E.ON AG · P.O. Box 30 10 51 · 40410 Düsseldorf

International Accounting Standards Board
30 Cannon Street

London EC4M 6XH
United Kingdom

E.ON AG
E.ON-Platz 1
40479 Düsseldorf
Germany
www.eon.com

T +49-2 11-45 79-0
F +49-2 11-45 79-5 01

September 24, 2008

IASB Discussion Paper "Preliminary Views on Amendments to IAS 19 Employee Benefits" issued on March 27, 2008

Dear Project Managers of the post-employment benefits project,

On behalf of E.ON AG we appreciate the opportunity to comment on the IASB's Discussion Paper "Preliminary Views on Amendments to IAS 19 Employee Benefits" issued in March 2008.

E.ON is one of the world's largest investor-owned energy services providers and operates along the entire value chain in power and gas. Our business in about 30 countries is organized as market units in line with the structure of our respective target markets: Central Europe, the United Kingdom, Northern Europe, Southern Europe, Russia and the Midwestern United States. E.ON is a member of the major European stock index Dow Jones Stoxx50 and the German stock index DAX.

Retirement benefits for employees have always been of significant importance within the E.ON Group, as they are a meaningful component of the employees' provision for old age and social security.

As an introductory statement, we would like to point out our guiding principles for this comment.

- Pension Accounting Standards should guarantee that financial statements present an economically true and fair view of an entity's entire post-employment benefit obligations granted to their active employees, vested terminees and retirees.
- Pension Accounting Standards should to the largest possible extent limit their impact on the (country-specific) design of post-employment benefit arrangements, the funding policy and the plan asset management strategy of the respective plan sponsors.

In general, we welcome the IASB's initiative to submit selective changes in the accounting for post-employment benefit arrangements, particularly with regard to an improvement of comparability and comprehensibility of financial statements to its users. We share the Board's opinion that there are limited areas within IAS 19 which have to be reviewed and adjusted by precisely fixed and communicated definitions and approaches.

E.ON carefully reviewed the preliminary views (PV) and discussion provided by the Board and decided not to comment separately on each of the fifteen questions mentioned in the Discussion Paper (DP). Instead, we focus our statement on those issues to which we attach key importance for both users and preparers of financial statements. Our comment is organized according to the Board's structure presented in the Introduction of the Discussion Paper (IN4):

(a) The deferred recognition of some gains and losses arising from defined benefit plans
(b) Presentation of defined benefit liabilities
(c) Accounting for benefits that are based on contributions and a promised return
(d) Accounting for benefit promises with a 'higher of' option.

Comments:

(a) The deferred recognition of some gains and losses arising from defined benefit plans (PV2 to PV4 / Question 2):

We totally agree with the Board's view in the Discussion Paper to abolish the deferred recognition of changes in the value of plan assets and in the post-employment benefit obligation in the balance sheet and thus, to eliminate the corridor-method described in IAS 19.92.

In this context, we also support the IASB's assessment not to allow the recycling approach, as described in item 3.9 of the DP.

- PV2 ("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."):

We think the appropriate way of presenting an economically true and fair view of an entity's post-employment benefit arrangement is the recognition of all actuarial gains and losses in other comprehensive income (OCI) in order to present the net surplus or deficit of benefit obligations and plan assets in the balance sheet. Therefore, we support the Board's view with regard to a full and immediate recognition of all changes in the balance sheet.

However, we strongly disagree with the recognition of all changes in the value of plan assets and post-employment benefit obligation in the income statement (I/S). From a corporate perspective, we can largely follow the arguments supporting the recognition of all changes in the value of plan assets and in the post-employment benefit obligation outside the income statement (see item 2.5 of the DP), although we know the Board came to a different conclusion. In line with other comments, already displayed on the website of the IASB, our paramount concern is the unquestionable argument of short-time volatility. This was adequately described in the 3rd bullet point of item 2.5 of the DP: "The effect of such an accounting methodology would not be useful to users because the volatility associated with the changes in post-employment benefit obligation or plan assets would overwhelm the results and financial position of the business operations." In our opinion, the income statement should enable all users to gain a true and fair view of an entity's operating business. It should not be layered with oscillatory short-term volatility arising from the quantitative assessment of naturally long-term pension obligations. In this context, the extreme volatility in the discount rate recently experienced reinforces our basic concern.

