EFRAG
European Financial Reporting Advisory Group

DRAFT COMMENT LETTER

Comments should be sent to commentletters@efrag.org by 25 August 2010

IASB
30 Cannon Street
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XX XXXXX 2010

Dear Sir/Madam

Exposure Draft Amendments to IAS19 *Employee Benefits*

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Exposure Draft *Amendments to IAS19 Employee Benefits*. This letter is submitted in EFRAG's capacity of contributing to IASB's and IFRIC's due process and does not necessarily indicate the conclusions that would be reached in its capacity of advising the European Commission on endorsement of the definitive IFRS on the issue.

EFRAG welcomes the publication of the Exposure Draft and believes that IAS 19 could benefit from short-term improvements given the various inconsistencies and implementation difficulties encountered to date in applying it.

We note some of the key requirements set out in the Exposure Draft:

(a) Immediate recognition of changes in the estimation of the defined benefit obligation and in the fair value of the plan assets. Elimination of the corridor approach.

(b) Recognition of unvested plan costs in the year when an amendment to the plan is made.

(c) Disaggregation of the plan costs into three components: service costs, finance costs and remeasurement. Service and finance costs should be recognised in profit and loss. Remeasurements should be recognised in OCI. Changes in the estimate of service costs and in demographic assumptions should be included in the remeasurement component.

(d) The exposure draft proposes that the finance cost component comprises net interest income or expense, determined by applying the high quality corporate bond rate to the net defined asset or liability. As a consequence, it eliminates the requirement in IAS 19 to present an expected rate of return in profit or loss.

(e) The exposure draft proposes to delete the discussion of curtailments and settlements from IAS 19. However, the disclosure requirements would be retained and modified. Entities should disclose a narrative description of any plan amendments and non-routine settlements, and the effect of such plan amendments and non-routine settlements on the statement of comprehensive income.

(f) Expected salary increases, risk-sharing, conditional indexation, current estimates of the expected mortality and taxes payable by the plan should be considered in the estimation of the defined benefit liability. The return on plan assets shall be reduced by administration costs only if those costs relate to managing plan assets. IAS 19 is also amended to include the considerations in IFRIC 14 about "minimum funding requirement".

(g) Disclosure objectives and new proposed disclosures.

While we broadly welcome the proposals in the Exposure Draft as short term improvements, EFRAG wishes to emphasise that , in its view, a comprehensive review of employee benefit accounting is needed to bring significant improvement to the financial reporting of employee benefits. In particular, such a review is necessary to define appropriate accounting for 'modern' schemes that combine features of defined benefit plans and defined contribution plans. Also such a review needs to rely on a clear and appropriate distinction between profit or loss and other comprehensive income. We acknowledge that the IASB has still to determine and consult publicly on its post mid-2011 technical agenda, but EFRAG believes it is important that such a comprehensive review should be proposed by the Board as a matter of priority.

Our comments should therefore be read in the context of EFRAG's support for the project as a short-term solution for pension accounting pending the debate on fundamental issues related to both pensions and performance reporting. In addition, the views expressed here should be read exclusively in the context of this project and do not necessarily apply to other standards or projects such as the *Financial Statements Presentation* project.

EFRAG agrees with the removal of the corridor approach and the immediate recognition of unvested plan costs in the year when an amendment is made, as it will bring increased transparency in the valuation of the net defined benefit liability and remove some inconsistency with the overarching IAS 19 measurement principle.

EFRAG also agrees with the disaggregation of the plan costs into three components (service costs, finance costs and remeasurement) , the proposed presentation of these three components and the removal of various options. More particularly EFRAG supports the removal of the requirement in IAS 19 to reflect in profit or loss a return on assets based on an expected rate of return. We believe that the presentation of net finance cost (income) arising from the net liability (asset) has the potential to enhance in relevance and objectivity by making a clear distinction between the costs of benefits, how those benefits are financed and changes in the value of the net liability (asset). Furthermore, EFRAG agrees with the disclosure objectives proposed by the Board and recommends that disclosures be required in the context of a principle-based approach.

Our detailed responses to the questions in the ED are set out in the appendix to this letter.

If you would like further clarification of the points raised in this letter, please do not hesitate to contact either Joaquin Sanchez-Horneros or me.

Yours sincerely

Francoise Flores

EFRAG, Chairman

Appendix

EFRAG's detailed responses to the questions asked in the Exposure Draft

Question 1

The exposure draft proposes that entities should recognise all changes in the present value of the defined benefit obligation and in the fair value of plan assets immediately when they occur. Do you agree? Why or why not?

Notes for EFRAG's constituents

1 *The exposure draft confirms the preliminary view in the discussion paper that entities should recognise all changes in the value of plan assets and in the post-employment benefit obligation in the financial statements in the period in which they occur.*

2 *In the Board's view, immediate recognition provides the most useful information to users of financial statements because:*

(a) it generates amounts in the statements of financial position and comprehensive income that are transparent, easy to understand and provide information about changes in the defined benefit obligation and plan assets in that period;

(b) it improves comparability across entities by eliminating the options; and

(c) it produces information that is neutral.

3 *Respondents to the discussion paper expressed several concerns about immediate recognition:*

(a) Some respondents consider that the measurement model needs a substantial review. However, the Board believes that any such review will retain the fundamental conclusion that an entity must account for its obligation to provide benefits as a result of service already rendered by employees;

(b) The current defined benefit measurement model was intended to take account of the long-term nature of the defined benefit obligation and the corridor approach is considered fundamental to treat a long-term liability. However, the Board concluded that the deferral features of defined benefit accounting are not necessary components of the model;

(c) Some changes to the net defined benefit asset/liability occurring in a period are not relevant to the measurement of a long-term defined benefit liability. This is because past gains or losses may be offset by future losses or gains. However, the Board notes that it is not inevitable that future gains and losses will occur and offset past losses and gains.

