Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

DRSC

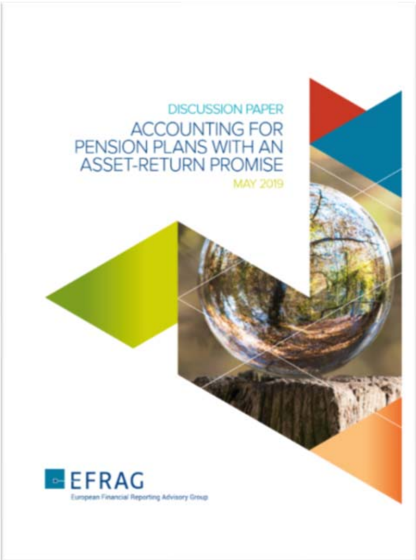
© DRSC e.V. ‖ Zimmerstr. 30 ‖ 10969 Berlin ‖ Tel.: (030) 20 64 12 - 0 ‖ Fax.: (030) 20 64 12 - 15
www.drsc.de - info@drsc.de

IFRS-FA – öffentliche SITZUNGSUNTERLAGE

Sitzung:	75. IFRS-FA / 13.06.2019 / 13:30 – 15:30 Uhr
TOP:	03 – EFRAG DP Pension Plans
Thema:	Erörterung vorgeschlagener Bilanzierungsalternativen
Unterlage:	75_03a_IFRS-FA_Pension Plans_Disk

Introduction

EFRAG’s DP on pension plans



- Explores **alternative accounting treatments** for post-retirement employee benefits promising the higher of the return on identified item(s) holding by the entity and a minimum guaranteed return
- Uses a **simplified case** to illustrate and to compare the accounting outcomes of the alternative approaches to the existing IAS 19 requirements
- Provides an initial **assessment** of alternative accounting treatments by listing differences in how the approaches meet aspects of the qualitative characteristics of useful financial information included in the IASB’s Conceptual Framework

Introduction

Three alternative accounting approaches

Alternatives for accounting for plans with an asset-return promise

Capped Asset Return approach*	Fair Value Based approach	Fulfilment Value approach
the rates used to project the final benefit entitlement are capped to the discount rate	the measurement of the pension obligation is based on the fair value of plan assets and the minimum return guarantee	the measurement of the pension obligation is based on the present value of the fulfilment cash flows and the value of the minimum return guarantee

* Approach explored in IASB's research project

Agenda

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1.	Previous discussions and projects in the field of pension accounting (context information)
2.	Assessment of approaches discussed (chapter 5 of the DP)
3.	ASCG activities: next steps

Previous discussions and projects in the field of pension accounting

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D9 Employee benefit plans with a promised return on contributions or notional contributions

- In 2004, the IFRS IC issued a Draft Interpretation *D9 Employee Benefit Plans with a Promised Return on Contributions or Notional Contributions*, to provide guidance on how to apply the requirements of IAS 19 to an employee benefit plan with a promised return on actual or notional contributions.
- The model in the Draft Interpretation D9 required entities to measure benefits with a variable return at the fair value of the underlying reference assets and those with a fixed return using the guidance for defined benefit plans in IAS 19. The liability would then be measured at the higher of those two amounts.
- However, the IFRS IC removed this project from its agenda because it was unable to reach a consensus on a suitable scope for an amendment that would both:
  a) Improve the accounting for a sufficient population of plans such that the benefits would exceed the costs; and
  b) Limit any unintended consequences that would arise from making an arbitrary distinction between otherwise similar plans.

Source: DP p. 16

Previous discussions and projects in the field of pension accounting

IASB Research Project “Pension Benefits that Depend on Asset Returns”

- Pension Benefits that Depend on Asset Returns is a **narrow-scope research project** designed to consider only some types of pension benefits paid that depend, wholly or partly, on asset returns. The assets could be held by the plan itself (as plan assets) or by the employer. It might be that they are held by neither the plan nor the employer, being used solely as a reference point to determine the amount to be paid.
- The scope of the project is defined in terms of types of benefit, not types of plan. Some plans might provide some benefits within the scope of the project and other benefits that are not.
- The project will not investigate other aspects of these benefits, or other aspects of plans that provide such benefits. For example, it will not investigate:
  - (a) ‘higher of’ guarantees (i.e. when the employee is guaranteed the higher of two or more possible outcomes, of which one is based on the actual return on plan assets); or
  - (b) risk-sharing or other features of what are sometimes called ‘hybrid plans’.
- The expected output of this research project is evidence to help the Board decide whether to undertake standard-setting to develop proposals for a targeted amendment to IAS 19.
- If the research establishes that this approach would not be feasible, the staff expects to recommend no work on pensions.

