INVESTMENT COMPANY INSTITUTE

MEMO# 15262

October 15, 2002

ICI COMMENT LETTER ON IASB PROPOSAL ON FUND SHARES

[15262] October 15, 2002 TO: ACCOUNTING/TREASURERS COMMITTEE No. 47-02 INTERNATIONAL COMMITTEE No. 74-02 RE: ICI COMMENT LETTER ON IASB PROPOSAL ON FUND SHARES The Institute recently filed a comment letter with the International Accounting Standards Board in response to its request for comments on proposed changes to IAS 32 Financial Instruments: Disclosure and Presentation and IAS 39 Financial Instruments: Recognition and Measurement. The proposed changes would require funds preparing financial statements under international accounting standards to treat the value of their outstanding shares as a liability for financial accounting purposes. The proposed changes to IAS 32 and IAS 39 are similar to changes first proposed in IASB Interpretation SIC – D34 Financial Instruments – Instruments or Rights Redeemable by the Holder.1 A copy of the Institute's comment letter is attached and it is summarized below. The Institute's comment letter argues that fund shares should be classified as equity for financial accounting purposes since they represent a residual interest in the fund's net assets after deducting all of its liabilities. The letter notes that fund shares entitle shareholders to participate in the fund's profits and losses, and to receive distributions of investment income and capital gains. Further, fund shares entail voting rights (e.g., elect directors, approve changes in advisory contracts and fundamental investment policies) typically associated with an equity investment. The letter indicates that the exposure draft's conclusion that fund shares are liabilities is inconsistent with a recent FASB exposure draft2 that would treat fund shares as equity. The letter notes that the IASB proposal would frustrate convergence of accounting standards. Finally, the Institute's letter expresses concern that the characterization of fund shares as liabilities may cause shareholders to believe that their investment in a fund is analogous to a deposit or that it is a debt instrument with a fixed redemption date. Gregory M. Smith Director – Operations/ Compliance & Fund Accounting Attachment (in .pdf format) 1 The Institute filed a comment letter with the IASB opposing SIC – D34. See Accounting/Treasurers Committee No. 32-01 (November 5, 2001). In response to comments by the Institute and others, the IASB agreed to defer SIC – 34 and consider it as part of a broader project to revise IAS 32 and IAS 39. 2 See FASB Exposure Draft Accounting for Financial Instruments with Characteristics of Liabilities, Equity, or Both (October 27, 2000).