(d) Volatility would impede year-on-year comparability and obscure the profitability of the core business. However, the Board believes that a measure should be volatile if it represents faithfully transactions and other events that are themselves volatile, and financial statements should not omit such information. The Board proposes to require a presentation of changes in defined benefit cost that permits users of financial statements to isolate remeasurements of the entity's defined benefit plan;

(e) There may be adverse behavioural and social consequences if the Board requires entities to recognise all changes in the defined benefit obligation and in plan assets. In the Board's view, it is not the responsibility of accounting standard setters to encourage or discourage particular behaviour. Their responsibility is to set standards intended to result in clear and consistent information that faithfully represents an entity's financial position, financial performance and cash flows so that users of that information can make well-informed decisions; and

(f) There may be potential difficulties relating to certain covenants. However, in the Board's view, it is up to the entity and the holder of a covenant to determine whether to insulate the covenant from the effects of a future IFRS and, if not, how they might renegotiate it so that it reflects changes in the underlying financial condition rather than changes in reporting.

EFRAG´s response

- EFRAG agrees that all changes in the value of post-employment benefit obligations and plan assets should be recognised in the period in which they occur.

4 In our comment letter on the DP, EFRAG was generally supportive of eliminating options in IAS 19 as they hinder comparability between entities. Furthermore, EFRAG cannot find any compelling conceptual basis for the deferral or smoothing of actuarial gains and losses. Accordingly, EFRAG concurs with the Board's view that all changes in the value of the post-employment benefit obligation and plan assets should be recognised in the period in which they occur, with the proviso that the measurement of the plan assets and the pension obligation must take into account the long-term nature of the items. We agree with the arguments and advantages outlined in the ED, and would place particular emphasis to the lack of transparency caused by the use of the corridor approach and other deferral mechanisms, and the measurements that result.

5 In expressing the view above, EFRAG refers both to the need to present the resulting changes appropriately in the performance statement(s), and the need to measure the obligation using a basis that is consistent with the way the obligation will be settled from the point of view of the reporting entity.

6 As stated in the cover letter, the view above is expressed in the context of the short-term project to improve the current IAS 19 *Employee Benefits*. The views expressed in this comment letter do not necessarily apply to other standards or projects.

Question 2

Should entities recognise unvested past service cost when the related plan amendment occurs? Why or why not?

Notes for EFRAG's constituents

7 *In the Board's view, financial reporting would be significantly clearer if entities recognised all changes in the fair value of plan assets and in the post-employment benefit obligation in the period in which those changes occur. Accordingly, the exposure draft proposes to delete from IAS 19 options that allow an entity to defer the recognition of actuarial gains and losses (former paragraphs 92-93D and 95 of IAS 19).*

8 *The attribution of unvested benefits to past service results in a liability as defined by IAS 19. Therefore, the Board concluded that such a liability should be recognised in the period of the plan amendment.*

EFRAG´s response

- EFRAG agrees that unvested past service costs should be recognised immediately and in full.

9 Recognising unvested past service costs in their entirety in the period in which a plan amendment is made improves internal consistency of the IAS 19 measurement requirements. Indeed the general approach in existing IAS 19 is to allocate benefits to periods of service regardless of whether they have vested or not.

10 EFRAG observes that this is inconsistent with IFRS 2 *Share-based Payment* (paragraphs 27 and B43 of which require increases in benefits made within the vesting period to be attributed to each period of employees´ services from the time of the modification until the vesting date is reached). However, EFRAG thinks that internal consistency within IAS 19 is more important than consistency of this one aspect with IFRS 2.

Question 3

Should entities disaggregate defined benefit cost into three components: service cost, finance cost and remeasurements? Why or why not?

Notes for EFRAG's constituents

11 *Many commentators indicated in their response to the DP that disaggregation is essential to provide a proper understanding of the reasons for changes in the defined benefit assets and obligations during the period. The comment letters also noted an undesirable lack of comparability in how entities present components of defined benefit cost under the existing version of IAS 19.*

12 *Many commentators identified service cost, interest cost and remeasurements as components of defined benefit cost. Both service cost and interest cost convey information about an entity's recurring costs. In contrast, although information*

about remeasurements provides an indicator of the uncertainty of future cash flows arising from the defined benefit plan, it provides little direct information about the estimated amount and timing of those cash flows.

13 *The Board agrees that it is useful to present separately items that have different predictive implications. Accordingly, the Board proposes that entities should disaggregate changes in defined benefit cost into:*

(a) Service cost, that directly represents the cost of the services received. This includes current and past service cost, but not changes in the estimate of service cost.

(b) Finance cost, which represents the financing cost of deferring payment of service costs and comprises net interest income or expense on the net defined benefit asset or liability.

(c) Remeasurements, which represent the period-to-period fluctuations in the long-term value of the defined benefit obligation and plan assets. Remeasurements comprise: actuarial gains and losses on the defined benefit obligation, the return on plan assets, excluding amounts included in net interest income or expense any gain or loss on settlement; and any effects of the limit to the recognition of an asset.

EFRAG´s response

- EFRAG agrees with the proposed disaggregation of defined benefit costs.

14 EFRAG agrees with the proposed disaggregation of defined benefit costs and the fact that there will be only one way of presenting interest cost. In EFRAG's view, the presentation proposed improves comparability between entities by making a distinction between the costs of benefits and how those benefits are financed.

