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International Accounting Standards
Board (IASB)
Project Managers IAS 19
30 Cannon Street
London
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Zurich, 22 September 2008

Discussion Paper
Preliminary Views on Amendments to IAS 19 Employee Benefits

Dear Project Managers,

The Swiss Institute of Certified Accountants and Tax Consultants (the "Institute") appreciates the opportunity to submit comments on the Discussion Paper Preliminary Views on Amendments to IAS 19 Employee Benefits (the "DP").

The Institute is the professional body that represents, among others, the Swiss accounting profession.

The Institute welcomes the publication of a DP to improve IAS 19. IAS 19 is indeed the standard that causes the most issues and discussions between the accounting profession and the preparers of financial statements in Switzerland. In Switzerland, all employers are required by law to provide pension, death in service and disability benefits. Because of inherent guarantees under the law, virtually all Swiss pension plans are classified as defined benefit plans under the current version of IAS 19. The significance of the Swiss pension system is also reflected by the amount of pension assets which amount to approximately CHF 700 billion; an amount that is significant not only to the Swiss economy as a whole, but significant compared to other European countries.

The Institute supports any improvement to IAS 19 which makes the standard more relevant for Swiss pension plans and which help users and preparers to better understand the requirements of the standard. Although we recognize that the DP attempts to address some of the key concerns of IAS 19, we do have some major issues as discussed in Appendix 1. In summary, we are reluctant to support this project unless the following major issues are addressed:

- The DP does not consider promises where the risks are shared between the employer and the employee but rather assumes that the employer is fully responsible for all risks. This seems to be UK/US biased and does not consider pension models in many other countries including Switzerland which use a shared risk model (see comment to question 1).
- Clarification of the consequences if "more than one outcome" is possible according to the benefit schedule. If the conclusion will be that plans which cover also the risks of death in service, disability and other benefits would still fall under the defined benefit category, then the Institute sees no merit in continuing with that project (see comment to question 5).
- The Institute is also concerned about the potential complexity of measurement of contribution-based promises under these proposals and would welcome some clarification with respect to the Boards' intentions regarding the measurement of such promises. The Institute also strongly believes that the entity's own credit risk should not be taken into account in the measurement of such promises (see comment to question 9).

Our detailed comments are given in Appendix 1. We further include in Appendix 2 a brief description of the Swiss pension system, which may help to better understand some of the key concerns we express in this letter.

If you have any questions concerning our comments, please contact either Matthias Jeger (matthias.jeger@ch.pwc.com) or Martin Welser (mwelser@deloitte.ch).

Yours sincerely

Matthias Jeger

Thorsten Kleibold

Appendix 1
Comments to the Discussion Paper

Chapter 1 Introduction

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?

In the view of the Institute, there is one important issue which should be addressed as a matter of priority:

The DP does not consider promises where the risks are shared between the employer and the employee. One of the characteristics of Swiss pension plans is the sharing of risk. Risks are shared based on the relative contribution of employers and employees. The law stipulates that the employer must pay at least 50% of the contribution. This, together with other provisions in the law, indicates that the employee will share at least some of the risks during the accumulation phase of the plan (see further details in Appendix 2). There are a variety of different funding solutions starting from strictly applying the minimum financing requirement (50:50) up to the employer assuming the full liability. On average, Swiss employers pay 57% of the contribution (as per pension plan statistics 2006). The basic assumption that the employer has a constructive obligation for the all risk in the structure is vehemently refuted by some of the employers and preparers. Entities that take this view are not willing to recognize 100% of the net pension liability or asset. Those companies claim that in case of a shortfall of a pension plan, the employees will have to share the shortfall either by reduced benefits or making additional contributions. The question is further complicated by the fact that the Swiss pension law sets limits with respect to minimum benefits, although any benefits in excess of the legal minimum may be reduced at least in the accumulation phase. Most pension plans provide benefits in excess of the legal minimum.

Another element of shared risk is that there is no mandatory indexation of benefits (except for death-in –service and disability benefits) as seen in some other countries. Indexation of pension payments is a discretionary decision by the Board of Trustees and depends on, amongst other considerations, upon the financial situation of the pension plan in accordance with Swiss law.

Chapter 2 – Deferred recognition of changes in the liability for defined benefit promises

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?

In principle, the Institute supports the DP's proposal to recognise all changes in the value of plan assets and post-employment benefit obligations in the financial statements in the period in which they occur, i.e. removal of the optional "corridor" deferral method for actuarial gains and losses. However, we are concerned that this would be dealt with in a short-term project, before the IASB has finalised its financial statement presentation project. We believe the removal of the “corridor” method should rather be incorporated in a comprehensive project.

Chapter 3 – Presentation approaches for defined benefit promises

Question 3
(a) Which 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?

