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International Accounting Standards Board
30 Cannon Street
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Dear Sirs

DISCUSSION PAPER Preliminary Views on Amendments to IAS 19 Employee Benefits

We are grateful for the opportunity to respond to the above discussion paper.

We can understand the IASB's desire to address a number of concerns over the current accounting under IAS 19 and to achieve solutions in advance of a larger project to undertake a total review of the accounting for employee benefits. We acknowledge, for example, the inconsistency that arises from the differences in measurement of financial instruments falling under the scope of IAS 39 and of similar instruments providing post retirement benefits under IAS 19.

However, we have major concerns that the current proposals would result in changes in the accounting for certain types of arrangement that appear better suited to examination in the longer term project.

Our major concern is that the discussion paper proposes that the status of certain promises would change from being accounted for as liabilities arising in defined benefit plans to liabilities arising from contribution-based promises introducing inconsistency of measurement and presentation for economically similar liabilities.

In addition, we are concerned that the paper proposes changes in the presentation of gains and losses arising from post retirement benefits, which should be considered in parallel with the IASB's project on the presentation of financial statements.

We attach our responses to the questions on which comments were invited but set out below our main concerns on the paper.

Scope of changes proposed

We understand the IASB's desire to make improvements to existing standards where limited shortcomings are identified. We accept that the abolition of the corridor approach and of the deferral of actuarial gains and losses are relatively straightforward changes, which would improve the accounting by ensuring full recognition of the assets and liabilities arising under post retirement schemes in all entities.

We are however concerned with the alternative proposals for reporting the changes in post retirement liabilities in the performance statements. The paper proposes some fundamental changes in presentation that cannot be dealt with in isolation and which should be considered in the broader project on the presentation of financial statements. We believe that the IASB should address the presentation of actuarial gains and losses in this wider project, which should itself, provide a framework for distinguishing the nature of all gains and losses and ensure that gains and losses are accounted for according to this framework. We consider it premature to propose any changes to the presentation of actuarial gains and losses before this preliminary work is completed.

We disagree with the changes that would arise from the change in status of certain post retirement benefits. In particular we do not agree with the proposals to change the status of certain promises currently accounted for in defined benefit plans to being considered as contribution-based promises. We believe that these changes would produce further inconsistencies in accounting (rather than removing inconsistencies) and that the concepts are too important to be addressed in this interim review. We discuss this issue further in the next section.

Redefinition of certain arrangements as contribution-based promises

We understand that one of the objectives of the proposals to redefine certain types of arrangements, as contribution-based promises, is to ensure that there is a higher level of consistency between instruments that are measured under IAS 19 and similar liabilities measured under IAS 39. We have some sympathy with this objective.

However, the definitions as currently presented, would result in very different, and perverse, accounting for certain types of pension arrangement.

By way of example, it is proposed that salary related annuities provided on retirement, which are based upon the salary earned in each period of service (a "career average" scheme, would be accounted for as contribution-based promises. However, a scheme providing a similar benefit of a salary related annuity based on (say) final salary would be accounted under the rules governing defined benefit promises. For these two types of promise to be accounted for differently is inappropriate.

We believe that the proposed change for these arrangements would create inconsistencies in (rather than converge) accounting for similar transactions. To us, this outcome appears wrong and inconsistent with the principles set out in the IASB's own Framework for the Preparation and Presentation of Financial Statements. Therefore, we believe that this aspect of the proposals needs to be reassessed.

We believe that the IASB should avoid making the changes in an interim standard or else redefine the contribution promise to limit the change to those where a change is more appropriate.

Presentation of gains and losses arising from defined benefit promises

As expressed previously, we do not believe that the presentation of actuarial gains and losses should be addressed within this stage of the project. More specifically, we believe that the IASB's project on Presentation of Financial Statements should be looking at the principles to be applied to the presentation of gains and losses generally and, consequently, at the application of those principles within existing standards.

Focusing on the IASB's proposals on revising the presentation of actuarial gains and losses, we have grave concerns over the reaction of employers to changes, which could introduce extreme volatility into the published earnings of reporting entities. There is a very real danger that the accounting presentation will result directly in the further erosion of retirement benefits provided to employees, which will have adverse social consequences.

We urge the IASB to reconsider making any changes to the presentation of actuarial gains and losses at this stage.