15 For example the service cost may be seen as representing part of the total employment cost for the period, with the view that employees services have been obtained in exchange for salaries and other benefits including the promise of pension benefits. Unless such a distinction is made, the current employment costs for the period are either understated (by omitting the value of pension promises made in the year) or overstated (by including interest expense). Comparability between entities is therefore enhanced by making this distinction.

16 The presentation requirements lead to clearer differentiation between funded and unfunded plans. In EFRAG´s view, this difference in presentation is justified because of differences in the underlying facts. The risks to investors and the existence of control over the plan assets depend on whether or not the assets are managed by the reporting entity.

Question 4

Should the service cost component exclude changes in the defined benefit obligation resulting from changes in demographic assumptions? Why or why not?

Notes for EFRAG's constituents

17 *The Board considered whether the effect of changes in demographic assumptions should be associated with service cost and included in the service cost component. In the discussion paper, the Board argued that changes in demographic assumptions cause a re-estimate of service costs and, if not treated in the same way as service costs, might encourage underestimation of service costs to achieve an accounting result.*

18 *The Board considers that the predictive values of service costs and of changes in estimates of service costs differ; thus the service cost component would be more relevant for assessing the ongoing operational costs of an entity if it did not also contain changes in estimates of service cost.*

EFRAG´s response

- EFRAG agrees that changes in demographic assumptions should not be presented as part of the service cost.

19 EFRAG agrees with the IASB that there are different drivers to changes in the pension obligation which have different predictive values. The service cost for pensions is affected by many assumptions. Separate presentation enhances the ability of users to make their own assessment about the possible changes in the underlying assumptions and their impact on future costs.

20 As a result, EFRAG agrees to separate:

(a) he current service cost (increase in the present value of liabilities for pensions expected to arise from employee service in the current period) and past service cost (change in the present value of the defined benefit obligation for employee service in prior periods, resulting from the introduction of, or changes to, long-term employee benefits) from

(b) the changes in the present value of liabilities due to changes in other factors or changes that are not directly related with performance by employees (or the introduction/changes in benefits from one period to the next e.g., staff turnover rates, early retirement rates or mortality rates). These changes would be considered changes in the estimate of service costs and included in the remeasurement component, being presented separated in the financial statements from those costs included in a)

Question 5

The exposure draft proposes that the finance cost component should comprise net interest on the net defined benefit liability (asset) determined by applying the discount rate specified in paragraph 78 to the net defined benefit liability (asset). As a consequence, it eliminates from IAS 19 the requirement to present an expected return on plan assets in profit or loss.

Should net interest on the net defined benefit liability (asset) be determined by applying the discount rate specified in paragraph 78 to the net defined benefit

liability (asset)? Why or why not? If not, how would you define the finance cost component and why?

Notes for EFRAG's constituents

21 *The discussion paper acknowledged the widespread view that an important economic effect of a funded plan is that there is offset between the change in plan assets that arises from the time value of money and the interest cost that arises from the defined benefit obligation. As a consequence, the return on plan assets should be divided into a component that arises from the effect of the time value of money and a component that results from the effect of changes in the underlying assumptions.*

22 *The Board concluded that part of the return on plan assets should appear in the finance cost component. The Board also proposes not to require that the total return on plan assets be classified as interest income, because that would be inconsistent with its decision to disaggregate the defined benefit cost into service cost, finance cost and remeasurements.*

23 *The Board found it difficult to distinguish interest income on plan assets from other changes in the value of plan assets, particularly for assets that do not bear explicit interest. The Board rejected approximations to the effect of passage of time on plan assets using:*

(a) the expected return on plan assets (as currently required by IAS 19) because it could not be determined in an objective way; and

(b) dividends received on equity plan assets and interest earned on debt plan assets (using the current rate market participants would require for equivalent asset). In the Board's view, if dividends from equity investments and returns from non-dividend-paying equity investments were presented in different ways, entities would have an incentive to invest in particular plan assets to achieve an accounting result, rather than for economic reasons.

24 *The Board considered using market yields on high quality corporate bonds to calculate interest income on plan assets. This approach is consistent with the view that the finance cost component of changes in defined benefit cost should include only interest on the net defined benefit asset or liability.*

25 *As an entity recognises a net defined benefit asset or liability, it is not relevant to present separately movements on the underlying assets and liabilities that combine to make a net defined benefit asset or liability.*

26 *Therefore the exposure draft proposes that the finance cost component comprises net interest income or expense. This is defined as the amount determined by applying the discount rate specified in paragraph 78, as determined at the start of the period, to the net defined benefit asset or liability throughout the period, taking account of any material changes in the net defined benefit asset or liability.*

EFRAG´s response

- EFRAG supports the proposal in the ED and agrees with the removal of the requirement in IAS 19 to reflect in profit or loss a return on assets based on an expected rate of return.

27 As stated in the cover letter, EFRAG expresses its view on the expected return on assets only in the context of the short-term project to improve the current IAS 19 *Employee Benefits*. The views expressed in this comment letter do not necessarily apply to other standards or projects.

28 A net approach is consistent with the current practice of investment strategies. Such strategies are designed to match the cash flows required to settle pension liabilities. Therefore, the impact of the time value of money on plan assets and defined benefit obligations should be presented together in the same section, that is, within finance costs. As a result, EFRAG agrees with the proposal.

29 EFRAG considers that expected return on assets is, at best, an amount estimated for budgetary purposes rather than the outcome from an economic event and there is no conceptual reason for including the expected return on assets in the statement of comprehensive income. The estimates of returns are based on market expectations rather than a unique assessment of the individual asset portfolio held by the pension plan. It is not necessarily true that assets of a pension plan are held with a long-term view and changes in market values are therefore irrelevant. It is not self evident that gains and losses will reverse (this may be the objective of investment policies but that objective may not be realised). Besides, distinguishing irrelevant short-term changes from relevant long-term changes is sometimes arbitrary.Therefore, in the context of information about management funding strategies (see response to Question 9), EFRAG thinks that information about expected return on assets may provide useful information to existing and potential equity investors, lenders and other creditors.