The Institute clearly does not support suggested approach 3. As the Board states in the DP, it will be difficult to distinguish interest income on plan assets from other changes in the value of plan assets. This approach is not only difficult to apply, but it may also lead to controversial (and unproductive) discussions between preparers and their auditors.

Approaches 1 and 2 would both be acceptable for the Institute. There are certainly good arguments for both approaches. Approach 1 is simple and straight forward. However, the Institute shares the concerns of other constituents who claim that the volatility of income due to changes in the fair value of pension assets and liabilities makes the financial statements less useful for users. The Institute therefore believes that should Approach 1 shall be chosen, the Board needs to consider how these concerns can be addressed. Such considerations could also include the question whether fair value measurement is the appropriate measurement attribute for long term pension obligations.

The Institute also sees merits in approach 2. However, we believe the IASB should consider whether it is appropriate that the funding situation of a plan does not affect pension expense.

Finally, the Institute wonders whether it is wise to discuss these presentation approaches while at the same time the Boards have a long-term project on Financial Statement Presentation that will develop a new approach on the presentation of gains and losses in the performance statement. The Institute believes it would be preferable to defer this discussion to a later phase of amendments to IAS 19. The methods currently allowed (in short: recognition of actuarial gains and losses in either profit or loss or in the statement of comprehensive income) could be maintained over the next years until new Financial Statement Presentation standards are available.

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 discussed above, the Institute believes that the Board should consider deferring the issue of presentation approaches to a later phase of the project. Two of the methods currently allowed could continue to be used until the finalisation of the long term project to pension accounting.

Chapters 4 and 5 – Introduction to contribution-based promises and definitions

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?

The Institute acknowledges the efforts the Board has made to identify a variety of promises that fall under this category. However, the Institute believes that the DP does not clearly define contribution-based promises. The Institute is therefore not sure whether typical Swiss pension schemes would fall under this category, although it is believed this was the intention of the DP.

Most Swiss pension plans are contribution-based, but because of inherent legal guarantees, have to be classified as defined benefit plan under the current standard. These plans usually have a fixed return and fixed annuity rate – i.e. a combination of the examples "promise 5" and "promise 12" in the DP. Please refer also to the general description of Swiss pension plans in Appendix 2.

However, the Institute believes that the Board might have underestimated the complexities of such plans and that, for various reasons, the typical Swiss pension plan would still have to be classified as a defined benefit promise. The Institute is particularly concerned about paragraph 5.60 of the DP ("Benefit promises with more than one outcome") which states that the DP does not discuss the accounting treatment of an employee's option to receive different benefits for different events. A promise of a Swiss pension plan ordinarily (and as required by law) includes various promises, including old age pension (or lump-sum payment), death in service (widow and orphans pensions), disability, payment of pension contributions in case of disability, and other promises. If based on any of these risk-based promises Swiss pension plans would continue to be classified as benefit promises as under the current standard, the Institute would discourage the Board from continuing with the project. The Institute acknowledges the difficulties inherent in including such promises in a short term project. However, the Institute suggests that further research be done to determine whether it is possible and practicable to separate these "risk-based" promises from "contribution-based" promises.

In cases where the entity has full insurance coverage against these risks, the Institute believes that the appropriate treatment of the cost for the insurance would be to expense when premiums are due, because the entity does not have any (legal) liability other than to pay the insurance premium. In cases where the entity is assuming the risk of death-in-service, disability and other, the Board should propose a solution that does not automatically relegate such plans to the category of defined benefit. Since in such cases, the entity effectively writes an insurance policy, the Board might consider the results of phase 2 of the insurance project for the measurement of such "risk-based" promises.

The Institute therefore encourages the Board to look closely at risk benefits and to examine whether such benefits constitute a separate component of a pension promise for which guidance on recognition and measurement is required.

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 refer to our response to question 5. We believe that, based on the pension commitment alone, a majority of the Swiss pension plans would be reclassified from defined benefit to contribution-based promises. However, the uncertainties around the other promises included in the same plan (e.g., death-in-service and disability) may preclude such a reclassification.

Question 7
Do the proposals achieve that goal? If not, why not?

No comment. (Question relates to continuing treatment of defined contribution plans under the current standard. Such plans are extremely rare in Switzerland).

Chapter 6 Recognition issues relating to contribution-based promises

Question 8
The Board's preliminary views are summarised in paragraphs PV9-PV11. Do you have any comments on those preliminary views? If so, what are they?

The Institute agrees with the Board's preliminary views, particularly the fact that for contribution-based promises, higher benefits earned in later periods should not affect accounting (PV 10). This is the case for many Swiss pension plans (due to legal requirements which stipulate minimum benefits based on age as well as contributions that increase with age) and one of the reasons why applying defined benefit accounting for Swiss contribution-based plans leads to unsatisfactory results.

The other two preliminary views (PV 9 and 11) are less relevant in the Swiss environment.