Short-term fluctuations in earnings and particularly in earnings per share will be likely to prompt users of financial statements, like the financial analysts and investors, to adjust earnings related key figures appropriately by eliminating the volatile effects arising from recognition of all changes in the post-employment benefit obligation and the market value of plan assets in the income statement. Therefore, we come to the conclusion that such an accounting approach would not constitute an improvement in financial reporting. In fact, it would create additional work and costs both for the preparers and the users triggered by the need for calculation of pro forma figures with predictive character reflecting the entity's operating business.

We also want to voice our serious concern that, as a consequence of the "all through the profit and loss accounting", investor-oriented companies worldwide could be forced to undertake a series of measures with an aim to reduce the oscillatory short-term income statement volatility, e.g. the closing of current benefit plans for future service of existing staff and/or new entrants or an amendment of the asset management policy. The latter reflects the concern that the new accounting approach could result in a more or less uniform "liability hedging investment strategy" applied by large investor-oriented corporations worldwide in order to control the accounting volatility in the income statement. Due to the insufficient supply and liquidity of appropriate long-term fixed income securities and derivative instruments, we would assume that the effects of this could result in remarkable and by the IASB unintended distortions in different segments of the capital market. This could lead to increasing long-term costs with regard to already existing post-employment benefit plans.

Finally, E.ON would recommend to continue with the approach of recognising all actuarial gains and losses in other comprehensive income (OCI), as is the current practice under IAS 19.93A. This form of recognising actuarial gains and losses of pension assets and pension obligations avoids short-term volatility in the income statement, but notwithstanding, it is highly transparent and provides the required information for the different users of financial statements. Furthermore, it is reasonably neutral with regard to an entity's funding policy and investment strategy. A reflection of the changes in the income statement would offer no additional informational value for professional users of our financial statements. The wide acceptance of the currently practiced approach of recognising all actuarial gains and losses in other comprehensive income (OCI) by both users and preparers of financial statements is a further argument to choose it as the only common approach under IAS 19.

Moreover, against the background of the forthcoming convergence project with the FASB, the IASB fair value accounting considerations and particularly the current revision of the financial statement presentation, the recommended approach could warrant an appropriate uniform and transitional accounting treatment of pension assets and liabilities.

- PV3 ("Entities should not divide the return on assets into an expected return and an actuarial gain or loss."):

We disagree with the Board's PV3, as underlined by the Board's argument mentioned in item 2.15 of the DP: "the Board is concerned that the subjectivity inherent in determining the expected rate of return provides entities with an opportunity to choose a rate with a view to manipulating profit or loss". We cannot share this view of the Board. As our own experience shows, the basic input for the determination of the expected long-term rate of return on plan assets is a sophisticated asset-liability study carried out by external specialist-experts. The whole process of fixing an appropriate best-estimate return expectation comprises several steps of validation and approval by E.ON and by the involved external consultant, the auditor and in some cases the regulator. They all carefully consider and judge the calculated expected rate of return on plan assets. Therefore, E.ON's opinion is that this process combined with a comprehensive documentation reflects sufficient objectivity in estimating the expected rate of return on plan assets.

The approach ("entities divide the return on assets into an expected return and an actuarial gain or loss") currently practiced smoothes the short-term volatility of the value of plan asset in the income statement and, therefore, helps to avoid the aforementioned negative consequences (as described in our comment to PV2) in a consistent manner. Nevertheless, in combination with the approach of recognising all actuarial gains and losses in other comprehensive income, all changes in the market price of assets and in the market-oriented valuation of liabilities are visible in the balance sheet. In the light of a highly desirable symmetric treatment of the periodical fluctuation in the discount rate and unexpected changes in the market value of plan assets, this constitutes a practical and prudently balanced approach. Additionally, improved disclosures (e.g. more information on the determination of the expected rate of return on plan assets) could be considered to provide the users of financial statements with sufficient information to evaluate the appropriateness of the expected rate of return on plan assets.