30 In addition, EFRAG wants to reiterate its support (which was included in EFRAG´s Comment Letter on IASB ED *Discount Rate for Employee Benefits*) for the proposal to have a single principle to determine the discount rate used for employee benefit obligations. However, EFRAG thinks entities need guidance on estimating a market yield and, in particular, guidance that resolves the issues that arise if there is not a deep market for high quality corporate bonds in an entity's jurisdiction.

Question 6

Should entities present:

a. service cost in profit or loss?

b. net interest on the net defined benefit liability (asset) as part of finance costs in profit or loss?

c. remeasurements in other comprehensive income?

Why or why not? Why or why not?

Notes for EFRAG's constituents

31 *The Board concluded that entities should disaggregate changes in the defined benefit obligation and in plan assets into service cost, finance cost and remeasurement components because these components have different characteristics and need to be distinguished. Further, although the changes included in the remeasurement component may provide information that helps with an assessment of the uncertainty of future cash flows, many regard those changes as non-recurring and less useful than the other components for assessment of the amount and timing of future cash flows.*

32 *The Board noted that it might be possible to disaggregate components of defined benefit costs without the need to recognise gains or losses in other comprehensive income by using additional line items in profit or loss. However, the Board argued that the most informative way to disaggregate the components of defined benefit cost with different predictive values is to present the remeasurement component in other comprehensive income.*

EFRAG´s response

- EFRAG agrees that service cost should be presented as an operating item in profit or loss, net interest income or expense should be presented as finance cost in profit or loss and remeasurements should be presented in OCI.

33 EFRAG is in favour of the removal of the options as it improves comparability and results in single accounting treatment and presentation.

34 However, EFRAG reiterates that all these views are only in the context of a short-term project to improve the current IAS 19 *Employee Benefits*. The views expressed in this comment letter do not necessarily apply to other IASB standards or projects like *Financial Statements Presentation* project or EFRAG pro-active projects like, for example, *Performance Reporting* project.

35 EFRAG believes that there is a need for a deeper debate on the conceptual issues underlying performance reporting, such as the notion of performance and the impact of business models on it, the content of performance statement(s) and recycling.

36 Some consider that all the components should be presented in profit and loss. A revision to an estimate is generally recognised in the same position in the statement of comprehensive income as the original estimate is recognised. However, EFRAG considers it useful that the accounting treatment of components that represent the period-to-period fluctuations in the long-term value of the defined benefit obligation and plan assets to be presented separately from the rest of components of pension costs. Indeed, the underlying reasons and causes of those fluctuations in long-term value are different in nature from the factors that cause changes in the other components of pension costs. If such changes in non-recurring components are recognised in profit and loss of an entity that may be unhelpful for users of financial statements in assessing performance on its operational activities.

Question 7

a. Do you agree that gains and losses on routine and non-routine settlement are actuarial gains and losses and therefore presented in the remeasurement component? Why or why not?

b. Do you agree that curtailments should be treated in the same way as plan amendments, with gains and losses presented in profit or loss?

c. Should entities disclose (i) a narrative description of any plan amendments, curtailments and non-routine settlements, and (ii) their effect on the statement of comprehensive income? Why or why not?

Notes for EFRAG's constituents

37 *In the existing version of IAS 19, curtailments and settlements trigger the recognition of previously unrecognised gains and losses.*

38 *The proposals in the exposure draft eliminate the potential for previously unrecognised gains and losses. Gains and losses arise on settlements because of a difference between the net defined benefit liability (asset), as remeasured at the transaction date, and the settlement price. Thus, settlements are accounted for as other remeasurements (with gains and losses presented in other comprehensive income) because they are experience adjustments arising in the period.*

39 *In addition, the exposure draft proposes that unvested past service costs should be recognised in the period of a plan amendment. This proposal means that curtailments are accounted for in the same way as negative past service costs (as plan amendments, with gains and losses recognised in profit or loss).*

40 *IAS 19 currently requires separate disclosure about curtailments and settlements. The Board proposed to retain similar disclosures to current IAS 19.*

EFRAG´s response

- EFRAG agrees with the proposals but thinks that clarification of the expression "non-routine settlements" is needed.

41 EFRAG agrees that, if the exposure draft eliminates the potential for previously unrecognised gains and losses, a detailed separate discussion of settlements and curtailments is not needed.

42 EFRAG also agrees with the proposals that settlements and curtailments should be accounted for in the same way as remeasurements and plan amendments respectively.

43 EFRAG thinks that disclosures for both curtailments and settlements are useful in providing an understanding of the causes of gains and losses and/or changes in the value of the net defined benefit liability in the period.

44 Having said that, EFRAG also thinks some clarification of the expression "non-routine settlements" is needed.

Question 8

The exposure draft states that the objectives of disclosing information about an entity's defined benefit plans are:

a. to explain the characteristics of the entity's defined benefit plans;

b. to identify and explain the amounts in the entity's financial statements arising from its defined benefit plans; and

c. to describe how defined benefit plans affects the amount, timing and variability of the entity's future cash flows.

Are these objectives appropriate? Why or why not? If not, how would you amend the objectives and why?

