CFA Institute

67 Lombard Street
7th Floor
London EC3V 9LJ
United Kingdom

+44 (0) 20 7330 9500 tel
+44 (0) 20 7330 9501 fax
info@cfainstitute.org
www.cfainstitute.org

July 29, 2019

Ms. Fredre Ferreira and Ms. Isabel Batista
European Financial Reporting Advisory Group
Square de Meeus 35
1000 Bruxelles
BELGIUM.

Via email: fredre.ferreira@efrag.org and isabel.batista@efrag.org

Re: Equity Instrument Request for Feedback

Dear Ms. Ferreira and Ms. Batista:

CFA Institute appreciates the opportunity to comment on the *Equity Instruments – Research on Measurement* questionnaire (web-based survey and pdf) and discussion or background paper[1] (collectively, the Request for Feedback) published in May 2019 in the wider context of the *Sustainable Finance* initiative undertaken by the European Commission. We are submitting a letter rather than complete the survey as we believe our views are best articulated in the aggregate through a letter rather than in response to specific questions in the web-based survey.

CFA Institute[2] is providing comments consistent with our objective of promoting fair and transparent global capital markets and advocating for investor protections. An integral part of our efforts toward meeting those goals is ensuring that corporate financial reporting and disclosures – and the related audits – provided to investors and other end users are of high quality. Our advocacy position is informed by our global membership who invest both locally and globally and in consultation with Corporate Disclosure Policy Council ("CDPC")[3]

---

1 http://www.efrag.org/Assets/Download?assetUrl=/sites/webpublishing/SiteAssets/EFRAG%2520Secretariat%2520background%2520paper%2520for%2520public%2520consultation%2520%2520Equity%2520Instruments%2520Research%2520on%2520Measurement.pdf

2 CFA Institute is a global, not-for-profit professional association of nearly 171,400 investment analysts, advisers, portfolio managers, and other investment professionals in 165 countries, of whom more than 164,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 154 member societies in 77 countries and territories.

3 The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The CDPC is comprised of investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the CDPC provides the practitioners' perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.

Fair Value: Our Long-Held Position on the Most Relevant Measurement Basis

CFA Institute has long advocated for fair value accounting as the most relevant and useful accounting basis for investors. In our comment letters in 2010 and 2013 to the FASB and IASB we articulated our support for recognition and measurement principles based on fair value as this reflects the most current and complete estimation of the value of assets and liabilities, including the amount, timing, riskiness of future cash attributable to such assets and liabilities. Fair values are the premise of all asset and liability exchanges, and as such, should be represented in the financial statements. Any other estimates are not necessarily more difficult, subjective, or complex than fair values. As such, to gain our support financial instruments accounting must advance wider use of fair value for the recognition and measurement of such instruments.

Investors invest globally so the FASB and the IASB's decision to go separate ways in the accounting for financial instruments is not helpful for investors. As it relates to the accounting for equity investments, CFA Institute has supported the FASB's approach that all equities should be measured at fair value through profit or loss (net income).

Other Comprehensive Income: Our Historical Position

CFA Institute has written extensively on the topic of other comprehensive income[4]. We oppose the use of other comprehensive income and accumulated other comprehensive income because they have no conceptual underpinning – other than to reduce income statement volatility. We do not believe this is either a necessary or sufficient basis to eliminate reflecting the change in value of a financial instrument – or other measurements – through profit or loss (net income). We know from our extensive outreach that investors pay less attention to items reflected in other comprehensive income and accumulated other comprehensive income than they do to items reflect through profit or loss (net income) and retained earnings.

