

Draft Comment Letter

Comments should be submitted by 5 July 2013 to Commentletters@efrag.org

XX July 2013

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir/Madam,

Re: Exposure Draft Defined Benefit Plans: Employee Contributions

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Exposure Draft *Defined Benefit Plans: Employee Contributions (Proposed amendments to IAS 19)* issued by the IASB on 25 March 2013 (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 the definitive IFRS in the European Union and European Economic Area.

EFRAG agrees with the IASB's proposals on the basis that they clarify the existing requirements in IAS 19 (2011) on accounting for contributions from employees or third parties and provide relief to preparers. We also support the IASB in addressing the existing inconsistency in IAS 19 (2011) in relation to the attribution of these contributions as this would reduce potential divergence in practice.

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 Apostolena Theodosiou, Anna Vidal or me.

Yours faithfully,

Françoise Flores

EFRAG Chairman

Appendix

EFRAG's responses to the questions raised in the Exposure Draft

Question 1: Reduction in service cost

The IASB proposes to amend IAS 19 to specify that contributions from employees or third parties set out in the formal terms of a defined benefit plan may be recognised as a reduction in the service cost in the same period in which they are payable if, and only if, they are linked solely to the employee's service rendered in that period. An example would be contributions that are a fixed percentage of an employee's salary, so the percentage of the employee's salary does not depend on the employee's number of years of service to the employer. Do you agree? Why or why not?

Notes to constituents

- 1 *The amendments to IAS 19 Employee Benefits made in 2011 require employees or third parties contributions either to reduce service cost, if they are linked to service, or reduce remeasurements (e.g. if the contributions are required to reduce a deficit arising from losses on plan assets or actuarial losses). In particular, employees or third parties contributions in respect of service should be attributed to periods of service as a negative benefit (paragraph 93 of IAS 19).*
- 2 *As noted in paragraph BC4 of the ED, constituents raised concerns about the complexity of the required calculations because entities should consider the present value of employees' or third parties' contributions that relate to the employee's service before the reporting date when measuring the defined benefit obligation. Even a very simple contributory plan (e.g. a fixed percentage of salary) would be subject to a complex calculation for attributing the benefits to periods of service as a negative benefit.*
- 3 *Based on the outreach activities carried out by IASB staff, the current prevalent approach to account for employee contributions is to deduct them from service cost when received, rather than to include them in measuring the defined benefit obligation. Therefore, most would need to revise their accounting policy in the light of the amendments made in 2011.*
- 4 *The IASB proposes to amend IAS 19 to add a practical expedient to paragraph 93. The practical expedient specifies that contributions from employees or third parties set out in the formal terms of a defined benefit plan may be recognised as a reduction in the service cost in the same period in which they are paid, if the contributions are linked solely to the employee's service rendered in that period.*
- 5 *Entities would be required to apply the amendment retrospectively, in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Earlier application is permitted.*

EFRAG's response

EFRAG supports the IASB's proposal on the basis that it clarifies existing requirements in IAS 19 (2011) and provides helpful relief for preparers.

- 6 EFRAG supports the amendment of IAS 19 (2011) on the basis that the ED clarifies existing paragraph 93 and provides relief to preparers on the accounting for contributions from employees and third parties in certain circumstances. We

believe that the proposed amendment to paragraph 93 would address diversity in practice that otherwise would likely arise regarding the accounting for contributions from employees or third parties to defined benefit plans.

- 7 EFRAG agrees with paragraph BC4 of the ED which explains that contributions from employees or third parties to a defined benefit plan should be attributed to the periods of service as a negative benefit, since entities should recognise service cost in profit or loss according only to its share on the total cost of the employee's benefit.
- 8 EFRAG, in its comment letter on the Exposure Draft *Amendments to IAS 19 Employee Benefits*, already noted that risk sharing (and conditional indexation) features should be considered more fully in the measurement of the pension obligation to ensure that financial statements reflect the best estimate of the ultimate cost of providing the pension benefit. Accordingly, we agree that the measurement of the defined benefit obligation should consider the present value of those future contributions that relate to the employees' service before the reporting date.
- 9 EFRAG is however aware that constituents have raised concerns about the complexity of the calculations required by paragraph 93 of IAS 19 (2011). We understand that this is because entities should consider all future contributions that relate to the employee's service in the current and prior periods when measuring the defined benefit obligation.
- 10 Therefore, we agree to a practical expedient that allows entities to choose between accounting for contributions from employees or third parties either as a reduction in service cost or considering them as a negative benefit when applying the projected unit method, provided that these contributions are linked solely to the employee's service rendered in that period. We believe that the practical expedient will provide helpful relief to constituents in the accounting for simple and widespread plans like those where employees' contributions are a reduction in salary.

Question to EFRAG constituents

- 11 Are constituents aware of any circumstances where the application of the practical expedient would result in contributions being inappropriately recognised as reductions in service cost? If so, please provide details.

Question 2: Attribution of negative benefit

The IASB also proposes to address an inconsistency in the requirements that relate to how contributions from employees or third parties should be attributed when they are not recognised as a reduction in the service cost in the same period in which they are payable. The IASB proposes to specify that the negative benefit from such contributions is attributed to periods of service in the same way that the gross benefit is attributed in accordance with paragraph 70. Do you agree? Why or why not?

Notes to constituents

- 12 *Paragraph 93 of IAS 19 (2011) is unclear on whether the back-end loading test in paragraph 70 should be performed on the net benefit, or the gross benefit and the*

negative benefit separately. To address this issue, the ED proposes to specify in paragraph 93 that the negative benefit from employee contributions or third parties should be attributed to periods of service in the same way that the gross benefit is attributed in accordance with paragraph 70 when they are not recognised as a reduction in the service cost in the same period in which they are payable. That is, unless the proposed practical expedient applies.

EFRAG's response

EFRAG supports the IASB's proposal on the basis that it addresses an existing inconsistency in IAS 19 (2011).

- 13 EFRAG supports the amendment, because we believe that attribution should be consistent between gross benefit and employee contributions to arrive at a net benefit. Using different attributions would distort the measurement of the defined benefit obligation. In other words, if the gross benefit is attributed on a straight-line basis because of a materially higher level of benefit in later years (as required by paragraph 70 of IAS 19 (2011)), then employee contributions should also be attributed on a straight-line basis. In addition, we agree with the argument in paragraph BC7 that performing the test on the net benefit would result in added complexity.

Question 3: Other comments

Do you have any other comments on the proposals?

EFRAG's response

- 14 EFRAG does not have any other comments on the proposals.