Notes for EFRAG's constituents

45 *The Board considered whether to provide specific guidance on how to apply the general notion of materiality in this context. However, the Board proposes not to provide guidance in IAS 19 on materiality, nor to require disclosures that cover the rage of circumstances that entities with a defined benefit plan may have. Rather, the Board proposes to articulate objectives for disclosures about defined benefit plans. This approach gives entities the flexibility to decide on an appropriate level of disclosure that enables users to see the overall picture but without combining information that has different characteristics.*

46 *The Board also considered whether it should require the same disclosure objectives for defined benefit plans as for long term financial instruments and insurance contracts. However, the Board concluded that much of the information about risks required by IFRS 7 and IFRS 4 for assets would be unnecessary in depicting an entity's involvement with a defined benefit plan because the entity does not manage the plan assets directly and does not have an unrestricted ability to access the economic benefits from those assets.*

47 *Accordingly, the Board focused the disclosure objective in IAS 19 on the matters most relevant to users of the sponsoring entity's financial statements, i.e. information that:*

(a) Explains the characteristics of the defined benefit plans.

(b) Identifies and explains the amounts in the financial statements arising from the defined benefit plans.

(c) Describes how participation in defined benefit plans affects the amount, timing and variability of the entity's future cash flows.

EFRAG´s response

- EFRAG agrees with the Board´s proposal to adopt a principle-based approach rather than a list of disclosures and agrees with the proposed disclosure objectives.

48 EFRAG considers disclosures should provide information that explains the economic consequences arising from the provision of pension benefits (that are not necessarily the same as other liabilities), having regard to the materiality of the amounts involved, such that:

(a) financial statements contain adequate disclosure of the cost of providing pension benefits and any related gains, losses, assets and liabilities;

(b) users of financial statements are able to obtain a clear view of the different effects, implications and consequences arising from liabilities to pay pension benefits and from the assets held to fund those benefits; and

(c) the funding obligations of the entity, in relation to liabilities to pay pension benefits, are clearly identified.

Question 9

To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:

a. information about risk, including sensitivity analyses;

b. information about the process used to determine demographic actuarial assumptions;

c. the present value of the defined benefit obligation, modified to exclude the effect of projected salary growth;

d. information about asset-liability matching strategies; and

e. information about factors that could cause contributions to differ from service cost.

Are the proposed new disclosure requirements appropriate? Why or why not? If not, what disclosures do you propose to achieve the disclosure objectives?

Notes for EFRAG's constituents

49 *The disclosures about the characteristics of defined benefit plans and the amounts in the financial statements arising from defined benefit plans are based on those in the existing version of IAS 19. In addition, the Board considered the following issues:*

(a) Exposure to risk: The exposure draft proposes that entities provide a narrative description of exposure to risk arising from their participation in the plan. The purpose is to provide more disclosures about the risks inherent in a defined benefit plan and the risks associated with plan assets held to fund the benefit.

(b) Plan assets: The Board concluded that extensive disaggregated information about plan assets was not necessary for users of the employer entity's financial statements because they are not held directly by the entity. Similarly, the Board concluded that disclosures about the fair value of plan

assets, such as those proposed in its exposure draft Fair Value Measurement, would not be relevant.

(c) *Specific actuarial assumptions: The exposure draft proposes an approach in which entities will have to use their judgement to determine which actuarial assumptions require disclosure. In particular, the Board proposes not to require specific disclosures about mortality rates. Instead, entities will need to use judgment to determine whether assumptions about mortality rates are a "principal actuarial assumption", requiring disclosure.*

(d) *Actuarial assumptions and the process used to determine them: The Board proposes to retain the requirement in IAS 19. Therefore, the exposure draft also proposes that entities should explain how it determined those actuarial assumptions (e.g., if an entity has developed mortality assumptions using a standard table, it could disclose the source of that table and when it was compiled).*

(e) *Alternative measure of the post-employment benefit liability: The Board proposes that entities disclose the defined benefit obligation, excluding projected growth in salaries (sometimes referred to as the accumulated benefit obligation). In some circumstances, this amount is similar to the amount of the entity's obligation if the plan were to be terminated, and some users believe that is relevant additional information. In addition, this amount is relevant to some who believe that the measurement of these liabilities should exclude projected salary growth.*

50 *The Board responded to requests for improved information about the amount, timing and variability of future cash flows to the plan as follows:*

(a) *The exposure draft proposes that entities provide quantitative disclosures, including sensitivity analysis, about actuarial assumptions used to determine the defined benefit obligation.*

(b) *With respect to asset-liability matching strategies, the exposure draft proposes that an entity disclose details of any asset-liability matching strategies that it uses, and the use of annuities and other techniques such as longevity swaps to manage longevity risk.*

(c) *The exposure draft proposes disclosure of factors that could cause contributions to differ from service cost. The Board believes this is more useful than merely disclosing expected payments in the next year.*

EFRAG´s response

- EFRAG agrees with most of the disclosures proposed by the Board. However, the IASB should avoid, to an even greater degree, exhaustive lists of mandatory disclosures but rather present useful examples that show how the disclosure objectives might be met.

51 EFRAG agrees with most of the disclosures proposed by the Board because they contribute to meeting the disclosure objectives stated in the ED. However, EFRAG thinks that, in line with the standard's principle-based approach, the IASB should not present the disclosure requirements in the form of an exhaustive list of

mandatory disclosures but rather present them in the form of useful examples that show how the disclosure objectives might be met.

52 EFRAG thinks that information about demographic and actuarial assumptions (disclosing changes in those assumptions and their impact) are more relevant and useful than the reference to the process used to determine demographic and actuarial assumptions because those assumptions are not expected to be volatile.

53 EFRAG considers disclosures about management funding strategies, information about expected costs and outflows to be especially relevant to help users assess future cash flows arising from the net liability. In addition, we also believe that information on how the assets are managed to be relevant, particularly if there are restrictions on the use of those assets.