Chapter 7 Measurement of contribution-based promises

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?

The Institute acknowledges the difficulties of arriving at a sound measurement concept for contribution-based promises that cover all possible pension arrangements.

However, from the perspective of a contribution-based Swiss pension plan, the measurement concept the Board proposes appears far too complicated. In case of a Swiss contribution-based plan, the amount due to the employee is known at any point in time (it is the amount that would be transferred to the new pension plan when an employee leaves the company). It would be difficult to explain to the constituents why entities have to measure the amounts due to the employee at something other than the cash balance due to the employee.

There is however the issue of the inherent guarantees in the pension promise (interest rate guarantee and fixed annuity rate for legal minimum benefits) which needs to be recognized. Although there is currently little experience with measuring such long term guarantees at fair value, the Institute believes that the difficulties of measuring such guaranties could be overcome through practical experience.

Consequently, the Institute does not share the Board's view that the unit of account in case of contribution-based promise shall be the contribution amount and the promised return taken together. The consequences of the Board's conclusion could be the following (using the example in paragraph 7.5 of the DP): The promised "lump sum" of CU 1,000 (in the Swiss environment: the cash balance?) plus the expected interest guarantee (as defined by the government) of say 2.5% shall be discounted at a rate of 4%. This will lead to a "fair value" of less than CU 1,000 and therefore less than the cash balance (that would be transferred to the employees' subsequent pension plan in case of termination of employment). Such a result would not only be counter-intuitive, but – in the Institute's view, wrong.

The Institute believes that the Board has not sufficiently explained why it believes that a different measurement base to the contribution amount and the promised return would be wrong or why it could provide opportunities for accounting arbitrage (paragraph 7.6). The Institute believes that the opposite is true, as above example shows. The Institute is, however, unsure of the meaning of "contribution amount" and whether this includes contributions made (part of the cash balance) or the contributions projected until retirement. If the latter is the case, the Institute cannot see any improvement to the current method of defined benefit accounting, other than the fact that future salary increases would not be relevant for contribution-based promises.

Further, it appears that the Board believes that the entity's own credit risk should be considered in the measurement of contribution-based promises. The DP does not discuss how this shall be understood if the promise is fully funded and the assets are held by a separate pension fund. We assume that in such a case, the pension fund's credit risk rather than that of the employer is relevant for a fair value measurement. The Institute also strongly believes that the credit risk (neither that of the pension fund nor that of the employer) should not be reflected in the fair value measurement. The Institute believes that measuring own credit risk or even any requirement to disclose such information is onerous and not useful to users of financial statements. Finally, as the DP does not address changes to the measurement of benefit defined promises, it appears that only contribution-based promises would require the inclusion of credit risk. There is no conceptual basis on which to justify such different approaches between benefit defined and contribution-based promises.

If the Board continues deliberating this measurement approach as suggested in the DP, the Institute is concerned that the project merely replaces a complex, inadequate measurement approach for contribution-based promises by another complex and even less adequate measurement approach.

Chapter 8 Measurement of benefits after the accumulation phase

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?

As discussed under question 9, the Institute does not agree to the measurement principles for contribution-based promises during the accumulation phase as laid out in the DP.

The Institute believes that it would be inadequate to measure the benefits after the accumulation phase differently depending on classification of the plan (benefit versus contribution-based). Therefore, the Institute's answer to question 10(a) is no.

The problem arises because the DP suggests to measure contribution-based promises differently from benefit defined promises. The Institute agrees with the Board's view that the current accounting for defined benefit promises should not be changed at this stage. The consequence of this should be, in our view, to align the measurement principles of contribution-based promises to current measurement principles of benefit defined promises for benefits after the accumulation phase.

Chapter 9 Disaggregation, presentation and disclosure of contribution-based promises

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?

This question is linked to question 9. The Board's conclusions are coherent if the measurement approach of chapter 7 is followed.

If, however, the components of the contribution-based promise are to be measured separately (contribution amount or cash balance and promised return) as suggested above, then the logical consequence would be a disaggregation into the value changes of these components.

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 (see Chapter 3)? Why?

The Institute does not have a strong preference in this regard.

Chapter 10 Benefit Promises with a "higher of" option

Question 13
(a) What are the practical difficulties, if any, in identifying and measuring the 'higher of' option that an entity recognises 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?

The Institute has not analysed in detail the impact of this question for Swiss pension plans. It could be relevant for the beneficiary's option to choose between a lump sum, an annuity or a combination thereof at the time of retirement.

Other matters

Question 14
What disclosures should the Board consider as part of that review?

No comments.

