

Draft Comment Letter

Comments should be submitted by 9 October 2015 to commentletters@efrag.org

International Accounting Standards Board

30 Cannon Street
London EC4M 6XH
United Kingdom

40. Sitzung IFRS-FA am 30.07.2015
40_02c_IFRS-FA_IAS 19_DCL_EFRAG

[Date]

Dear Sir/Madam,

Re: Exposure Draft ED/2015/05 Remeasurement on a Plan Amendment, Curtailment or Settlement / Availability of a Refund from a Defined Benefit Plan (Proposed amendments to IAS 19 and IFRIC 14)

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the amendments proposed in the Exposure Draft ED/2015/05 *Remeasurement on a Plan Amendment, Curtailment or Settlement / Availability of a Refund from a Defined Benefit Plan (Proposed amendments to IAS 19 and IFRIC 14)*, issued by the IASB on 18 June 2015 (the ED).

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS in the European Union and European Economic Area.

EFRAG welcomes the proposed amendments and agrees that they address issues needing clarification. EFRAG supports the proposed amendments in respect of other parties' (including plan trustees) power to use the plan surplus for other purposes that affect the benefits for plan members and the proposed clarifications of accounting for a plan amendment, curtailment or settlement. EFRAG also supports the proposed limited retrospective application of the amendments based on the cost-benefit trade-off.

Our detailed comments and responses to the questions in the ED are set out in the Appendix.

If you would like to discuss our comments further, please do not hesitate to contact Robert Stojek or me.

Yours faithfully,

Roger Marshall
Acting President of the EFRAG Board

APPENDIX

Question 1 - Accounting when other parties can wind up a plan or affect benefits for plan members without an entity's consent

The IASB proposes amending IFRIC 14 to require that, when an entity determines the availability of a refund from a defined benefit plan:

- (a) the amount of the surplus that an entity recognises as an asset on the basis of a future refund should not include amounts that other parties (for example, the plan trustees) can use for other purposes (for example, to enhance benefits for plan members) without the entity's consent.
- (b) an entity should not assume a gradual settlement of the plan as the justification for the recognition of an asset, if other parties can wind up the plan without the entity's consent.
- (c) other parties' power to buy annuities as plan assets or make other investment decisions without changing the benefits for plan members does not affect the availability of a refund.

Do you agree with the proposed amendments? Why or why not?

Notes to constituents

- 1 *In accordance with paragraph 64 of IAS 19 Employee Benefits, the measurement of a net defined benefit asset is limited to the lower of the surplus in the defined benefit plan and the asset ceiling. The latter is defined in paragraph 8 of IAS 19 as the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.*
- 2 *IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction in paragraph 11 clarifies that a refund is available to an entity only if the entity has an unconditional right to a refund.*
- 3 *Paragraph BC10 of IFRIC 14 notes that the existence of an asset at the end of the reporting period depends on whether the entity has the right to obtain a refund or reduction in future contributions. Accordingly, if the surplus may be affected in future by the entity through a decision to improve the benefits available to the plan members, or due to future losses in the value of plan assets, the effects of eventual future events that may change the amount of the surplus, are recognised only when they occur.*
- 4 *Paragraph 12 of IFRIC 14 further explains that if a right to refund of a surplus depends on the occurrence or non-occurrence of one or more uncertain future events not wholly within its control, the entity does not have an unconditional right and shall not recognise an asset.*
- 5 *However, the guidance is not clear on what precedence should be applied to the circumstances discussed in paragraphs BC10 and BC12 of IFRIC 14 in situations when a trustee which acts on behalf of the plan's members, is independent of the employer and has discretion to make alternative use of the plan surplus by augmenting the benefits payable to members or by winding up the plan through the purchase of annuities, and has not exercised its rights yet.*
- 6 *The ED confirms that paragraph BC10 of IFRIC 14 was not intended to address the circumstances covered by these amendments. Therefore, the ED addresses the issue and prohibits the recognition of an asset when other parties can use the surplus for other purposes without the entity's consent.*

- 7 *Furthermore, the ED clarifies that an entity does not have an unconditional right to a refund of a surplus on the basis of assuming a gradual settlement when an independent trustee can decide at any time to make a full settlement (plan wind-up) and thus prevent the gradual settlement. This clarifies paragraph 11 of IFRIC 14 which allows the entity to assume that a refund is available when an entity has an unconditional right to a gradual settlement over time until all members have left the plan.*
- 8 *Finally, the ED clarifies that another party's power to buy annuities as plan assets (or make other investment decisions) is different from a trustee's power to use a surplus to enhance benefits or to wind up the plan and should not prevent the entity from recognising a plan surplus as an asset.*

EFRAG's response

EFRAG supports the proposal to clarify that:

- (a) other parties (for example, the plan trustees) that can use the plan surplus for other purposes that affect the benefits for plan members without the entity's consent prevent the availability of a refund of the surplus from being recognised as a plan asset;**
- (b) an entity should not assume a gradual settlement of the plan as the justification for the recognition of an asset, if other parties have the power to wind up the plan without the entity's consent; and**
- (c) other parties' power to buy annuities as plan assets without changing the benefits for plan members does not affect the availability of a refund.**

- 9 EFRAG notes that the impact of the unconditional power of a trustee or similar party to use the surplus in a defined benefit plan is not specifically addressed in IAS 19 *Employee Benefits* and IFRIC 14 *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. EFRAG, therefore, welcomes the amendment and supports the three proposed clarifications for the following reasons.
- 10 Firstly, EFRAG agrees that a surplus should not be recognised as a plan asset if a trustee or other party has the unconditional power to reduce the surplus by using it for other purposes.
- 11 EFRAG acknowledges that this may appear to trigger accounting asymmetry compared to recognition of a plan deficit as a liability and, therefore, some believe that this amendment may result in the reported net defined benefit asset not properly depicting the economics of the plan.
- 12 However, EFRAG thinks that the power to use the plan surplus for other purposes restricts an entity's ability to use the surplus to generate future cash inflows to the entity. Consequently, the amount of the surplus that the entity recognises as an asset on the basis of a future refund, does not include amounts that other parties can use for other purposes that change the benefits for plan members without the entity's consent. The power to use a plan surplus does not impact on the recognition of a liability and, in EFRAG's view, both a plan deficit and a plan surplus recognised in accordance with IAS 19 and IFRIC 14 (as revised by the ED) properly reflect the economics of the plan.
- 13 Secondly, EFRAG notes that paragraph 11(b) of IFRIC 14 refers to situations where the entity's ability to manage a gradual settlement of the plan is unconditional. EFRAG also agrees with paragraph BC13 of the ED that the costs associated with an immediate wind-up may be significant due to the market cost of annuities being significantly higher than that implied by the IAS 19 basis and other legal and

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professional fees. Consequently, a plan with an apparent surplus may not mean that the entity has the ability to recover any of that surplus on winding-up the plan.

- 14 EFRAG, therefore, agrees that power of a trustee or other party to wind-up the plan or make a full settlement, at any time, prevents the gradual settlement over time until all members have left the plan. This power restricts an entity's ability to realise economic benefits through a gradual settlement.
- 15 Finally, EFRAG agrees that a trustee's power to buy annuities as plan assets or make other investment decisions is different from a trustee's power to use a surplus to enhance benefits or to wind up the plan. The former power affects the funding of the plan, while the latter power allows a change in the benefits for plan members.
- 16 EFRAG notes that plan trustees may take the actions to de-risk the plan and, therefore, any surplus may end up being utilised through plan trustees' decisions to purchase the annuities on the market. The power to buy annuities as plan assets relates to the future value of plan assets and does not relate to the entity's right to a refund of a surplus. Consequently, EFRAG agrees with the IASB's conclusion that the power to buy annuities, on its own, would not prevent the entity from recognising a surplus as an asset, and therefore EFRAG supports the clarification.
- 17 In conclusion, EFRAG believes that the proposed amendments will result in less divergence in practice, provision of relevant information and therefore supports the proposed amendments.

Question 2 - Statutory requirements that an entity should consider to determine the economic benefit available

The IASB proposes amending IFRIC 14 to confirm that when an entity determines the availability of a refund and a reduction in future contributions, the entity should take into account the statutory requirements that are substantively enacted, as well as the terms and conditions that are contractually agreed and any constructive obligations.

Do you agree with that proposal? Why or why not?

Notes to constituents

- 18 *Paragraph 7 of IFRIC 14 requires an entity to determine the availability of a refund or a reduction in future contributions in accordance with the terms and conditions of the plan and any statutory requirements in the jurisdiction of the plan.*
- 19 *The ED confirms that this requirement applies to conditions of the plan that are contractually agreed, as well as constructive obligations referred to in paragraph 61 of IAS 19 and statutory requirements that are substantively enacted. The ED proposes to apply the same requirement when the plan is remeasured due to an amendment, curtailment or settlement.*

EFRAG's response

EFRAG supports the proposal to clarify that at the end of the reporting period, and when a plan amendment, curtailment or settlement occurs, an entity should determine changes in the impact of the asset ceiling in accordance with the contractually agreed conditions of the plan, constructive obligations and substantively enacted statutory requirements.

- 20 EFRAG notes that an entity's informal practices may result in recognition of a constructive obligation to enhance the benefits provided to plan members, for example when a change in the entity's informal practices would cause unacceptable damage to the entity's relationship with employees. This concept is introduced in

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the requirements related to the measurement of the defined benefit obligation in paragraphs 61 and 88 of IAS 19.

