspect of the Conceptual Framework. If this happens the IASB would describe the departure from the Conceptual Framework, and the reasons for that departure, in the Basis for Conclusions on that Standard.*
>
> *Do you agree with the preliminary views? Why or why not?*

IMA agrees that the primary purpose of the CF should be to identify consistent concepts to be used when the IASB develops and revises IFRS and that in rare cases, where IASB decides to issue an IFRS that conflicts with an aspect of the CF, it should describe the departure and the reasons for it in the Basis for Conclusions. In this context, the CF is not just for the development of individual standards but also for ensuring consistency between standards as a whole. The overall aim of the CF should be that financial statements prepared under the IFRS accounting framework give a true and fair view.

We agree that the IASB should review the framework from time to time in the light of its experience (CF 1.33) in that we consider it important that it continually evolves.

Section 2 Elements of Financial statements

> 2. *The definitions of an asset and a liability are discussed in paragraphs 2.6-2.16. The IASB proposes the following definitions:*
>
> *(a) an asset is a present economic resource controlled by the entity as a result of past events.*
> *(b) a liability is a present obligation of the entity to transfer an economic resource as a result of past events.*
> *(c) an economic resource is a right, or other source of value, that is capable of producing economic benefits.*
>
> *Do you agree with these definitions? Why or why not? If you do not agree, what changes do you suggest, and why?*

IMA supports these definitions. The removal of the word 'expected' from the definitions of both an asset and a liability is an improvement in that it implied a probability threshold and led to differing interpretations by both preparers and users of financial statements.

The proposed definitions share the benefit of brevity but to avoid too broad an interpretation for assets and too narrow an interpretation for liabilities – hence the need to separately address constructive obligations - recognition criteria at a standards level are important. In this context, the term "capable" is very broad – many assets can be capable - and the IASB may wish to reconsider this. Moreover, whilst guidance in the CF is desirable, too much could be interpreted as rules rather than principles and should be avoided.

IMA'S ANSWERS TO THE DETAILED QUESTIONS RAISED

3. Whether uncertainty should play any role in the definitions of an asset and a liability, and in the recognition criteria for assets and liabilities, is discussed in paragraphs 2.17-2.36. The IASB's preliminary views are that:

(a) the definitions of assets and liabilities should not retain the notion that an inflow or outflow is 'expected'. An asset must be capable of producing economic benefits. A liability must be capable of resulting in a transfer of economic resources.
(b) the Conceptual Framework should not set a probability threshold for the rare cases in which it is uncertain whether an asset or a liability exists. If there could be significant uncertainty about whether a particular type of asset or liability exists, the IASB would decide how to deal with that uncertainty when it develops or revises a Standard on that type of asset or liability.
(c) the recognition criteria should not retain the existing reference to probability.

Do you agree? Why or why not? If you do not agree, what do you suggest, and why?

The DP discusses existence and outcome uncertainty. Investors would not welcome the use of probability thresholds to determine the existence of an asset or liability. Nor do we consider the reference to probability should be retained in the recognition criteria (DP2.35). Probability thresholds should be addressed at standards level in that it is important that there are safeguards against the recognition of assets and liabilities where to do so merely contributes to clutter and does not provide useful information. In this context, we consider "relevance" should also be considered when evaluating whether an asset or liability is recognised and we would welcome indicators of relevance being given in the CF.

4. Elements for the statement(s) of profit or loss and OCI (income and expense), statement of cash flows (cash receipts and cash payments) and statement of changes in equity (contributions to equity, distributions of equity and transfers between classes of equity) are briefly discussed in paragraphs 2.37-2.52.

Do you have any comments on these items? Would it be helpful for the Conceptual Framework to identify them as elements of financial statements?

IMA welcomes the IASB addressing performance reporting in the CF. Investors would like clarity around profit or loss reporting performance from operations and OCI, however determined, reporting other results for the period. However, not all items in the profit and loss or in OCI are necessarily income or expense and it may be more helpful if the CF referred to gains and losses. These would include income and expense but also revaluations and losses, however, caused.

