



Private & Confidential
FAO of Mark Sherwin
Investment Management Association
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29 October 2013

Dear Mark

Invitation to Comment Statement of Recommended Practice – Financial Statements of UK Authorised Funds

We are pleased to respond to the Investment Management Association's invitation to comment on the exposure draft of the Statement of Recommended Practice – Financial Statements of UK Authorised Funds, July 2013.

Consultation response

Q1 How many funds do you expect to have significant numbers of instruments that are valued using unobservable inputs?

Given the nature of our role, we are not in a position to comment meaningfully on this question beyond observing that in our experience it is relatively uncommon for UK authorised funds to have significant numbers of instruments that are valued using unobservable inputs. We stress that this is based on our experience as auditors and professional advisors and not on survey or statistical results.

Q2 Do you have systems or processes in place to support the IFRS reporting levels?

In our role we do not prepare financial statements, and as such do not have a requirement for such systems or processes. Nevertheless typically our clients for which the corporate entity or non-authorised fund investment vehicles currently report under IFRS do have systems and processes to support the IFRS reporting levels.

Q3 Do you agree that the SORP's emphasis justifies the additional disclosure category for unobservable inputs? If not, please explain why.

We appreciate that there is a disconnect between the fair value hierarchies in existing IFRS and in FRS 102, and as such we welcome a solution which complies with FRS 102 as well as providing meaningful and transparent information to users of the financial statements. We are also supportive of the proposed requirement to distinguish between valuation techniques using observable and unobservable market data as this provides compliance with FRS 102, but also a degree of consistency with the existing IFRS disclosure requirements with which investors are already familiar.

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However, we believe it would be beneficial to provide additional specific guidance on which category in the fair value hierarchy different categories of investment asset and liability would be expected to be disclosed under. We understand that it may be appropriate to disclose certain investments under different categories dependent on the facts and circumstances and where this is the case we believe that it would be beneficial to provide guidance on the factors and variables that should be considered in determining the most appropriate categorisation.

Q4 Do you agree with the generic approach for all authorised funds or should it be more focussed on UCITS with non-UCITS funds being dealt with by exception in appendix III?

We agree with the generic approach for all authorised funds for risk management policy disclosures as it promotes comparability between UCITS and non-UCITS funds. In our opinion, the level of guidance adequately addresses the disclosure requirements for the two types of funds.

Q5 Do you agree with the integrated approach of using a single set of disclosures to satisfy accounting and regulatory requirements?

Specific to the risk management policy disclosures, we agree with the integrated approach of using one set of disclosures to satisfy the regulatory and accounting requirements as it helps the SORP function as a complete set of guidelines and promotes consistency as noted above.

We, however, do not recommend using financial statements to reflect ALL of the regulatory reporting requirements as financial statements serve a different purpose from that of a regulatory reporting. In addition there are some accounting requirements, such as the unrealised gains/realised gains disclosure requirements for non-UCITS funds that we do not think should be made mandatory for UCITS funds. Also refer to our comments relating to risk management disclosures under question 15.

Q6 Do you think the SORP should define realised and unrealised gains/losses for non-UCITS funds?

Yes. There are several different methods for calculating realised and unrealised gains/losses. The different methods would provide for materially different outcomes and therefore it is important to provide a clear definition to the industry as to the expected calculation methodology.

Q7 If so, should it use definition A, B or something else?

We support the view that determination of realised profits and losses should follow the ICAEW Guidance on determination of realised profits and losses in the context of the Companies Act 2006 (Tech 02/10).

It should be noted that the separation of the profit or loss into recognised and unrecognised portions as proposed by Option B relates to the portion that arose in the current period only. Therefore there may be situations where profits or losses were presented in prior periods as unrecognised that would become recognised as the result of a sale in a later period under the application of Tech 02/10 (this would be the difference between the opening value and cost price where the opening value was not readily convertible to cash).

Q8 Do you think the proposal will help investors better understand the performance and costs? If not, please suggest how it might be improved.

We agree that it would be helpful to have all the information about each share class pulled together in one table or area of the accounts and that including the transaction % per share is a lot more

informative than the current disclosures against purchases and sales.

However, we do not agree that including operating charges and a detailed breakdown of transaction costs will help the investor better understand the accounts. While the split of commissions between research and execution might be interesting for the investment industry, we do not believe this will be useful or meaningful for the investor. Decisions on investment will clearly be made using other information than the accounts. In addition there is an OCF figure disclosed in the accounts already which may be at odds with the per unit expense numbers required by the exposure draft of the SORP.

Returns before and after operating charges and the operating charges are not figures taken directly from the accounts, so we believe may cause confusion and would require additional reworking when pulling the accounts together.