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

The short term project could integrate IFRIC 14 into the standard and, at the same time, eliminate the flaws of IFRIC 14. This interpretation has lead to intense debate among Swiss constituents, particularly with respect to paragraph 20 of IFRIC 14 that may lead to counter-intuitive results. Particularly, when future minimum contributions are higher than future service cost, any additional advance contributions made by the employer above the minimum requirements may have to be expensed immediately because IFRIC 14 does not permit recognition as an asset. Such a situation may be used for accounting arbitrage. Pre-IFRIC 14, contribution prepayments[1] were considered as part of plan assets but were measured separately. Swiss entities generally did not recognise pension assets unless there were future benefits available, which was generally acknowledged to be the case for contribution prepayments. Future benefits were considered only available if it was probable that the employer could reduce its contributions below the minimum contribution as stipulated by the pension plan's regulation. IFRIC 14 introduced a new concept, whereby the employer is assumed to have a benefit if the future contribution is below the future service cost. Many Swiss entities have had to restate their accounts against their true belief of what is true and fair.

[1] Contribution prepayments, or so called „employer contribution reserves“, are tax deductible to a certain extent and are therefore usually made for tax planning purposes

Appendix 2
A brief description of the Swiss Pension System

Swiss law requires entities (employers) to provide post-employment benefits, including old-age pension, death-in-service and disability, to virtually all of their employees. Swiss law requires that a pension plan be set up in an entity legally separated from the employer, usually in the form of a foundation.

The law stipulates the minimum benefits. Employers are free to grant improved benefits. The benefits, contributions and other terms of each plan are laid out in the pension fund regulation. Because the law only stipulates minimum benefits, there is a wide range of possible regulations, because employers usually grant improved benefits. The pension law is quite complex, as it regulates management, investment policy, supervision, rights of the employees and many other things.

Contributions to the pension plan are shared by the employer and the employees. The law stipulates that at least 50% of the contributions must be paid by the employer. The pension plans are governed by a Board of Trustees, which must be equally represented by employers and employees.

The contributions normally are determined as a percentage of current salary. Such plans are, under Swiss law, defined as contribution-based. There exist also benefit-based plans, which are however becoming less frequent as they expose the entities to higher risks.

Contributions consist basically of
a) the “age-saving” (which is credited to the individual’s cash balance account). This contribution usually increases with the age of the plan participants (because the minimum contributions stipulated by the law use that model. It is possible, however, to use a flat rate as long as the legal minimum for all age groups is met).
b) risk premiums that cover the risk for death-in-service, disability and other risks.

There may be other elements of the contributions (e.g. admin cost in case the plan is managed by an insurance company.)

All contributions must be transferred by the employer at least annually to the pension plan, i.e. the pension plans are fully funded according to the requirements of Swiss law.

There are three main guarantees written into law:
- a minimum return on the minimum contributions as stipulated by the law (1)
- a minimum conversion rate that converts cumulative contributions (including minimum returns) into an annuity (2)
- a provision that plans need to be fully funded in the medium term and therefore appropriate measures need to be taken to make up any shortfall in the plan (3)

(1) Typically the pension arrangement is run as a cash balance plan whereby each employee has a “savings account” comprising of contributions and minimum return of currently 2.75% p.a.
(2) Upon retirement of an employee, the total amount of his cash balance is converted into an annual pension payment at a minimum rate defined by the law (currently 7.1%

to be applied at least on the legal minimum amount). This means that a cash balance of CHF 100,000 would result in an annuity of CHF 7,100. The conversion rate is fixed by the law and therefore is not based on statistics but on political considerations and could be considered excessive. Therefore, pension funds must set up provision to finance the excessive conversion rate.

(3) If the plan has a significant deficit, the Board of Trustees must take appropriate actions to make good the shortfall in mid-term perspective. The Board of Trustees has, for example, the following alternatives:
   1. Reducing benefits for active employees of the plan but not below regulatory required minimums; and
   2. Requiring increased contributions for both the employer and employees (again, at least 50% must be paid by the employer)

The Entity’s sole legal responsibility relating to the Swiss pension plan is to fund contributions at a level defined in the plan rules and pursuant to Swiss regulatory requirements. However, because of the guarantee that pension funds must be fully funded on a medium term basis, entities may be hit by the requirement to pay additional contributions as described above.

If an employee changes the employer, he or she will get the full amount of the saving account (or cash balance) at that point in time. The amount will be transferred to the pension plan of the new employer.

Classification of Swiss Pension Plans under IAS 19

Because of the guarantees written into the law as described above, Swiss pension plans generally are classified as defined benefit plans under IAS 19. This is true also for fully insured plans. In Switzerland, the term „fully insured“ is applied to pension plans in which the entity/employer has ceded all risks, including demographic risks and investment risks, to an insurance company. In a recent paper, the Institute has concluded that even fully insured plans should be classified as defined benefit plans under the current IAS 19, because the insurance coverage is only temporary and because of the risk benefits inherent in the plans, which result in variable premiums over time.