In addition, the current approach whereby the key defined elements are assets and liabilities and changes in those assets and liabilities are income and expense gives too much priority to the statement of financial position. Each of the primary statements should be of equal importance.

Moreover, only the elements as defined should be reported in the primary financial statements, and the CF needs to define those elements. However, we do not believe cash receipts and payments necessarily need to be defined

Section 3 Additional guidance to support the asset and liability definitions

5. Constructive obligations are discussed in paragraphs 3.39-3.62. The discussion considers the possibility of narrowing the definition of a liability to include only obligations that are enforceable by *legal or equivalent means. However the IASB tentatively favours retaining the existing definition, which encompasses both legal and constructive obligations – and adding more guidance to help distinguish constructive obligations from economic compulsion. The guidance would clarify the matters listed in paragraph 3.50.*

Do you agree with this preliminary view? Why or why not?

IMA agrees that constructive obligations should be recognised as liabilities rather than liabilities simply being those that are enforceable legally or by equivalent means. Investors need information on likely future cash flows from economic realities.

We agree with the preliminary view in DP3.62 of need for more guidance to distinguish constructive obligations from economic compulsion because the latter does not necessarily involve an obligation to another party to act in a particular way (DP3.45 & 46). Investors would expect a duty or responsibility to a third party to be recognised as a liability.

6. The meaning of 'present' in the definition of a liability is discussed in paragraphs 3.63-3.97. A present obligation arises from past events. An obligation can be viewed as having arisen from past events if the amount of the liability will be determined by reference to benefits received, or activities conducted, by the entity before the end of the reporting period. However, it is unclear whether such past events are sufficient to create a present obligation if any requirement to transfer an economic resource remains conditional on the entity's future actions. Three different views on which the IASB could develop guidance for the Conceptual Framework are put forward:

(a) View 1: a present obligation must have arisen from past events and be strictly unconditional. An entity does not have a present obligation if it could, at least in theory, avoid the transfer through its future actions.
(b) View 2: a present obligation must have arisen from past events and be practically unconditional. An obligation is practically unconditional if the entity does not have the practical ability to avoid the transfer through its future actions.
(c) View 3: a present obligation must have arisen from past events, but may be conditional on the entity's future actions.

The IASB has tentatively rejected View 1. However, it has not reached a preliminary view in favour of View 2 or View 3.

Which of these views (or any other view on when a present obligation comes into existence) do you support? Please give reasons.

We support the IASB rejecting View 1. This is too narrow in that, for example, it would not permit an accrual of staff bonuses on the grounds they could be avoided by terminating the employment contract – even if this is unrealistic. This could conflict with prudence and the entity's business model. The IASB should explore a variation combining Views 2 and 3. It may be helpful to expand the number of examples, in that there is not enough differentiation in Tables 3.2 and 3.3.

7 . Do you have comments on any of the other guidance proposed in this section to support the asset and liability definitions?

The DP refers to the substance of a contract in 3.102 thereby indicating that this is being considered. IMA believes substance over form should be reinstated in the CF. This Qualitative Characteristic used to be in the pre-2010 CF in paragraph 35 but is not currently a component of faithful representation. This is a well understood concept and we consider that "economic substance over accounting and legal form" is an essential qualitative characteristic of financial reports and should be re-introduced.

In addition, we have concerns about DP3.112 which states that trade date accounting is inconsistent with the views in this DP. Trade date accounting is the general practice used by banks and is important for a true and fair view. Moreover, AG 53-56 of IAS 39 allows trade date accounting. We consider this should be addressed.

Section 4 Recognition and derecognition

8. Paragraphs 4.1-4.27 discuss recognition criteria. In the IASB's preliminary view, an entity should recognise all its assets and liabilities, unless the IASB decides when developing or revising a particular Standard that an entity need not, or should not, recognise an asset or liability because:

(a) recognising the asset (or the liability) would provide users of financial statements with information that is not relevant, or is not sufficiently relevant to justify the cost
(b) no measure of the asset (or the liability) would result in a faithful representation of either the asset (or the liability) and the changes in the asset (or the liability), even if all necessary descriptions and explanations are disclosed.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

It is important that the recognition criteria provide a safeguard against asset and liabilities being recognized where to do so merely contributes to clutter and does not provide useful information. In particular, the definition of assets is very broad in using the term "capable" – see answer to question 2. "Relevance" should be considered when evaluating whether an asset or liability is recognised and we would welcome indicators of relevance being given in the CF very much as outlined in DP4.26. These may include cases where the asset or liability is particularly difficult to identify or measure reliably.