Source: ASAF, December 2018, AP 7

Agenda

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1.	Previous discussions and projects in the field of pension accounting (context information)
2.	Assessment of approaches discussed (chapter 5 of the DP)*
3.	ASCG activities: next steps

* According to the DP/EFRAG

Assessment of approaches discussed

Questions relating to chapter 5

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Q 2 Assessments of approaches – aspects to consider Do you agree with the aspects of qualitative characteristics considered in the assessment of the various approaches in Chapter 5? If not, which aspects do you think should/should not have been considered? Do you agree with the assessments of the various approaches made in Chapter 5?

Q 3 Assessment of approaches – assessment of complexity The assessment in Chapter 5 of the costs related to the various approaches presented in this DP, only considers implementation costs. Do you think that the complexity related to preparing financial information in accordance with the approaches would differ significantly? If yes, which approaches would be the most complex and least complex to apply?

Q 4 Choice of approach Which of the three alternative approaches, presented in this DP, do you support? How should it be further developed?

Assessment of approaches discussed

Summarised assessment

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
Is the information relevant?				
• Does the approach reflect how the pension obligation will be settled?	★	★	★	★★
• Is the economic covariance between plan assets and pension obligation reflected?		★	★★★	★★★
• Is a net pension liability recognised when the plan assets are expected to be insufficient to cover the portion of the final benefit entitlement for the service provided to date?	★★	★★	★★★	★★★
• Does the calculation of current service cost result in a useful reflection of pension cost related to a particular period?	★★	★★	★★★	★★★
• Is information about the value of the minimum return guarantee provided?			★★★	★★★
Is the employee's right to receive the higher of the return on plan assets and the minimum guaranteed return reflected in a complete manner?	★	★	★★★	★★★
Can requirements be applied retrospectively?	N/A	★★★	★★	★★
Is the obligation element related to the minimum guaranteed return accounted for similarly to plans under IAS 19?	N/A	★★★	★	★
Is the obligation related to the return on plan assets accounted for similarly to plans under IAS 19?	N/A	★	★★★	★★★
Is the information understandable?	★	★	★★	★★
Will the implementation of the approach be uncostly?	N/A	★★	★	★

★ Low fulfilment of the qualitative characteristic. ★★ Medium fulfilment of the qualitative characteristic.
★★★ High fulfilment of the qualitative characteristic. N/A The effect is not relevant to consider for the approach.

Source: DP p. 40

Assessment of approaches discussed

Aspects to consider

Relevance: slide 11-15

- Does the approach reflect how the pension obligation will be settled?
- Is the economic covariance between plan assets and pension obligation reflected?
- Is the pension liability recognised when the plan assets are expected to be insufficient to cover the portion of the final benefit entitlement for the service provided to date?
- Does the calculation of current service cost result in a useful reflection of pension cost related to a particular period?
- Is information about the value of the minimum return guarantee provided?

Faithful Representation: slide 16

- Is the employee‘s right to receive the higher of the return on plan assets and the minimum guaranteed return reflected in a complete manner?

Comparability: slide 17-18

- Can the requirements be applied retrospectively?
- Is the obligation element related to the minimum guarantee return accounted for similarly to plans under IAS 19?
- Is the obligation related to the return on plan assets accounted for similarly to plans under IAS 19?

Understandability: slide 19

- Is the information understandable?

Implementation costs: slide 20

- Will the implementation of the approach be uncostly?