- 21 EFRAG also notes that paragraph 87 of IAS 19 and paragraph 21 of IFRIC 14 use a concept of substantively enacted regulations. Moreover, IAS 12 *Income Taxes* uses a similar concept. EFRAG agrees that an entity should not take account of future changes in regulations or tax if they are not substantively enacted.
- 22 Therefore, EFRAG believes that an amendment to IAS 19 is not necessary in respect of this matter. However, EFRAG also agrees that amending paragraph 7 of IFRIC 14 in this respect will do no harm and may clarify any confusion when assessing the availability of a refund.
- 23 Consequently, EFRAG supports the clarification that an entity, when assessing the availability of a refund, should consider not only the contractually agreed conditions of the plan but also constructive obligations and substantively enacted requirements and believes that it will result in less divergence in practice and provision of more relevant information.

Question 3 - Interaction between the asset ceiling and past service cost or a gain or loss on settlement

The IASB proposes amending IAS 19 to clarify that:

- (a) the past service cost or the gain or loss on settlement is measured and recognised in profit or loss in accordance with the existing requirements in IAS 19; and
- (b) changes in the effect of the asset ceiling are recognised in other comprehensive income as required by paragraph 57(d)(iii) of IAS 19, as a result of the reassessment of the asset ceiling based on the updated surplus, which is itself determined after the recognition of the past service cost or the gain or loss on settlement.

Do you agree with that proposal? Why or why not?

Notes to constituents

- 24 *As explained under Question 1, the IASB decided to restrict the recognition of assets in some specific circumstances. Therefore, the ED addresses the relation of those restrictions with general requirements of IAS 19 and confirms that:*
 - (a) *the asset ceiling may not affect recognition or measurement of a past service cost or a gain or loss on settlement when a plan amendment, curtailment or settlement occurs; and*
 - (b) *after the recognition of the past service cost or a gain or loss on settlement, an entity shall determine the effect of the asset ceiling based on the updated surplus, using the fair value of the plan assets and the discount rate used to remeasure the net defined benefit liability (or asset). Any changes are recognised in other comprehensive income in accordance with paragraph 57(d)(iii).*

EFRAG's response

EFRAG agrees with the proposed clarification that the asset ceiling may not affect the measurement and recognition of past service cost or a gain or loss on settlement at the time of the event. After a plan amendment, curtailment or settlement, the asset ceiling shall be determined using the updated surplus and updated actuarial assumptions including the discount rate.

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- 25 EFRAG notes that when a plan amendment, curtailment or settlement occurs, entities are required to remeasure the surplus or deficit of the defined benefit plan using the updated fair value of plan assets and actuarial assumptions and recognise eventual past service cost or a gain or loss on settlement.
- 26 However, the existing requirements of IAS 19 and IFRIC 14 do not clearly state that an entity's assessment of the availability of a refund should not affect the remeasurement of the surplus or deficit.
- 27 Therefore, EFRAG supports the amendment to clarify that the process of remeasurement of a defined benefit plan comprises of two distinct steps:
- (a) the past service cost or the gain or loss on settlement is measured and recognised in profit or loss in accordance with the existing requirements in IAS 19; and
 - (b) after the recognition of the past service cost or a gain or loss on settlement, the entity determines the effect of the asset ceiling based on the updated surplus, using the fair value of the plan assets and the discount rate used to remeasure the net defined benefit liability (or asset). Any changes in the asset ceiling are recognised in other comprehensive income as required by paragraph 57(d)(iii) of IAS 19.
- 28 EFRAG believes that this clarification is likely to result in less divergence in practice and therefore provision of more relevant information.

Question 4 - Accounting when a plan amendment, curtailment or settlement occurs

The IASB proposes amending IAS 19 to clarify that:

- (a) when the net defined benefit liability (asset) is remeasured in accordance with paragraph 99 of IAS 19:
 - (i) the current service cost and the net interest after the remeasurement are determined using the assumptions applied to the remeasurement; and
 - (ii) an entity determines the net interest after the remeasurement based on the remeasured net defined benefit liability (asset).
- (b) the current service cost and the net interest in the current reporting period before a plan amendment, curtailment or settlement are not affected by, or included in, the past service cost or the gain or loss on settlement.

Do you agree with that proposal? Why or why not?