Presentation of gains and losses arising from contribution-based promises

As discussed above, we would advocate a re-examination of the scope of the definition of contribution-based promises to ensure that similar promises are accounted for in a consistent manner. The IASB should ensure that the actuarial gains and losses arising on assets and liabilities relating to contribution-based promises are accounted for on a consistent basis with those arising from defined benefit promises.

There is a particular issue in respect of investment return on assets backing contribution-based promises in that the current proposals include the requirement that the whole of the asset return is recognised in the income statement. In the case of a pension fund containing liabilities arising from both defined benefit promises and from contribution-based promises there would be a requirement to attribute the assets within the fund if a different presentation requirement exists for the two types of liability

Any such bifurcation is likely to be spurious where the assets and liabilities are managed in aggregate. This is likely to be the case where the liabilities are of similar expected duration and are exposed, in substance, to the same risks. This would occur if, as discussed above, an artificial economic distinction were made between the types of contribution-based promises and the defined benefit promises. .

We trust that you will find our response of assistance in your ongoing project to refine IAS 19, but if you would like further information, please do not hesitate to contact me.

Yours faithfully

D.R Logan
Director, Group Technical Accounting

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RSA Insurance Group

DISCUSSION PAPER: Preliminary Views on Amendments to IAS 19 Employee Benefits – responses to questions on which comments were invited

Question 1
Given the objective of the IASB project to address specific issues in a limited time frame, are there additional issues which you think should be addressed by the Board as part of this project? If so, why do you regard these issues as a matter of priority?

As described in our covering letter, we do not believe that the IASB should be making substantial changes to the existing standard at this time and we therefore would not support an increase in the scope of the project.

If the IASB considers it necessary to make changes now, with a fundamental review of IAS 19 to follow as a separate project, then it should ensure that the changes made at this interim phase are highly focussed and in particular should not introduce inconsistencies in accounting for liabilities that are economically the same. We do not believe that the current proposals within the discussion paper achieve this objective as explained below.

Question 2
Are there factors that the Board has not considered in arriving at its preliminary views? If so, what are those factors? Do those factors provide sufficient reason for the Board to reconsider its preliminary views? If so, why?

We have followed the discussions held by the IASB, and previously by IFRIC, and can appreciate the overall objectives that the Board is attempting to achieve at this interim review.

However, we would ask the IASB to reconsider whether the introduction of different bases for the valuation of liabilities that are economically identical is appropriate. By way of example, we believe that the current proposals to exclude certain types of salary based schemes (namely certain career average salary based schemes) from the definition of defined benefit schemes, will result in a different measurement basis being applied to individual cohorts of liabilities which economically are the same. This outcome is acknowledged in the discussion paper in paragraph 8.8

In the UK, a number of companies have revised the pension arrangements of its current employees to move from a final salary based scheme to a modified career-average salary based arrangement providing a formula-based fixed annual pension. The consequence of this change may be that the liabilities accrued during an individual's career would be measured as a defined benefit promise prior to the change and the liabilities accrued after the change would be measured as a contribution-based promise.

We are unclear whether the Board has considered the practical implications of a situation such as that described above. The liabilities relating to the period that members were earning benefits on the former basis would be valued as deferred pensions arising from a defined benefit promise and the liabilities arising on benefits earned after the change would be valued on the revised basis as contribution-based promises.

It is unclear whether the Board has considered the practical issue of making an arbitrary split of the asset base of a pension fund that provides benefits based on each of the promise types. This may be necessary if the accounting for the return on the assets differs according to the underlying promise. It

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would therefore arise in two of the three alternatives on the accounting for the investment return on assets backing liabilities arising from defined benefit promises. The assets in such funds are unlikely to be accounted for separately since the liabilities would be viewed as economically the same (as deferred annuity promises). Any attribution would therefore be artificial.

Question 3

(a) Which [alternative] approach to the presentation of changes in defined benefit costs provides the most useful information to users of financial statements? Why?

(b) In assessing the usefulness of information to users, what importance do you attach to each of the following factors, and why:

(i) presentation of some components of defined benefit cost in other comprehensive income; and

(ii) disaggregation of information about fair value?

(c) What would be the difficulties in applying each of the presentation approaches?