9. In the IASB's preliminary view, as set out in paragraphs 4.28-4.51, an entity should derecognise an asset or a liability when it no longer meets the recognition criteria. (This is the control approach described in paragraph 4.36(a)). However, if the entity retains a component of an asset or liability, the IASB should determine when developing or revising particular Standards how the entity would best portray the changes that resulted from the transaction. Possible approaches include:

(a) enhanced disclosure
(b) presenting any rights or obligations retained on a line item different from the line item that was used for the original rights or obligations, to highlight the greater concentration of risk; or
(c) continuing to recognise the original asset or liability and treating the proceeds received or paid for the transfer as a loan received or granted.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

We believe further consideration is needed of the control approach and whether an entity should derecognise an asset or liability when it no longer meets this criterion. The risk and rewards approach is well understood in the UK and prohibits derecognition when there is no significant change to the entity's exposure to risks and rewards. We would welcome a derecognition approach that gave equal prominence to both concepts in the CF in that considering risks and rewards in determining whether control is maintained will help identify the substance of a transaction – see answer to question 7.

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We believe that the detail of derecognition is better addressed in individual standards, for example, the financial instruments or leasing standards because this is an area where it is most difficult to understand what has happened in practice. Thus we support the preliminary view that if the entity retains a component of that asset or liability then this should be determined on a standard by standard basis. This could be by enhanced disclosure; presenting any rights or obligations retained on a line item different from the line item that was used for the original rights or obligations to highlight the different concentration of risk; or continuing to recognise the asset or liability.

Section 5 Definition of equity and distinction between liabilities and equity instruments

10. The definition of equity, the measurement and presentation of different classes of equity, and how to distinguish liabilities from equity instruments are discussed in paragraphs 5.1-5.59. In the IASB's preliminary view:

(a) the Conceptual Framework should retain the existing definition of equity as the residual interest in the assets of the entity after deducting all its liabilities.
(b) the Conceptual Framework should state that the IASB should use the definition of a liability to distinguish liabilities from equity instruments. Two consequences of this are:
(i) obligations to issue equity instruments are not liabilities; and
(ii) obligations that will arise only on liquidation of the reporting entity are not liabilities (see paragraph 3.89(a)).
(c) an entity should:
(i) at the end of each reporting period update the measure of each class of equity claim. The IASB would determine when developing or revising particular Standards whether that measure would be a direct measure, or an all allocation of total equity
(ii) recognise updates to those measures in the statement of changes in equity as a transfer of wealth between classes of equity claim.
(d) if an entity has issued no equity instruments, it may be appropriate to treat the most subordinated class of instruments as if it were an equity claim, with suitable disclosure. Identifying whether to use such an approach, and if so, when, would still be a decision for the IASB to take in developing or revising particular Standards.

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

IMA agrees that the existing definition of equity as a residual should be retained and the views stated in (b). This is consistent with a proprietary perspective. As set out in the covering letter and in our answer to question 22, we believe the primary users of financial statements are the equity shareholders. Thus as opposed to the "entity perspective" which looks top-down at the entity, we believe accounting should be based on the "parent entity perspective". The latter is where the assets and liabilities of an entity, even if that entity is not fully owned, are consolidated in full, and non-controlling interests are separately identified such that the financial statements reflect what the shareholders of the consolidated parent company own.

With regard to (c), we are not convinced that updating the measure of each class of equity, for example, by reference to market value would provide useful information to investors. The amount that equity is stated in financial statements does not claim to represent the market value of the entity. In addition, although potential dilution through equity options can be important information, it is preferable for it to be in a note to the financial statements rather than in a primary statement.