Question 10

The exposure draft proposes additional disclosures about participation in multi-employer plans. Should the Board add to, amend or delete these requirements? Why or why not?

Notes for EFRAG's constituents

54 *Entities participating in a defined benefit multi-employer plan face greater risks than other entities, for example, risks that result from action by other participants in the plan. Accordingly, the exposure draft proposes additional disclosures about participation in a multi-employer plan. Such disclosures requirements vary depending upon the plan has been accounted as a defined contribution plan or a defined benefit plan.*

EFRAG´s response

- EFRAG finds the additional disclosures required by the ED very useful. However, we refer the Board to the additional disclosures identified in our answer.

55 EFRAG believes that no net asset or liability (asset) should be recognised except for the current pension contributions payable and any additional amounts that an entity might be required to pay to a multi-employer plan. However, as it is difficult to identify a "reliable" basis for measuring an individual employer's share in a multi-employer plan's net liability (asset), we believe the additional disclosures required by the ED to be very useful.

Question 11

The exposure draft updates without further reconsideration, the disclosure requirements for entities that participate in state plans or defined benefit plans that share risks between various entities under common control to make them consistent with the disclosures in paragraphs 125A-125K. Should the Board add to, amend or delete these requirements? Why or why not?

Notes for EFRAG's constituents

56 *The Board has updated disclosure requirements for entities that participate in state plans or defined benefit plans that share risks between various entities under common control to maintain consistency with the disclosures required for the rest of entities.*

EFRAG´s response

- EFRAG agrees with the proposed amendments because EFRAG considers that needs of information for users are the same regardless of the control structure.

Question 12

Do you have any other comments about the proposed disclosure requirements?

57 EFRAG does not have any other comments at this stage.

Question to EFRAG's constituents

58 Do you have any other comments about the proposed disclosure requirements?

Question 13

The exposure draft also proposes to amend IAS 19 as summarised below:

a. The requirements in IFRIC 14 IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction, as amended in November 2009 are incorporated without substantive change.

b. "Minimum funding requirement" is defined as any enforceable requirement for the entity to make contributions to fund a post-employment or other long-term defined benefit plan.

c. Tax payable by the plan shall be included in the return on plan assets or in the measurement of the defined benefit obligation, depending on the nature of the tax.

d. The return on plan assets shall be reduced by administration costs only if those costs relate to managing plan assets.

e. Expected future salary increases shall be considered in determining whether a benefit formula expressed in terms of current salary allocates a materially higher level of benefits in later years.

f. The mortality assumptions used to determine the defined benefit obligation are current estimates of the expected mortality rates of plan members, both during and after employment.

g. Risk sharing and conditional indexation features shall be considered in determining the best estimate of the defined benefit obligation.

Do you agree with the proposed amendments? Why or why not? If not, what alternative(s) do you propose and why? Do you agree? Why or why not? What alternative do you propose?

Notes for EFRAG's constituents

IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

59 *The exposure draft proposes that IAS 19 should incorporate, without substantive change, the requirements of IFRIC 14. The Board noted reports of diversity in how entities interpreted the definition of "minimum funding requirement" in IFRIC 14. The Board proposes to eliminate this diversity by clarifying that a minimum funding requirement is any enforceable requirement for the entity to make contributions to fund a post-employment or other long-term defined benefit plan.*

Tax payable

60 *The Board noted that some have interpreted IAS 19 as excluding from the measurement of the defined benefit obligation taxes paid by a plan on contributions made by the entity. In the Board's view, the ultimate cost of meeting an obligation to a plan would be the amount of any deficit in the plan, plus any additional tax payable by the plan when the contribution is made. Accordingly the Board proposes to amend IAS 19 to clarify that the estimate of the defined benefit obligation can include taxes payable by the plan, and if this is the case, that those taxes should not be included in the return on plan assets.*

Costs relating to the management of plan assets

61 *The Board decided to remove the options in IAS 19 for entities to include plan administration costs in either the return on plan assets or in the actuarial assumptions used to measure the defined benefit obligation. In the Board's view, only administration costs relating to the management of plan assets should be included in the return on plan assets. Other administration costs (e.g., the cost of administering benefit payments) are unrelated to the plan assets and should be included in the measurement of the defined benefit obligation.*

62 *In the Board's view:*

(a) When the benefit promise depends on the return on plan assets less asset management costs, asset management costs should be included in the measurement of the defined benefit obligation because they affect the amount of the obligation.

(b) When the benefit promise does not depend on the return on plan assets less asset management costs (e.g., a salary-related promise), asset management costs should be included in the return on plan assets because they have no bearing on the defined benefit obligation.

63 *Therefore, the Board proposes that the return on plan assets should include plan administration costs if those costs relate to the management of plan assets; and the benefit promise does not depends on the return on those plan assets.*

Expected future salary increases

64 *Paragraph 67 of IAS 19 requires an entity to attribute benefit on a straight-line basis if an employee's service in later years will lead to a materially higher level of benefit than in earlier years. Some respondents to the DP stated that it is unclear how to interpret this requirement.*

65 *The exposure draft proposes that expected future salary increases are included in determining whether a benefit formula expressed in terms of current salary allocates a materially higher level of benefit in later years.*

66 *The Board believes that if expected future salary increases are not included in determining whether a benefit formula expressed in terms of current salary allocates a materially higher level of benefit in later years, there would be different attribution requirements for career average salary benefits and current salary benefits. Such benefits could be the same economically. In the Board's view benefits that are economically the same should be measured equally regardless of how they are described in the benefit formula.*