We do not support making any change to the presentation of defined benefits costs at this time. There is uncertainty surrounding performance measurement with the IASB's current project on financial statement presentation and therefore we believe that any amendments to the presentation of gains and losses recognised in respect of retirement should be addressed in this project.

We acknowledge that with disclosures, users can make individual assessments of the impact of the retirement schemes that are appropriate to their individual needs, but we do not accept that the recognition of all gains and losses arising from such arrangements in the income statement will be the most useful prime presentation. Any of the other choices proposed could further cloud the issue since (as previously mentioned) the paper currently proposes that gains and losses arising from similar arrangements (e.g. certain career average schemes) are all recognised in the income statement. We would therefore strongly urge IASB to review its current position on the gains and losses arising on contribution-based promises to ensure that inconsistencies do not arise.

We believe that the current basis of presentation, whilst having some shortcomings, avoids the excessive volatility in the income statement that could dominate the results of entities with exposures to retirement benefit schemes. We share the concern that the introduction of extreme volatility will have severe social consequences on the willingness of employers to continue with such retirement arrangements.

The discussion paper focuses upon the treatment of the potential volatility arising from economic variables (discount rate and investment returns). We also believe that there may be an economic link to another actuarial assumption (namely the inflation assumption). We accept that the link may not be as observable as the items previously mentioned, but we would have grave concerns if the impact of changes in these assumptions were presented in a different financial statement from the impact of the economic assumptions. We would therefore reiterate our preference that no changes are made to the basis of recognition of actuarial gains and losses at this stage.

Question 4

(a) How could the Board improve the approaches discussed in this paper to provide more useful information to users of financial statements?

(b) Please explain any alternative approach to presentation that provides more useful information to users of financial statements. In what way does your approach provide more useful information to users of financial statements?

As explained in our response to the previous question, in our view any changes to the treatment of gains and losses arising from defined benefit arrangements should be deferred until the project on financial statements presentation is concluded and hence we have no further comments on this issue.

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Question 5
Do you agree that the Board has identified the appropriate promises to be addressed in the scope of this project? If not, which promises should be included or excluded from the scope of the project, and why?

As previously stated we cannot agree with the distinction made between final salary based promises and career average based promises where each is providing a promise of a formula–based and fixed value annuity on payout. Whilst we can understand the process for the classification of the latter, we believe that the ramifications for the distinction (in particular the subsequent accounting impacts) are perverse.

In the case of a career average based promise of the type described above the liability that emerges from the arrangement is an insurance liability in the form of an annuity. It appears inconsistent to treat an annuity liability arising from a final salary arrangement in a different manner from an identical liability arising under a career average arrangement. Indeed this conflict is contrary to paragraph 39 of the IASB's own framework for the Preparation and Presentation of Financial Statements.

On a related point, we are unable to understand the rationale for making the distinction discussed above whilst retaining post-employment life insurance promises and post-employment medical care promises within the scope of defined benefit arrangements. We were unable to find any reason for retaining these insurance type promises within the same category as final salary based promises with a different treatment for other benefits that are insurance related. This does not appear to be justifiable.

Question 6
Would many promises be reclassified from defined benefit to contribution-based under the Board's proposals? What are the practical difficulties, if any, facing entities affected by these proposals?

We are unable to comment upon the impact on the proposals on post retirement arrangements outside of our own Group and hence leave it to others to respond on this point.

We have already addressed in our response to question two a couple of practical issues; namely the point of classification where a scheme arrangement changes during the service period of an employee and the attribution of assets within a composite scheme.

A further problem with the current proposals is the requirement to measure a contribution-based promise at fair value. In the case of a promise that provides benefits in the form of an annuity, there is no agreed basis under IFRS for valuing such liabilities as insurance contracts. We believe that it would be inappropriate for the IASB to introduce a measurement basis that may be inconsistent with the measurement basis that emerges on insurance contracts. Equally, we believe that it would be wrong to have, potentially, to make a further change to align the valuation of such post retirement liabilities with insurance contracts upon completion of the second phase of the insurance contracts standard.

Question 7
Do the proposals achieve that goal [of not significantly changing the accounting for plans currently classified as defined contribution plans]? If not, why not?

We are again only able to comment upon the schemes that we have within our Group, but we have not identified any issues within our Group that would cause problems for the accounting for plans currently classified as defined contribution plans.