Assessment of approaches discussed

Relevance (1/5)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
• Does the approach reflect how the pension obligation will be settled?	★	★	★	★★

– Fair value approach reflect the amount an entity would have to pay to *transfer* the obligation to a *third party*; IAS 19, the Capped Asset Return approach and the Fulfilment Value approach reflect an estimate of the resources needed to *fulfil* the obligation to the *employee.*
– IAS 19 and Capped Asset Return approach do not always reflect the outflow assessed to be necessary to settle the obligation.

The Fulfilment Value approach best reflects how the pension obligation will be settled.

Assessment of approaches discussed

Relevance (2/5)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
• Is the economic covariance between plan assets and pension obligation reflected?		★	★★★	★★★

- Under the Capped Asset Return approach different measurement bases are used for the plan assets and the pension obligation. However, in cases in which an employee's service in later years will not lead to a materially higher level of benefit than in earlier years and the (uncapped) expected return rate is higher than the discount rate, the approach could appropriately reflect the covariances.
- Under the Fair Value Based approach both the assets and the obligation will be measured at the fair value of the plan assets. In addition, the measurement of the obligation will include the fair value of the minimum return guarantee.

The covariance between plan assets and the pension obligation is best reflected by the Fair Value Based approach and the Fulfilment Value approach.

Assessment of approaches discussed

Relevance (3/5)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
• Is a net pension liability recognised when the plan assets are expected to be insufficient to cover the portion of the final benefit entitlement for the service provided to date?	★★	★★	★★★	★★★

- IAS 19 would not always result in a net pension liability being recognised when a pension plan is underfunded. The same could happen under the Capped Asset Return approach.
- The Fair Value Based approach and the Fulfilment Value approach would always result in the recognition of a net pension liability in such circumstances.

Whether or not a pension plan is underfunded is best reflected by the Fair Value Based approach and the Fulfilment Value approach.

Assessment of approaches discussed

Relevance (4/5)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
• Does the calculation of current service cost result in a useful reflection of pension cost related to a particular period?	★★	★★	★★★	★★★

– IAS 19 and the Capped Asset Return approach will result in current service cost representing a proportion of the final benefit entitlement. However, the measurement of the pension obligation, and hence the current service cost may not reflect the actual expected outflow of resources.
– Under the Fair Value Based approach and the Fulfilment Value approach current service cost equals the contribution of the employer for the period and the value of the minimum return guarantee.

This aspect is best reflected by the Fair Value Based approach and the Fulfilment Value approach.

Assessment of approaches discussed

Relevance (5/5)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
• Is information about the value of the minimum return guarantee provided?			★★★	★★★

- The Capped Asset Return approach does not reflect the value of the minimum return guarantee.
- Under the Fair Value Based approach and the Fulfilment Value approach the value of the minimum return guarantee is reflected.

Information about the value of the minimum guarantee is best reflect by the Fair Value Based approach and the Fulfilment Value approach.

Assessment of approaches discussed

Faithful representation

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
Is the employee's right to receive the higher of the return on plan assets and the minimum guaranteed return reflected in a complete manner?	★	★	★★★	★★★

- A faithful representation would have to be complete, neutral and free from error.
- In most cases IAS 19 and the Capped Asset Return approach would measure the pension obligation based on the higher of the minimum guaranteed return and the expected return on plan assets.
- The Fair Value Based approach and the Fulfilment Value approach would reflect the value of the right to receive the higher of the two returns.

The Fair Value Based approach and the Fulfilment Value approach provide better information on the right to receive the higher of the return on plan assets and the minimum guaranteed return.

Assessment of approaches discussed

Comparability (1/2)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
Can requirements be applied retrospectively?	N/A	★★★	★★	★★

- Financial information is most useful when it can be compared between entities and with past financial information of the same entity.
- The information needed for calculating the pension obligation in accordance with the Capped Asset Return approach should in principle have been collected for the IAS 19 calculations and therefore it would be possible to apply the Capped Asset Return approach retrospectively.
- It may be difficult to apply the Fair Value Based approach and the Fulfilment Value approach retrospectively unless a sufficient time gap between the finalisation of new requirements and the effective date is introduced that would allow entities to collect the data used for presenting comparative under the new requirements.

