International Accounting Standards Board
30 Cannon Street
London
EC4M 6HX

14 January 2014

Dear Sirs

Re: BVCA response to A Review of the Conceptual Framework for Financial Reporting

Background to the BVCA

The British Private Equity and Venture Capital Association ("BVCA") is the industry body for the private equity and venture capital industry in the UK. With a membership of over 500 firms, the BVCA represents the vast majority of all UK based private equity and venture capital firms, as well as their professional advisers. This submission has been prepared by the BVCA's Legal & Technical Committee, which represents the interests of BVCA members in legal, accounting and technical matters relevant to the private equity and venture capital industry.

Our members have invested £33 billion in over 4,500 UK companies over the last five years. Companies backed by UK-based private equity and venture capital firms employ over half a million people and 90% of UK investments in 2012 were directed at small and medium-sized businesses. As major investors in private companies, and some public companies, our members have an interest in financial reporting matters, the conduct and information presented by such companies, and the burdens placed on the management of such companies.

Private equity ownership involves the close alignment of interests between investors and the management of a company, and this leads to closer and often more informal relationships than between comparable forms of ownership. As such, the level of communication between these parties tends to be high, and to a level that covers the areas investors require.

The BVCA welcomes the opportunity to comment on the Conceptual Framework.

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Our comments on the Conceptual Framework

The BVCA supports your efforts to define a revised conceptual framework that outlines the fundamental principles on which future accounting standards and revisions to current standards will be based in most cases. We note that the Conceptual Framework is not a Standard or Interpretation and does not override any specific Standard or Interpretation. We also note that in a limited number of cases, there may be a conflict between the Conceptual Framework and a Standard. Where there is a conflict, the requirements of the Standard prevail over the Conceptual Framework.

The BVCA's main concern when the framework was published was how it may impact the accounting for private equity and venture capital assets at fair value and how they are valued.

The relevant questions are

Question 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) for 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 the 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?

Question 23
Business model 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?

Question 24
Unit of account 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?

The BVCA agrees with the IASB's conclusions on the above matters. You state that:

"The objective of financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. In addition, if financial information is to be useful, it must be relevant and must faithfully represent what it purports to represent. Those two characteristics - relevance and faithful representation - are the fundamental qualitative characteristics of useful financial information.

A perfectly faithful representation is free from error. However, this does not mean that measurements must be perfectly accurate in all respects. An estimate of an unobservable price can be faithfully represented if it is described clearly and accurately as being an estimate, the nature and limitations of the estimating process are explained and no errors have been made in selecting and applying an appropriate process for developing the estimate.

This Discussion Paper suggests that a **current** exit price is the most appropriate measure for assets that will be realised through sale"

These comments are helpful to ensure the proper application of the International Private Equity and Venture Capital Valuation Guidelines. In particular they cut across arguments that an investment cannot be carried at fair value because it cannot be established in a perfectly accurate manner from directly observable data. It also stresses that the value to be used is the current value at the reporting date not some future exit value. The BVCA has commented on many previous responses to proposals that cost benefit needs to be considered very carefully when changing or adding to reporting requirements.

You also state that: "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 it develops or revises particular Standards, how an entity conducts its business activities.

Recently, the IASB required investment entities not to consolidate some of their subsidiaries (see paragraph BC226 of IFRS 10 Consolidated Financial Statements). This is because investment entities have a unique business model that makes reporting subsidiaries at fair value more appropriate than consolidation."

You know from previous correspondence and discussions that the BVCA fully supports the use of the business model concept, even if you do not specifically define it, and its application to the issue of non-consolidation for investment entities.

Finally you state that: "The unit of account used can also affect the measurement of recognised assets and liabilities, for example: a different measure of an equity investment may be obtained if: (i) the value of a single share in that equity investment is measured and multiplied by the number of shares held; or (ii) the value of the total equity investment is measured."

The BVCA supports the International Private Equity and Venture Capital Valuation Guidelines. These recognise that in some cases Price x Quantity is appropriate and in other cases it is not depending on the business situation and the likely future exit outcome to provide useful financial information to investors.

The BVCA would of course be willing to discuss further this submission and, if you so wish, you should contact Gurpreet Manku.

Yours faithfully

Simon Witney
Chairman – BVCA Legal and Technical Committee