Question 8
Do you have any comments on those preliminary views [relating to recognition of contribution-based promises]? If so, what are they?

We concur with the preliminary views as presented.

Question 9
(a) Are there alternative measurement approaches that better meet the measurement objectives described in this paper? Please describe the approaches and explain how they better meet the measurement objectives.
(b) To what extent should the effect of risk be included as a component of the measurement approach at this stage of the Board's post-employment benefit promises project? How should this be done?

As described in our earlier responses to questions, we do not agree with the different measurement bases that are currently proposed for liabilities arising from defined benefit promises and for similar (or identical) liabilities arising from some contribution-based promises. We can understand that the IASB has concerns over the measurement bases applied to those contribution-based promises that would be measured on a different basis if they were included in the accounts under IAS39 rather than IAS19. However, we have concerns over applying the revised measurement basis to liabilities that would meet the definition of insurance contract liabilities if treated on a standalone basis.

For this category of liabilities, we recommend that the IASB should retain the existing methodology and address the measurement issues again when the accounting for retirement benefits is reviewed in its entirety.

Similarly, we believe that the inclusion of risk within the measurement of such liabilities should be addressed in Phase II of the project.

Question 10
(a) Do you agree that the liability for benefits in the payout and deferment phases should be measured in the same way as they are in the accumulation phase? If not, why?
(b) What are the practical difficulties, if any, of measuring the liability for a contribution-based promise during the payout phase at fair value assuming the terms of the benefit promise do not change?

We agree with this conclusion for the reasons given previously, namely that any other methodology would appear to breach the IASB framework that requires "*the measurement and display of the financial effect of like transactions and other events must be carried out in a consistent way throughout an entity*". Our concern is rather that this principle may not be consistently applied across the defined benefit promise / contribution-based promise divide.

We do not believe that it would be right to impose fair valuation on insurance risk promises before the IASB has concluded its deliberations on the valuation attributes that should be applied to insurance contracts. Imposing such a requirement could result in the need for further change as measurement of insurance contracts is developed.

Question 11
(a) What level of disaggregation of information about changes in the liability for contribution-based promises is useful to users of financial statements? Why?
(b) Do you agree that it is difficult to disaggregate changes in the contribution-based promise liability into components similar to those required for defined benefit promises? If not, why not?

We agree with the IASB's conclusions on these issues, as there are potentially very different risk factors within promises falling within the proposed scope of contribution-based promises. We believe that any revised disclosure requirements should build upon the principles established under IFRS 7, aligning such disclosures with the factors that are used internally for assessing the reporting entity's risk exposures. This would capture the entity specific risks of the promises made.

Question 12
Should changes in the liability for contribution-based promises:
(a) be presented in profit or loss, along with all changes in the value of any plan assets; or
(b) mirror the presentation of changes in the liability for defined benefit promises?
Why?

As previously discussed, we do not agree with a presentation for changes in liabilities for contribution-based promises, which differs from the basis of presentation of changes in similar liabilities for defined benefit promises. Similarly, we do not believe that the presentation of the related assets on different bases according to the underlying liabilities can be justified.

Question 13
(a) What are the practical difficulties, if any, in identifying and measuring the 'higher of' option that an entity recognizes separately from a host defined benefit promise?
(b) Do you have any other comments on the proposals for benefit promises with a 'higher of' option? If so, what are they?

We have no comments to make on this issue.

Question 14
What disclosures should the Board consider as part of that review [the intended review of disclosures in a later stage of this project]?

We have no additional comments on disclosures.

Question 15
Do you have any other comments on this paper? If so, what are they?

We note that benefit promises with more than one outcome are beyond the scope of the project (paragraph 5.60). We believe that there will be a number of types of scheme for which this situation may arise in practice if the IASB continues with its current proposals.

The example that the IASB provides in paragraph 5.60 (namely a contribution-based promise if the member survives and a defined benefit promise, in the form of a widows pension, if the member dies in service) will arise in practice in some schemes. Currently this is unlikely to be an issue, where both outcomes are accounted for within a defined benefit plan.

We believe that where the IASB introduces a new issue as a direct result of the proposed changes to the existing standard, it is inappropriate to dismiss the resulting problem as beyond the scope of the project.