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In relation to (d), we do not believe it should be necessary for the CF to address the situation when no equity instruments are issued because the substance over form concept and the definition of equity in the CF should ensure instruments are correctly reported which should be determined at a an individual standards level.

Section 6 Measurement

11 How the objective of financial reporting and the qualitative characteristics of useful financial information affect measurement is discussed in paragraphs 6.6-6.35. The IASB's preliminary views are that:

(a) the objective of measurement is to contribute to the faithful representation of relevant information about:
(i) the resources of the entity, claims against the entity and changes in resources and claims; and
(ii) how efficiently and effectively the entity's management and governing board have discharged their responsibilities to use the entity's resources.
(b) a single measurement basis for all assets and liabilities may not provide the most relevant information for users of financial statements;
(c) when selecting the measurement to use for a particular item, the IASB should consider what information that measurement will produce in both the statement of financial position and the statement(s) of profit or loss and OCI;
(d) the relevance of a particular measurement will depend on how investors, creditors and other lenders are likely to assess how an asset or a liability of that type will contribute to future cash flows. Consequently, the selection of a measurement:
(i) for a particular asset should depend on how that asset contributes to future cash flows; and
(ii)f or a particular liability should depend on how the entity will settle or fulfil that liability.
(e) the number of different measurements used should be the smallest number necessary to provide relevant information. Unnecessary measurement changes should be avoided and necessary measurement changes should be explained; and
(f) the benefits of a particular measurement to users of financial statements need to be sufficient to justify cost.

Do you agree with these preliminary views? Why or why not? If you disagree, what alternative approach to deciding how to measure an asset or a liability would you support?

IMA agrees that no single measurement basis would be appropriate in all circumstances. IMA supports the mixed attribute model and two measurement bases of amortised cost and fair value where the latter, mark to market or mark to model, are applied to financial instruments that are not held for the long term.

That said, the discussion of specific measurement bass is cursory and incomplete. Moreover, financial statements will always contain estimates that have a degree of uncertainty. Investors want to trust the information reported and these estimates should be the best in the circumstances in that a certain level of precision is necessary. We do not consider that "freedom from material error" which is in the definition of "faithful representation" necessarily captures this.

We understand the reasoning in paragraphs BC20-BC25 explaining that there were perceived problems with interpretation of reliability in the pre-2010 CF with some apparently believing that it meant precision. The 2010 CF in QC12 acknowledges that 'perfection is seldom, if ever, achievable'. We believe that this would go some way to addressing the concern over striving for precision and that it should be explained further what is meant by

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reliability rather than removing the term. In summary, unreliable estimates should not be included in financial statements and "reliability" should be a separate qualitative characteristic.

12 The IASB's preliminary views set out in Question 11 have implications for the subsequent measurement of assets, as discussed in paragraphs 6.73-6.96. The IASB's preliminary views are that:
(a) if assets contribute indirectly to future cash flows through use or are used in combination with other assets to generate cash flows, cost-based measurement normally provide information that is more relevant and understandable than current market prices.
(b) if assets contribute directly to future cash flows by being sold, a current exit price is likely to be relevant.
(c) if financial assets have insignificant variability in contractual cash flows, and are held for collection, a cost-based measurement is likely to provide relevant information.
(d) if an entity charges for the use of assets, the relevance of a particular measurement of those assets will depend on the significance of the individual asset to the entity.

Do you agree with the preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

As noted in question 11, the discussion of specific measurement basis is cursory and incomplete and considerably more work is needed. None of the bases: cost; current market price; and cash-flow are described in any detail, and as a result the extent to which they can be appraised is limited. A concern is that cash-flow based measurements are to be used when cost or current market prices are unavailable or unsuitable. They are, therefore, the default and likely to be used frequently.

Measurement issues that could usefully be addressed in the CF are:

- the relationship between entity specific and market values;
- reflecting transaction costs;
- changing prices; and
- the relationship between assets held to fund liabilities.

13 The implications of the IASB's preliminary views for the subsequent measurement of liabilities are discussed in paragraphs 6.97-6.109. The IASB's preliminary views are that:

(a) cash-flow-based measurements are likely to be the only viable measurement for liabilities without stated terms.
(b) a cost-based measurement will normally provide the most relevant information about:
(i) liabilities that will be settled according to their terms; and
(ii) contractual obligations for services (performance obligations).
(c) current market prices are likely to provide the most relevant information about liabilities that will be transferred.

Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

We agree with the preliminary views with regard to subsequent measurement of liabilities that cash flow based measurements are likely to be the only viable alternative for liabilities without stated terms. Investors expect liabilities to be reported at the amount due on settlement, with discounting being specified at standards level.

With regard to liabilities that will be transferred, it is expected that this will be comparatively rare. For insurance liabilities, we note that fulfillment value is proposed for the reason that insurance liabilities are not routinely transferred. In addition, we agree with the tentative conclusion in paragraph 6.130 that own credit should be included in the estimate of a liability if the uncertainty in a cash flow reflects a market perspective. However, we would expect the CF to address how these gains and losses should be reported in the primary statements.

14 Paragraph 6.19 states that the IASB's preliminary view that for some financial assets and financial liabilities (for example, derivatives), basing measurement on the way in which the asset contributes to future cash flows, or the way in which the liability is settled or fulfilled, may not provide information that is useful when assessing prospects for future cash flows. For example, cost-based information about financial assets that are held for collection or financial liabilities that are settled according to their terms may not provide information that is useful when assessing prospects for future cash flows:

(a) if the ultimate cash flows are not closely linked to the original cost;
(b) if, because of significant variability in contractual cash flows, cost-based measurement techniques may not work because they would be unable to simply allocate interest payments over the life of such financial assets or financial liabilities; or
(c) if changes in market factors have a disproportionate effect on the value of the asset or the liability (i.e. the asset or the liability is highly leveraged).

Do you agree with this preliminary view? Why or why not?

We agree with the preliminary view.

15 Do you have any further comments on the discussion of measurement in this section?

Investors would expect the CF to explain more fully the meaning of the various terms used in the measurement section. For example:

- that cost means historical cost and not current cost or replacement cost;
- the meaning of value;
- that cost is a value distinct from fair value.

Section 7 Presentation and disclosure

16 This section sets out the IASB's preliminary views about the scope and content of presentation and disclosure guidance that should be included in the Conceptual Framework. In developing its preliminary views, the IASB has been influenced by two main factors:

(a) the primary purpose of the Conceptual Framework, which is to assist the IASB in developing and revising Standards (see Section 1); and
(b) other work that the IASB intends to undertake in the area of disclosure (see paragraphs 7.6-7.8), including:
(i) a research project involving IAS 1, IAS 7 and IAS 8, as well as a review of feedback received on the Financial Statement Presentation project;
(ii) amendments to IAS 1; and
(iii) additional guidance or education material on materiality.
Within this context, do you agree with the IASB's preliminary views about the scope and content of guidance that should be included in the Conceptual Framework on:
(a) presentation in the primary financial statements, including:
(i) what the primary financial statements are;
(ii) the objective of primary financial statements;
(iii) classification and aggregation;

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(iv) offsetting; and
(v) the relationship between primary financial statements.
(b) disclosure in the notes to the financial statements, including:
(i) the objective of the notes to the financial statements; and
(ii) the scope of the notes to the financial statements, including the types of information and disclosures that are relevant to meet the objective of the notes to the financial statements, forward-looking information and comparative information.

Why or why not? If you think additional guidance is needed, please specify what additional guidance on presentation and disclosure should be included in the Conceptual Framework.

With regard to the primary purpose, see answer to question 1 above. We welcome the IASB's other work in the area of disclosure. However, the scope of the CF should be limited to those disclosures that relate to the content of the financial statements. This is in line with the primary purpose of the CF being to assist in the development of IFRS. We do not expect the CF to address disclosures outside the financial statements and elsewhere in the annual report, for example, in the management commentary. These requirements are generally set by international standard setters.

We agree that the proposals in DP7.35 are areas for disclosure requirements at standards level and would support the objective of the notes as stated in DP7.33.