Assessment of approaches discussed

Comparability (2/2)

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
Is the obligation element related to the minimum guaranteed return accounted for similarly to plans under IAS 19?	N/A	★★★	★	★
Is the obligation related to the return on plan assets accounted for similarly to plans under IAS 19?	N/A	★	★★★	★★★

- When the minimum guaranteed return is high, i.e. the obligation is de facto be determined based on the minimum guaranteed return, the Capped Asset Return approach would result in similar information as if the requirements for defined benefit plans in IAS 19 had been applied.
- When the minimum guaranteed return is low, i.e. the pension obligation is determined based on the expected return on plan assets, the Fair Value Based approach and the Fulfilment Value approach would result in an outcome similar to the requirements for defined contribution plans in IAS 19.

Assessment of approaches discussed

Understandability

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
Is the information understandable?	★	★	★★	★★

– Information is understandable when it is easy to explain what the resulting figures represent.

The figures resulting from the Fair Value Based approach (par. 5.22) and the Fulfilment Value approach (5.21) are assessed to be relatively easy to explain. Do you agree?

Assessment of approaches discussed

Implementation costs

QUALITATIVE CHARACTERISTICS	IAS 19	CAPPED ASSET RETURN APPROACH	FAIR VALUE BASED APPROACH	FULFILMENT VALUE APPROACH
Will the implementation of the approach be uncostly?	N/A	★★	★	★

- The three approaches may all be as costly or costlier to apply than the requirements in IAS 19 for defined benefits obligations.
- As the Capped Asset Return approach would be quite similar to the current IAS 19 requirements, it could be expected that this approach will be significantly less costly to implement.

Do you agree? Please consider question 3!

Agenda

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1.	Previous discussions and projects in the field of pension accounting (context information)
2.	Assessment of approaches discussed (chapter 5 of the DP)
3.	ASCG activities: next steps

ASCG activities: next steps

Questions to constituents (1/2)

Q 1 — **Scope** The DP addresses only those pension plans that have an asset-return based promise and hold the assets upon which the benefits are dependent. Do you think that the approaches could also be applied to those plans with an asset-return promise, where the plan does not hold the reference assets.

Q 2 — **Assessments of approaches – aspects to consider** Do you agree with the aspects of qualitative characteristics considered in the assessment of the various approaches in Chapter 5? If not, which aspects do you think should/should not have been considered? Do you agree with the assessments of the various approaches made in Chapter 5?

Q 3 — **Assessment of approaches – assessment of complexity** The assessment in Chapter 5 of the costs related to the various approaches presented in this DP, only considers implementation costs. Do you think that the complexity related to preparing financial information in accordance with the approaches would differ significantly? If yes, which approaches would be the most complex and least complex to apply?

Q 4 — **Choice of approach** Which of the three alternative approaches, presented in this DP, do you support? How should it be further developed?

Questions relating to policy issues
Questions relating to assessment of the approaches (chapter 5)
Questions relating to specific issues

ASCG activities: next steps

Questions to constituents (2/2)

Q 5 — **Presentation of remeasurements** The DP assumes that the remeasurements under the Fair Value Based approach and the Fulfilment Value approach are presented in profit or loss. Do you agree with this approach? If not, how would you present components of defined benefit costs other than service costs?

Q 6 — **Risk adjustment** As stated in paragraphs 4.56 to 4.57, this DP proposes that a risk adjustment for non-financial risks is made when discounting the pension obligation under the Fulfilment Value approach. Do you agree? Which risk do you consider such an adjustment should cover?

Q 7 — **Disclosure** Do you think that additional disclosure requirements about pension plans, included in the scope of this DP, should be added to the requirements of IAS 19?

Q 8 — **Alternative approaches** Do you think there are other approaches to account for the pension plans within the scope of this DP that should have been considered? If so, which approaches?

ASCG activities: next steps

Timetable

1. **74. IFRS-FA Sitzung 25.-26.4.**
   - Educational session
2. **75. IFRS-FA Sitzung 13.-14.6**
   - Assessment of the approaches
   - Planning of the following ASCG activities (incl. working group)
3. **76. IFRS-FA Sitzung 15.-16.7.**
   - ...
4. **77. IFRS-FA Sitzung 5.-6.9**
   - ...
5. **78. IFRS-FA Sitzung 24.-25.10**
   - ...

Comment deadline 15 November 2019