Notes to constituents

- 29 *Paragraph 99 of IAS 19 requires entities to remeasure the net defined benefit liability (asset) on plan amendment, curtailment or settlement using the current fair value of plan assets and current actuarial assumptions. Paragraph BC64 of IAS 19 confirms that this remeasurement is required in order to determine past service cost and the gain or loss on settlement.*
- 30 *However, paragraph 123 of IAS 19 requires entities to recognise net interest on the net defined benefit liability (or asset) determined on the basis of measurement and assumptions assessed at the start of the annual reporting period. Similarly, paragraph BC64 explains that there is no reason to distinguish between the periods before and after a plan amendment, curtailment or settlement in determining current*

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service cost and net interest, i.e. determining how much service the employee has rendered to date and the effect of the time value of money to date.

- 31 *The ED proposes to amend IAS 19 to clarify that when the net defined benefit liability (asset) is remeasured on a plan amendment, curtailment or settlement:*
- (a) the current service cost and the net interest in the current reporting period before a plan amendment, curtailment or settlement are not affected by, or included in, the past service cost or a gain or loss on settlement; and*
 - (b) the current service cost and the net interest for the period after the remeasurement are determined using the assumptions used for the remeasurement.*

EFRAG's response

EFRAG agrees that the current service cost and the net interest after a plan amendment, curtailment or settlement should be based on the remeasured net defined benefit liability (asset) and reassessed actuarial assumptions. EFRAG also agrees that the current service cost and the net interest in the current reporting period before a plan amendment, curtailment or settlement are not affected by, or included in, the past service cost or the gain or loss on settlement.

- 32 EFRAG notes that paragraphs 123 and BC64 of IAS 19 imply that an entity should not revise any assumptions for the calculation of the current service cost and net interest during the period, even if an entity remeasures the net defined benefit liability (or asset).
- 33 EFRAG believes that ignoring the effects of the remeasurement will not result in provision of useful information and therefore agrees that there is a need for amendment.
- 34 However, EFRAG notes that implementation of this amendment may result in the following issues:
- (a) The costs of implementation may outweigh the benefits from the provision of more useful information if the amendments require an additional quarter-by-quarter analysis of the assumptions and remeasurement of net defined benefit liability (asset); and
 - (b) granting entities a choice of which plan assumptions would be updated may result in provision of financial information that is not comparable.
- 35 EFRAG therefore considered the required frequency of remeasurement and concluded that the frequency of remeasurement is determined in accordance with the existing guidance (i.e. paragraphs 58 and 99 of IAS 19 and paragraph B9 of IAS 34 *Interim Financial Reporting*) and, therefore, the amendments do not change the requirements in IAS 19 on whether and when an entity should remeasure the net defined benefit liability (asset) and therefore is not expected to change how frequently an entity will remeasure the net defined benefit liability (or asset) during a period.
- 36 EFRAG also agrees that the amendment would result in greater consistency between IAS 19 and paragraph B9 of IAS 34 which explains that an entity adjusts the pension cost for an interim period for significant market fluctuations and for significant one-off events, such as plan amendments, curtailments and settlements.
- 37 Moreover, EFRAG notes that the requirement to remeasure the net defined benefit liability (or asset) is determined on a plan-by-plan basis and this requirement is not changed by the proposed amendments.

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- 38 Finally EFRAG concluded that the amendment is not likely to result in considerable additional costs, because of the existing requirements to remeasure the net defined benefit liability (asset) as of the date of a plan amendment, settlement or curtailment for the purpose of determining the past service cost.
- 39 EFRAG therefore agrees with the proposed amendment and believes that it will likely result in provision of more relevant information and enhanced comparability and understandability of the financial information provided.

Question 5 - Transition requirements

The IASB proposes that these amendments should be applied retrospectively, but proposes providing an exemption that would be similar to that granted in respect of the amendments to IAS 19 in 2011. The exemption is for adjustments of the carrying amount of assets outside the scope of IAS 19 (for example, employee benefit expenses that are included in inventories) (see paragraph 173(a) of IAS 19).

Do you agree with that proposal? Why or why not?

Notes to constituents

- 40 *The ED proposes to apply the amendments retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. However, entities need not adjust the carrying amounts of assets (such as inventories) outside the scope of IAS 19 for changes in employee benefit costs that were included in the carrying amount of those assets before the beginning of the earliest comparative period presented in the financial statements in which these amendments are first applied.*
- 41 *Additionally, the IASB notes that the ED does not propose to require new estimates to be made.*

EFRAG's response

EFRAG supports the limited retrospective application of the proposals.

- 42 EFRAG generally supports full retrospective application of amendments and believes that this enhances comparability of financial information provided.
- 43 However, based on cost and benefit considerations, EFRAG agrees with the proposal to provide an exemption for adjustments of the carrying amount of assets outside the scope of IAS 19 for the periods before the earliest comparative period presented in the financial statements in which these amendments were first applied.
- 44 Consequently, EFRAG supports the proposed limited retrospective application of the amendments.

EFRAG's question to constituents

Do you identify any impediments in regard to the limited retrospective application of the proposals? Please explain your position.