17 Paragraph 7.45 describes the IASB's preliminary view that the concept of materiality is clearly described in the existing Conceptual Framework. Consequently, the IASB does not propose to amend, or add to, the guidance in the Conceptual Framework on materiality. However, the IASB is considering developing additional guidance or education material on materiality outside of the Conceptual Framework project.

Do you agree with this approach? Why or why not?

We agree with the above approach. In the interests of 'cutting clutter' it is important for investors not to have to work through immaterial items in order to arrive at information that is important to them.

18 The form of disclosure requirements, including the IASB's preliminary view that it should consider the communication principles in paragraph 7.50 when it develops or amends disclosure guidance in IFRSs, is discussed in paragraphs 7.48-7.52.

Do you agree that communication principles should be part of the Conceptual Framework? Why or why not?

If you agree they should be included, do you agree with the communication principles proposed? Why or why not?

We agree with the communication principles proposed and welcome the emphasis on communication to investors as opposed to a compliance exercise for preparers.

Section 8 Presentation in the statement of comprehensive income – profit or loss and other comprehensive income

19. The IASB's preliminary view that the Conceptual Framework should require a total or subtotal for profit or loss is discussed in paragraphs 8.19-8.22. Do you agree? Why or why not?

IMA'S ANSWERS TO THE DETAILED QUESTIONS RAISED

If you do not agree do you think that the IASB should still be able to require a total or subtotal profit or loss when developing or amending Standards?

We welcome a sub-total for profit and loss being retained. This should give a clear indication to investors of the return management has made on the economic resources entrusted to it in a period.

In this context, there is no clear principle that governs whether income and expenses or gains or losses are reported in profit or loss or in other comprehensive income (OCI). IMA firmly believes that the IASB should establish objectives and principles for performance reporting in that currently profit or loss is defined by those items of income and expense that are reported in profit and loss and recycled from OCI. Moreover, the DP proposes that items are reported in OCI, if the IASB determines that that is the best way of dealing with them. Profit or loss has no independent significance and we consider this is the wrong way round.

Investors want to know what management has generated from its operations and the resources allocated to it. We believe it is vital that the IASB develops a robust definition of profit or loss in the CF. In the absence of a clear definition, changes in net assets that do not represent business activity or result in cash flows can be reported part of performance. Investors want management to be accountable for its performance. This includes, but is by no means limited to, the link between executive remuneration and how the reporting entity creates, delivers, and captures value. There also needs to be a closer alignment between reporting and the business model to enable shareholders to hold management accountable for the execution of its business model and the creation of true shareholder value.

It is sometimes claimed that investors may overlook information contained in OCI because of the focus on profit or loss. This seems to imply that if valuation gains and losses are not treated as part of performance and taken direct to OCI, investors will tend to ignore them. We disagree with this in that investors will assess results overall in determining their exposure and management's performance and not just that in the profit or loss.

20. The IASB's preliminary view that the Conceptual Framework should permit or require at least some items of income and expense previously recognised in OCI to be recognised subsequently in profit or loss, i.e recycled, is discussed in paragraphs 8.23-8.26.

Do you agree? Why or why not? If you agree, do you think that all items of income and expense presented in OCI should be recycled into profit or loss? Why or why not?

If you do not agree, how would you address cash flow hedge accounting?

IMA agrees that the CF should permit or require at least some items of income and expense previously recognised in OCI to be recognised subsequently in profit or loss, i.e. recycled. Where assets and liabilities are stated at current values, it is important that holding gains and losses are reported separately from the effect of transactions and other events. However, this should not imply that all operating transactions should be at historical cost –to do so would not present meaningful information - particularly for a financial institution.

21. In this Discussion Paper, two approaches are explored that describe which items could be included in OCI: a narrow approach (Approach 2A described in paragraphs 8.40-8.78) and a broad approach (Approach 2B described in paragraphs 8.79-8.94).

IMA'S ANSWERS TO THE DETAILED QUESTIONS RAISED

Which of these approaches do you support, and why?

If you support a different approach, please describe that approach and explain why you believe it is preferable to the approaches described in this Discussion Paper.

