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Switching to International Accounting Standards Wouldn’t Likely Benefit U.S. Fund Investors, ICI Tells SEC

By Gregory Smith

A key issue for ICI’s Operations team is regulator interest in harmonizing worldwide accounting standards. As Donald Boteler, ICI’s Vice President for Operations and Continuing Education, said in ICI’s latest annual report, “It’s a noble purpose, but it’s a big, big challenge.”

In a recent letter to the Securities and Exchange Commission, we reviewed the benefits and costs to funds and their investors associated with a possible transition to International Financial Reporting Standards (IFRS). In particular, we discussed how applying IFRS to mutual funds’ financial statements would not provide the key benefits to fund investors that normally would be associated with a transition to a global set of accounting standards—such as the ability to more readily compare financial statements of issuers organized in different jurisdictions. Here are a few important reasons why:

- **Cross-border offering of fund shares is limited** U.S. securities laws strongly limit the extent to which foreign fund shares are offered into the U.S. Moreover, U.S. tax laws frequently disadvantage the sale of U.S. fund shares overseas. Thus, neither U.S. nor foreign fund investors have much to gain from making the financial statements of U.S. and foreign funds more comparable.
- **U.S. accounting standards work better for fund investors**. U.S. Generally Accepted Accounting Principles (GAAP) effectively illustrate the fund’s financial position and results of operations by requiring disclosure of the fund’s portfolio holdings, investment income, and the change in value of its holdings, as well as such key measures as total return, the income ratio, the expense ratio, and portfolio turnover. In contrast, IFRS does not provide accounting standards or guidance specific to the investment company industry. Under IFRS, investment companies would apply the same financial reporting standards followed by general corporate enterprises, which means their financial statements would be far less meaningful to shareholders than those prepared under U.S. GAAP.
- **There are significant costs associated with requiring investment companies to adopt IFRS**. These costs include: 1) decreased utility of financial statements delivered to fund shareholders; 2) initial conversion costs relating to accounting and financial reporting systems; 3) human capital and training costs; 4) ongoing systems and recordkeeping costs associated with increased volume of book/tax differences between public financial statements and statements prepared for tax purposes; and 5) increased print and mail costs attributable to increased length of shareholder reports. Costs associated with accounting for fund investments and preparing financial statements included in shareholder reports delivered to investors are typically borne by the fund. Accordingly, fund investors would bear these costs through increased fund expenses and decreased total returns.

The SEC is scheduled to make a decision on whether, when, and how to incorporate IFRS into the U.S. financial reporting system by the end of this year. Any transition to IFRS likely would not occur prior to 2016. ICI will continue to provide regulators with our input as this process unfolds.

- Read more about ICI’s work in Operations and Technology.
- Read more ICI comment letters.

Gregory Smith was senior director of operations, compliance, and fund accounting for ICI.