67 *The Board also noted that IAS 19 requires entities to measure the defined benefit obligation at the best estimate of the amount that reflects the future cost of settling that obligation. It would be consistent with this principle to include expected future salary increases in determining whether a benefit formula allocates a materially higher level of benefit in later years.*

Mortality assumptions

68 *In the Board's view, the best estimate of the amount that reflects the future cost of settling the defined benefit obligation should include the effect of estimates of future changes in mortality assumptions.*

Risk sharing and conditional indexation

69 *Some defined benefit plans include features whereby the benefits of a surplus or the cost of a deficit are shared between the employer and plan participants. Similarly, some defined benefit plans provide benefits that are conditional to some extent on there being sufficient assets in the plan to fund them. Such features result in the sharing of risk between the entity and plan participants. The Board noted that diversity in practice exists as to how the requirements of IAS 19 apply to arrangements with risk sharing and conditional indexation features.*

70 *The Board noted that any plans that expose the entity to risk are defined benefit plans. The Board also noted that IAS 19 requires that the defined benefit obligation is measured using the best estimate of the ultimate cost of providing that benefit. In the Board's view, assumptions about the effect of risk sharing and conditional indexation features affect that cost. Accordingly, the exposure draft proposes to clarify that risk sharing and conditional indexation features should be incorporated into the determination of the best estimate of the defined benefit obligation.*

EFRAG´s response

IFRIC 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

- EFRAG agrees with the IASB's analysis and reasoning about the incorporation of the requirements established by IFRIC 14 and the definition of "minimum funding requirement".

Tax payable

71 EFRAG agrees with the proposed amendment to clarify that taxes payable have to be considered. We think that their inclusion in the return on plan assets will depend on the nature of the tax payable. Taxes that are related to the administration of the assets should be considered in the return on assets.

Costs relating to the management of plan assets

72 Most EFRAG members agree with the Board´s proposal that costs of managing plan assets should be deducted from the return on those assets and other costs incurred should be included in the calculation of the defined liability. Nevertheless, these members recognise that in practice it might be difficult to separate these costs clearly (e.g., some insurance arrangements may combine both elements).

73 However, some other members consider that all costs should be expensed as incurred and not included in the calculation of the defined benefit liability. These expenses are within the entity's control (and, hence, avoidable) in the sense that the entity's future facts and circumstances will determine whether, and how much, expenses are incurred.

74 Administration costs for future periods could only be linked to the assets and liabilities if such assets or liabilities are directly related to the underlying arrangements. An analysis of the agreement is necessary to determine the allocation of costs and such allocation will depend on facts and circumstances.

Question to EFRAG's constituents

75 Do you believe that the costs of managing plan assets should be deducted from the return on those assets? Which approach do you prefer?

76 In your experience, do you believe it is possible in practice to separate the costs of managing plan assets from other costs incurred?

Expected future salary increases

- EFRAG agrees that expected salary increases should be considered in determining the best estimate of the defined benefit obligation when a benefit formula expressed in terms of current salary allocates a materially higher level of benefit to later years (for the reason explained in BC89).

Mortality assumptions

- EFRAG agrees that the best estimation of the liability should include the effect of estimates of future changes in mortality.

Risk sharing and conditional indexation

- EFRAG agrees with the clarification that risk sharing and conditional indexation features should be incorporated into the determination of the best estimate of the defined benefit obligation.

77 EFRAG agrees with the position that plans that share some of the risks between employers and employees do not fit easily into the traditional defined contribution or defined benefit accounting models. One of the shortcomings of the existing accounting standards on pensions is that they do not state a measurement objective. They specify a measurement method (projected unit method) for defined benefit liabilities – traditionally pension benefits that are related to employees' earnings and length of service. The measurement requirements of the standard do not deal adequately with the spectrum of risk-sharing that has evolved in pension plans.

78 Consequently, EFRAG believes that risk sharing and conditional indexation should be considered more fully in the measurement of the pension obligation.

79 Having said that, and in the context of the limited revision of IAS 19, EFRAG agrees that these kinds of plans should be accounted for as defined benefit plans. Indeed, an entity may have a legal or constructive obligation to fund deficits related to employee services in the current and prior periods, and EFRAG believes that this obligation should be recognised.

Question 14

IAS 19 requires that entities account for a defined benefit multi-employer plan as a defined contribution plan if it exposes the participating entities to actuarial risks associated with the current and former employees of other entities, with the result that there is no consistent and reliable basis for allocating the obligation, plan assets and cost to individual entities participating in the plan. In the Board's view, many plans that meet the definition of a defined benefit multi-employer plan would also meet the condition for defined contribution accounting.

Please describe any situations in which a defined benefit multi-employer plan has a consistent and reliable basis for allocating the obligation, plan assets and cost to the individual entities participating in the plan. Should participants in such multi-employer plans apply defined benefit accounting? Why or why not?

Notes for EFRAG's constituents

80 *In Board´s view, this exception would not be appropriate for all multi-employer plans. For example, the Board concluded that when an entity becomes a dominant participant in a multi-employer plan, perhaps because other participants leave the plan, it should not be exempt from accounting for the plan as a defined benefit plan.*

81 *Besides extending that exemption is contrary to the general approach of limiting exceptions.*

EFRAG´s response

- EFRAG considers that probably the best allocation basis is the internal agreement among all the employers that participate in the multi-employer plan.

82 Multi-employer plans exist in many jurisdictions. Sometimes these plans are initiated or ratified by local government (in order to create an industry-wide pension fund in which employers active in a certain industry are allowed or required to participate) or are established by certain entities at their own initiative (in order to pool assets, realise economies of scale and share the inherent actuarial risks).