IMA supports the broad approach in that it addresses concerns that the narrow approach recognises in profit or loss certain remeasurements that decrease the relevance of profit or loss. Approach 2 B adds a further category for transitory remeasurements which would only be recycled if they provide relevant information about the return an entity has made on its resources during the period. We agree with this in that, there has to be a primary statement that includes the recognition of changes that relate to, for example, pension remeasurement.

Section 9 Other issues

Chapters 1 and 3 of the existing Conceptual Framework

22 Paragraphs 9.2-9.22 address the chapters of existing Conceptual Framework that were published in 2010 and how those chapters treat the concepts of stewardship, reliability and prudence. The IASB will make changes to those chapters if work on the rest of the Conceptual Framework highlights areas that need clarifying or amending. However, the IASB does not intend to fundamentally reconsider the content of those chapters.

Do you agree with this approach? Please explain your reasons.

If you believe that the IASB should consider changes to those chapters (including how those chapters treat the concepts of stewardship, reliability and prudence), please explain those changes and the reasons for them, and please explain as precisely as possible how they would affect the rest of the Conceptual Framework.

The DP clarifies that the IASB does not intend to reconsider fundamentally chapters 1 and 3 that were published in 2010 but will make changes if work on the rest of the Conceptual Framework highlights areas that need clarifying or amending. It highlights specific areas of concern of: accountability or stewardship; reliability; and the removal of the concept of prudence. We strongly share these concerns, as noted below.

- *Primary users and the concept of stewardship or accountability.* The 2010 CF in OB2 states that "the objective of general purpose financial reporting is to provide financial information that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to an entity".

  We consider this too broad and firmly believe that the primary audience should be the holders of ordinary shares. These are the ultimate owners of a company, the providers of the risk capital and bearers of the residual risk. Financial statements should provide them with the information they need, not only for the purposes of deciding to buy, sell or hold their shares, but also to fulfill their responsibilities as owners – assessing company management and the strategies adopted for the longer term.

  We recognise that reporting is being expected to meet a growing set of needs, but in also aiming it at lenders and creditors, does not take account of the fact that these other stakeholders are protected by contractual and other rights that are not shared by shareholders. Their information needs are also narrower in that their focus is on ensuring that cash flows will meet their loan and interest payments as they fall due, and that any covenants will not be breached.

In addition, investors tend to base investment decisions and assessment of future prospects on a variety of sources of information; much of which is produced outside the annual reporting framework - via analyst briefings, investor meetings, strategy presentations, stock exchange announcements and certain non-financial information. Moreover, financial statements are published some time after the events to which they relate and in looking backwards and focusing on past performance, they are essentially confirmatory. Investors value them in so far as they demonstrate management's accountability – it is entrusted with the assets of the company and financial statements should show how effectively it put those assets to use and the performance derived from those assets. This is the concept of accountability or stewardship. Whilst the objectives of financial reporting in Chapter 1 encompass this concept, we believe it should be equal in prominence to that of providing information that is decision useful.

- *Prudence.* The concept of prudence, which was removed in 2010, should be specifically written into the CF. Investors want companies to err on the side of caution, i.e. be prudent, at an individual item level in the face of uncertainty, such that:

    - There is later rather than earlier recognition of revenues and assets;
    - There is earlier rather than later recognition of costs (incl. impairments) and liabilities; and
    - Assets and income are not overstated and liabilities and costs are not understated.

  We believe prudence should be a fundamental qualitative characteristic for guiding preparers (and auditors) when recognition involves estimates. We do not consider the prudence is necessarily incompatible with neutrality in that the former should prevail when there is uncertainty. It should also be possible to refer to it without it being used for income smoothing. Moreover, IFRS already requires prudence in that:

    - Revenue is to be recognised over time, but losses are recognised up front if the contract is onerous (i.e. at unfavourable terms).
    - Liabilities must be recorded for guarantees or warranties, even when they have not yet been called in.
    - Inventory is typically carried at lower of cost or net realisable value; again a prime example of exercising caution.
    - Both assets and liabilities measured at fair value are adjusted for risk. This reflects the effect of uncertainty by increasing the measure of a liability or decreasing the measure of an asset.
    - Asset impairment tests are required to ensure that the carrying amount in the statement of financial position is not greater than the [market] value of the asset and the IASB is moving to an expected from an incurred loss model.
    - Strict rules about balance sheet presentation give as complete a picture of an entity's exposure as possible to the investor.
    - Limited netting of derivatives and other financial instruments.
    - Consolidation rules are based on the principle of control rather than a "50%+1" bright line.
    - The IASB is proposing that entities should recognise all leases on the balance sheet.