In a recent blog, *Berkshire's Bottom Line: More Relevant Than Ever Before*, we responded to Warren Buffett and Donald Graham's criticisms regarding the FASB's accounting change to include all fair value changes related to equity investments through net income (profit and loss) – because they are "long-term" investments. CFA Institute argued that investors now have a more prominent and transparent display of the economics of the risks associated with the underlying investments – and such values were already reflected in other comprehensive income and comprehensive income. Buffett and Graham's criticisms highlight our long-standing position that investors pay less attention to comprehensive income than net income – because Berkshire Hathaway's true bottom line – comprehensive income – remained unchanged. In the blog, we highlighted that the IFRS treatment for these very same instruments would mean the profit and

---

4 What is the Relevance of "Other Comprehensive Income"? IASB's Cooper Explains - 21 April 2015
OCI Study: Understanding Bank Performance, Risk Through "Forgotten" Income Statement - 24 March 2015
Comment Letter on Conceptual Framework Discussion Paper: Other Comprehensive Income (OCI) 17 February 2014
Comment Letter on FASB Proposal to Change Presentation of Reclassification Adjustment - 31 October 2012
Coming Soon to an Income Statement Near You: Comprehensive Income - 13 April 2012
Comment Letter on Presentation of Items of Other Comprehensive Income - 30 September 2010

loss on the securities would never be recognized in net income. An alternative we believe Buffett and Graham would also find unacceptable.

We strongly believe that all equity investments should be measured at fair value through the profit or loss account because fundamental investors are interested in discovering the value of the business and historical cost measurements or measurements that imply such investments do not fluctuate in price due to economic conditions is actually uneconomic.

"Long-Term" Investments: What is Long-Term?

As correctly mentioned in Paragraph 4.3 of the background paper there is no definition of 'long-term investment' or 'long-term investor' in IFRS standards. We have long articulated our position that the term 'long-term investing' is generally used to support management intent-based historical cost accounting so that investors are not provided with an observable fair value. Management's intent, however, has no bearing on the underlying value of an asset. And as we note above, investors are most concerned with discovering the value of the asset and the business. Given the subjectivity and wide interpretation of the term "long-term," we have long articulated that we cannot support this as a reason to not reflect a financial instrument at its fair value.

Pulling it All Together: Our Position on Existing Accounting vs. Proposed Alternatives

Our View on the Current Equity Accounting – Notwithstanding our preferred policy choice, certain IASB's constituents have vigorously advocated in favour of other comprehensive income and accumulated other comprehensive income for strategic and long-term investments. We believe the current IASB's approach permitting a policy choice (other comprehensive income with a restriction of non-recycling to profit or loss account) is a middle ground to address diverse needs of its constituents but also to deter misuse of the category and to eliminate the timing of the recognition of profit and loss from such investments based upon management intent.

Consideration of the Alternative Measurement Methods – We reviewed and considered the various alternative measurement methods in the background paper. Our view is that further classification and measurement alternatives result in accounting complexity that does not reflect the underlying economics of the transactions. Further, the approaches are only likely to confuse investors – particularly as they make global investment choices. We believe any alternative approaches to measure equity instruments as covered in your background paper will not timely and fully reflect the economic reality and would obstruct useful information to investors. For that reason, we believe that the EFRAG and the IASB should not support any modifications to IFRS 9 and IFRS 13.

Preferred Solution – The right answer is fair value through profit and loss for all investments – with separate presentation of the cash dividends from the investment and the changes in fair value measurements. Investors want cash and fair value at each reporting date. Our view is that if companies believe investors should disregard the fair value in favour of some other measurement approach that they can provide disclosures that articulate the uncertainties associated with the fair value measurement and what they perceive to be a more useful long-term measurement. Investors can then decide what measurement they perceive is more decision-useful and adjust for it as they deem necessary.

Should EFRAG Advance This Proposal: At a Minimum Provide IFRS 13 Fair Value

We believe any changes to IFRS 9 and IFRS 13 will be unhelpful to investors. Therefore, we strongly oppose any reporting changes made under the false pretext of supporting long-term investments. Investors invest globally and, therefore, any further divergence would be confusing and increase complexities for both preparers and users of the financial statements. Nevertheless, should EFRAG press this issue forward with the IASB, we believe – at a minimum – an IFRS 13 compliant disclosure to ensure global comparability should be provided to investors.

****

If you or your staff have questions or seek further elaboration of our views, please contact Sandra J. Peters at sandra.peters@cfainstitute.org or Kazim Razvi at kazim.razvi@cfainstitute.org.

Sincerely,

/s/ Sandra J. Peters

Sandra J. Peters, CPA, CFA
Head, Global Financial Reporting Policy
CFA Institute

cc: Hans Hoogervorst, Chairman, International Accounting Standards Board