International Financial Reporting Standards
By email: commentletters@ifrs.org

10 May 2021

Dear Sir, Madam

Re: BVCA response to Post Implementation Review of IFRS 10, 11 & 12

We are writing on behalf of the British Private Equity and Venture Capital Association ("BVCA"), which is the industry body and public policy advocate for the private equity and venture capital industry in the UK. With a membership of over 700 firms, we represent the vast majority of all UK based private equity and venture capital firms, as well as their professional advisers and investors. Between 2015 and 2019, BVCA members invested over £43bn into nearly 3,230 UK businesses, in sectors across the UK economy ranging from heavy infrastructure to emerging technology. Companies backed by private equity and venture capital currently employ 972,000 people in the UK and the majority of the businesses our members invest in are small and medium-sized businesses.

The BVCA was supportive of the amendments to IFRS 10 which created an exception to the consolidation requirements (of the standard) for entities defined as investment entities. We actively engaged in the consultation processes for developing the consolidation exemption for investment entities and our feedback in this letter is limited to this area.

The application of IFRS 10 in practice has been positive, but in some cases, it can lead to information being presented in a manner that does not reflect how investments are monitored or is useful to the users of the financial statements. Further amendments could be made to the standard that are in line with the IFRS 10 approach of looking at the business model of the investment entity rather than its structure.

Consultation Questions

Q1. Given that the offences have now been set in law, is our overall approach consistent with the policy intent? To understand whether groups of stakeholders share similar views, the Board would like to know: (a) your principal role in relation to financial reporting. Are you a user or a preparer of financial statements, an auditor, a regulator, a standard-setter or an academic? Do you represent a professional accounting body? If you are a user of financial statements, what kind of user are you, for example, are you a buy-side analyst, sell-side analyst, credit rating analyst, creditor or lender, or asset or portfolio manager? (b) your principal jurisdiction and industry. For example, if you are a user of financial statements, which regions do you follow or invest in? Please state whether your responses to questions 2–10 are unrelated to your principal jurisdiction or industry.

The BVCA's members are primarily preparers of financial statements. Our membership also includes investors which are the users of this information. The BVCA's members operate in the UK and invest across the world and their investor base is also global.

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Q4 (a). In your experience:

(i) to what extent does applying the definition (paragraph 27 of IFRS 10) and the description of the typical characteristics of an investment entity (paragraph 28 of IFRS 10) lead to consistent outcomes? If you have found that inconsistent outcomes arise, please describe these outcomes and explain the situations in which they arise.

(ii) to what extent does the definition and the description of typical characteristics result in classification outcomes that, in your view, fail to represent the nature of the entity in a relevant or faithful manner? For example, do the definition and the description of typical characteristics include entities in (or exclude entities from) the category of investment entities that in your view should be excluded (or included)? Please provide the reasons for your answer.

In general the definition of what constitutes an investment entity, along with the typical characteristics, permits an appropriate identification of such entities.

We would like to highlight that in certain circumstances, there is an potential conflict in outcomes between IFRS 9 and IFRS 10 which could result in less meaningful information for users of the financial statements. Under IFRS 9, where financial instruments meet both the business model test and the cashflow characteristics test, an entity can hold financial instruments at amortised cost rather than fair value. Where these assets that are held at amortised cost are substantial to the entity, this would preclude the entity from meeting the definition of an investment entity due to IFRS 10:27 (c) which states that an investment entity "measures and evaluates the performance of substantially all of its investments on a fair value basis."

Where entities have a mixture of both debt and equity investment holdings, including private equity funds, they would need to either a) fair value all of the assets on their balance sheet, or b) apply amortised cost accounting to the debt/loan portfolio and not be able to benefit from the consolidation exemption for investments (and therefore consolidate their controlled investments). An entity wanting to avail itself of the consolidation exemption for investment entities would not be able to utilise the amortised cost approach for financial instruments, even if it met the qualifying conditions. This may not reflect how the private equity fund values its debt investments. We do however note that IFRS 9 does allow reporters to select the fair value option in situations where a financial instrument does meet the criteria for amortised cost.

We believe that the IFRS 10 definition of investment entities could be amended to still allow for debt investments to be held at amortised cost where this provides more meaningful information for investors.

Q4 (b). In your experience:

(i) are there situations in which requiring an investment entity to measure at fair value its investment in a subsidiary that is an investment entity itself results in a loss of information? If so, please provide details of the useful information that is missing and explain why you think that information is useful.

(ii) are there criteria, other than those in paragraph 32 of IFRS 10, that may be relevant to the scope of application of the consolidation exception for investment entities?

We agree with the feedback included in the Request for Information on page 21. Where an investment entity is required to account for an investment in another investment entity at fair value, instead of consolidating it, it does lead to a loss of information. We therefore support the feedback submitted by a BVCA member on the challenges this leads to in practice, and the additional reconcilations required in their financial statements to provide users with more meaningful information on portfolio investments.

At present, only subsidiaries that act as an extension of the operations of the investment entity parent which do not themselves qualify as investment entities, can be consolidated. This should be extended to include intermediate holding companies that are also investment entities where it would be better to consolidate the results, assets and liabilities of these entities, rather than showing them in a single line item at fair value. We believe that this would be the most useful approach for investors and would retain the principles-based approach which was the intention of the original standard and would mean that for groups that are identical in all respects other than in their legal structure, the same accounting presentation and results would apply.

We would be very keen to discuss the contents of this letter with you and look forward to hearing from you.

Yours faithfully,

GKManku

Gurpreet Manku
Deputy Director General and Director of Policy, BVCA