Q9 Are there any aspects of the proposals that you think will be particularly troublesome to produce?

As mentioned above, the calculation of operating charges and returns before and after will require additional calculations, while not too onerous, there would need to be clarity around what was included in operating charges and what was not.

We believe that obtaining the split of transaction costs and splitting out the dilution adjustment would be troublesome to produce. Also, the need to go back for 3 years for the initial adoption of the SORP may be problematic. This is historic data and may be little relevance to an investor in the fund as at the day of adoption. For this reason we believe that that the first set of accounts produced under the new SORP should show the current year cost and performance/share numbers without the previous two years needing to be included and that the three year record be built up from this point.

Q10 Do you agree with the simplification of principles for recognising revenue from debt securities?

The current SORP applies an amortised cost methodology for debt instruments that are measured on a fair value basis. The change to a simplified basis (should a fund provider chose to move away from their current effective interest method) prevents the occurrence of a situation that may result in unintended accounting consequences from this mixed approach. Therefore we agree with the simplification in the SORP consultation document. However, given the investment in systems to perform the calculations required under the current SORP we also agree that a fund provider should not be prohibited from using the effective interest method should they chose.

We are concerned that the guidance in paragraph 2.36 with regards to the spreading is vague and may result in an inconsistent application.

Q11 Do you agree with the removal of the aggregation?

Yes. The aggregation does not provide meaningful information for any investor, unless that investor invests in each of the sub-funds of the ICVC. This is rarely the case and even if it were an investor is more interested in the performance of each individual investment.

Q12 What do you think would be the earliest feasible date?

Q13 Which requirements need an earlier effective date?

Q14 Which requirements should be deferred?

We believe that the revised SORP should be implemented in full on one effective date, rather than deferring adoption of some of the elements to later dates. Deferral of elements of the revised SORP generates confusion for the industry and creates periods of constant change over several reporting periods, which is unhelpful for administrators, asset managers and auditors. We believe that the adoption should be aligned to the adoption of FRS 102 in the UK, with early adoption permitted post publication of the revised SORP in 2014.

Q15 Do you think the proposed SORP satisfies the requirements of FRS 102

We believe that the following areas do not satisfy the requirements of FRS 102:

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| Classification of units - | In paragraph 2.81 it is stated that the units should adhere to FRS 102, but additional criteria have been imposed upon the units. The third bullet of the additional criteria is not the same as those set out in FRS 102. We are not satisfied that the additional criteria are necessary. |
| Related parties - | In paragraph 3.75 it is mentioned that the authorised fund manager is generally not expected to be a related party based on it neither controlling the funds nor having significant influence. The definition of related parties in FRS 102 is broader than just control and significant influence; it also includes key management personnel. It is anticipated that the facts and circumstance for each entity will be different and should be considered in their own right but that in at least some cases, the fund manager will be key management personnel. Therefore such a blanket statement does not seem appropriate. It is also noted that presently the fund manager is often identified as a related party and this is not expected to change. |
| Contingent liabilities - | The relief from disclosure of contingent liabilities under paragraph 3.74A is not the same as the relief under 21.17 of FRS 102. The threshold under FRS 102 only applies in extremely rare circumstances and when it is expected to prejudice seriously the entity. No mention of the rarity is provided under 3.74A and 'expected to prejudice seriously' (the wording in FRS 102) is replaced with 'might be prejudicial' and the test for prejudice is on the unit holders rather than the entity. |
| Risk management - | The risks required by FRS 102 and regulation are not defined in the same manner. In particular the SORP has included credit risk as part of market risk where it relates to an issuer's credit quality and any residual risk is disclosed as part of counterparty risk. Counterparty risk is not a term defined under FRS 102. The disclosure requirements of FRS 102 are divided based on the defined risks. This departure from credit risk as defined in FRS 102 may result in the disclosures differing from those that would have been provided if FRS 102 had been applied alone. |



Q16 Do you have any other comments on the proposed SORP?

The following other items were identified:

It is not clear why the interest accrual is separated from the instrument. The fair value of the instrument would include interest. In addition using net realisable value as a measurement model for interest is unusual.

Paragraph 2.20 mentions a mark to market basis; this should be a fair value.

Reference is made in paragraph 2.29 to non-equity shares. These were previously defined under FRS 4 but are not defined under FRS 102. A definition should be included.

In paragraph 3.84 the wording used to describe the equivalent level 2 and 3 separation is not the same as the standard, though the wording is similar.

In paragraph 2.13 the inclusion of the line "arrived at in accordance with the instrument constituting the fund" does not seem relevant to the use of a valuation technique.

Yours sincerely