83 Current practice is diverse:

(a) In some countries these plans are treated as defined contribution.

(b) Sometimes, the treatment is based on a consensus between parties involved (reporting entities, accountants, enforcement authorities).

(c) In other countries the plans are accounted as defined contribution plans, but entities make use of the option stated in paragraph 32 a) of IAS 19 because they are not provided, despite their requests, with the necessary information to make proper calculations.

(d) Other entities make use of paragraph 32 b) of IAS 19 (no consistent or reliable basis for allocation) or may receive letters from the Board of the multi-employer plan in which this argument is used.

(e) In other cases the allocation of the plan is affected according to the options stated in paragraph 29 of IAS 19.

84 One of the possible allocation methods is to use a criterion that is related to the basis that is also used for determining the pension contribution. This basis would, in many cases, be related to the pensionable salary of the active employees. In this event the allocation criterion would be the pensionable salary of the individual employer divided by the total pensionable salary of all the participating employers. The basis for this criterion is that the amount of the contribution is directly related to the benefit (and, therefore, to the asset). The employer normally has access to information to calculate the ratio between its contribution to the plan and the total contributions (if it is possible, on a cumulative basis to avoid impacts due to deficits or surpluses). The proportionate share of the individual employer can be determined by multiplying the total pension asset (liability) by that ratio.

85 The periodic change in the employer’s share of the multi-employer plan’s total assets (liabilities) should be classified as a separate line item in OCI similar to actuarial gains and losses whereas the pension contribution payable could be classified as employee compensation expense.

86 However, it is agreed that the outcome of the approach described above is not perfect and also not necessarily the same as individual employer’s future cash-flows related to its participation in the fund.

87 It seems defined benefit accounting is better to provide useful and relevant information for users of financial information than defined contribution accounting with additional disclosures. However, it seems also clear that defined benefit accounting is only possible if a reliable allocation can be made.

Question 15

Do you agree that entities should apply the changes resulting from the proposed amendments retrospectively? Why or why not?

Notes for EFRAG's constituents

88 *The ED proposes that entities apply the proposed amendments to IAS 19 retrospectively, in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. As explained in BC91, in the Board's view it would not be unduly burdensome for entities to apply the proposed changes to IAS 19 retrospectively. Although some of the proposed amendments will change the amounts recognised, entities will not have to recalculate amounts for dates earlier than the beginning of the first period presented in the financial statements. The amounts depend solely on conditions at that date, not on assessments made on previous dates.*

89 *For first-time adopters, the Board proposes to delete paragraphs D10 and D11 of Appendix D of IFRS 1, because the proposals in the ED make these two paragraphs redundant. Paragraph D10 deals with the application of the corridor approach for first-time adopters of IFRSs. Paragraph D11 relates to the 5 year disclosure requirements of paragraph 120A (p) of the existing version of IAS 19. The Board proposes to delete this disclosure requirement.*

EFRAG´s response

- EFRAG agrees with the proposal in the ED that the amendment should be treated as a change in accounting policy.

Question to EFRAG's constituents

90 Concerns have been raised about the availability of the information needed by entities for a full retrospective application. Do you believe that the information needed for a full retrospective application is available to entities? If not, what information would not be available?

Question 16

In the Board's assessment the main benefits of the proposals are:

- **Reporting changes in the carrying amount of defined benefit obligations and changes in the fair value of plan assets in a more understandable way.**

- **Eliminating some presentation options currently allowed by IAS 19, thus improving comparability.**
- **Clarifying requirements that have resulted in diverse practices.**
- **Improving information about the risks arising from an entity's involvement in defined benefit plans.**
- **Improved comparability between entities**
- **Improved disclosures about defined benefit plans.**

Do you agree with the Board's assessment? Why or why not?

In the Board's assessment the costs of the proposal should be minimal because entities are already required to obtain much of the information required to apply the proposed amendments in applying the existing version of IAS 19.

Do you agree with the Board's assessment? Why or why not?

Notes for EFRAG's constituents

91 *The objective of the proposed amendments is to improve the usefulness of information available to users for their assessment of the amounts, timing and uncertainty of future cash flows of financial assets. However, the Board also considered the cost of implementing the proposed amendments and applying it on a continuous basis. In evaluating the relative costs and benefits of the proposed amendments, the Board was assisted by meetings with its Employee Benefits Working Group, a group of senior professionals with extensive practical experience in the operation, management, valuation, financial reporting, auditing or regulation of a variety of post-employment benefit arrangements.*

92 *The proposed amendments, if confirmed, should improve the ability of users to understand the financial reporting for post-employment benefits by:*

(a) Increasing transparency about changes in the defined benefit obligation and plan assets as they occur,

(b) Improving comparability by eliminating the options currently allowed by IAS19.

(c) Clarifying requirements in the existing version of IAS 19 that have resulted in diverse practices.

(d) Improving disclosures about defined benefit plans by clarifying the disclosure objectives.

93 *Costs would be involved in the adoption and ongoing application of the proposed amendments. Those costs will depend on the complexity of an entity's defined benefit arrangements and the options in IAS 19 it currently elects to apply. However, those costs should be minimal because entities are already required to obtain much of the information required to apply the proposed amendments in applying the existing version of IAS 19. Consequently, the Board believes that the benefits of proposed amendments outweigh the costs.*

EFRAG´s response

Question to EFRAG's constituents

94 In your assessment, do the benefits of these proposals outweigh the costs? Please support your response with evidence of the benefits and costs you believe grow from these proposals.

Question 17

Do you have any other comments on the proposals?

Question to EFRAG's constituents

95 Do you have any other comments about the proposed disclosure requirements?