IMA'S ANSWERS TO THE DETAILED QUESTIONS RAISED

- *Reliability as a qualitative characteristic*. Financial statements will always contain estimates that have a degree of uncertainty. Investors want to trust the information reported and these estimates should be the best in the circumstances in that a certain level of precision is necessary. We do not consider that "freedom from material error" which is in the definition of "faithful representation" necessarily captures this. Unreliable estimates should not be included in financial statements and "reliability" should be a separate qualitative characteristic. See question 11.

- *Substance over form.* Similarly substance over form is not a component of faithful representation. This is a well understood concept and we consider that "economic substance over accounting and legal form" is an essential qualitative characteristic of financial reports and should be re-introduced. See question 7.

Business model

23 The business model concept is discussed in paragraphs 9.23-9.34. This Discussion Paper does not define the business model concept. However, the IASB's preliminary view is that financial statements can be made more relevant if the IASB considers, when developing or revising particular Standards, how an entity conducts its business activities.

Do you think that the IASB should use the business model concept when it develops or revises particular Standards? Why or why not?

If you agree, in which areas do you think that the business model concept would be helpful?

Should the IASB define 'business model'? Why or why not?

If you think that 'business model' should be defined, how would you define it?

We agree with the IASB's preliminary view that financial statements can be made more relevant to investors if the IASB considers, when developing or revising particular IFRS, how an entity conducts its business activities. However, we do not believe that a definition of the 'business model' in the CF is needed because the business model is entity specific. IFRS9 'Financial Instruments: Recognition and Measurement' introduced the concept for financial instruments primarily to address measurement issues between the banking and trading books in the banking industry. A conglomerate can have several business models for its diverse activities. Any definition would of necessity have to be high level which would limit its usefulness.

Unit of account

24. The unit of account is discussed in paragraphs 9.35-9.41. The IASB's preliminary view is that the unit of account will normally be decided when the IASB develops or revises particular Standards and that, in selecting a unit of account, the IASB should consider the qualitative characteristics of useful financial information. Do you agree? Why or why not?

For investors, the unit of account, being the level of aggregation required in reporting individual resources, or other rights and obligations, is important. Clearly the selection of a unit of account should result in information that is useful and that would require consideration of the qualitative characteristics of financial information. Individual IFRS should address the need for disclosure of the unit of account for the purposes of measurement of those items that are the subject of the standard.

IMA'S ANSWERS TO THE DETAILED QUESTIONS RAISED

Going concern *25 Going concern is discussed in paragraphs 9.42-9.44. The IASB has identified three situations in which the going concern assumption is relevant (when measuring assets and liabilities, when identifying liabilities and when disclosing information about the entity). Are there any other situations where the going concern assumption might be relevant?*

The DP refers to the going concern concept in the existing CF but it is unclear what is proposed. We consider that this should continue to be one of the fundamental concepts that underlie financial reporting and it is important it is retained. We have not identified any situations other than those in DP9.43 where the going concern assumption might be relevant.

Capital maintenance *26 Capital maintenance is discussed in paragraphs 9.45-9.54. The IASB plans to include the existing descriptions and the discussion of capital maintenance concepts in the revised Conceptual Framework largely unchanged until such time as a new or revised Standard on accounting for high inflation indicates a need for change. Do you agree? Why or why not? Please explain your reasons.*

We agree with the IASB's plans to include the existing descriptions and the discussion of capital maintenance concepts in the revised *Conceptual Framework* largely unchanged. However, in the event that inflation increases significantly in countries that report under IFRS, there will need to be guidance on accounting that addresses erosion of capital in a period of inflation. That would be the time to revisit, but not necessarily change, the capital maintenance section in the CF. Inflation accounting of itself is best developed at standards level.