- PV4 ("Entities should recognise unvested past service cost in the period of a plan amendment."):

Considering PV4 we basically see the same risks of short-term volatility in the income statement. Due to its minor relevance in the accounting practice, we agree with the Board's PV4.

(b) Presentation of defined benefit liabilities (PV5 / Questions 3 and 4):

- PV5 ("The Board does not express a preliminary view on the presentation of the components of post-employment benefit cost in comprehensive income. Instead, the Board outlines three approaches to presentation that illustrate ways in which information about post-employment benefit costs could be presented. The approaches are: […].").

Approach 3 ("remeasurement approach") contains three different ways to estimate interest income on plan assets. In the following, we will call them Approach 3/1 ("using the expected return on plan assets, as currently required by IAS 19"), Approach 3/2 ("using dividends received on equity plan assets and interest earned on debt plan assets") and Approach 3/3 ("using market yields at the reporting date on high quality corporate bonds to input interest income").

As already stated, E.ON would recommend to continue with the approach of recognising all actuarial gains and losses in other comprehensive income (OCI), as currently practiced under IAS 19.93A, due to the aforementioned reasons in paragraph (a).

Nevertheless, we carefully analyzed all presentation approaches discussed by the Board in items 3.17 to 3.32 of the DP. If we had to choose one of the proposed approaches by the Board we would support Approach 3/1. We do not share the Board's concern that "the subjectivity inherent in determining the expected rate of return provides entities with an opportunity to choose a rate with a view to manipulating profit or loss" due to the reasons set forth above (see our comments to PV3.)

We strongly disagree with Approach 1 ("all changes through profit and loss") of the presentation of defined benefit liabilities. As already mentioned, we disagree with any presentation approach which results in full and immediate recognition of all changes in the value of plan assets and post-employment benefit obligation in the income statement. For the major arguments, underlining our view, see our comments in paragraph (a), especially the statement to PV2 of the DP.

We also disagree with Approach 2 ("entity presents the costs of service in profit and loss and all other costs in other comprehensive income"). Approach 2 completely ignores the fundamental economic difference between a funded and an unfunded pension obligation due to the non-consideration of interest cost on the pension obligations and (expected) return on the corresponding plan assets in profit and loss. Furthermore, it is inconsistent with the recognition of the return on financial assets not classified as plan assets. While return on plan assets would not be recognised in the income statement but in other comprehensive income, return on financial non-plan assets is included in the income statement. This inconsistency would set a substantial incentive for an entity's pension funding policy, as it penalizes the funding of pension liabilities. However, due to the resulting unsatisfactory comparability of financial statements we would assume that the users of financial statements would react rationally and adjust the figures for this effect. Finally, with respect to the interest cost on the pension obligation Approach 2 would be inconsistent with the accounting of long-term provisions and liabilities according to IAS 37.46 and 37.60 ("this increase is recognised as borrowing cost").

From our point of view, Approach 3/2 ("using dividends received on equity plan assets and interest earned on debt plan assets") is not acceptable either. It provides less useful information, as (un)realized capital gains and losses, which could represent a main part of the return on plan assets, would not be recognised in profit and loss. Additionally, it is foreseeable that this approach would seriously bias the asset management strategy towards investments in coupon/dividend-bearing assets and penalize investments in small cap or growth stocks, property and alternative investments. Furthermore, entities with quarterly reporting frequency would be exposed to significant seasonality in the plan asset returns due to the well-known seasonality in dividend/coupon payments to security-holders.

In our view, Approach 3/3 ("using market yields at the reporting date on high quality corporate bonds to input interest income") is a simple, pragmatic and in no way inconsistent approach of treating interest costs on pension obligations and interest income on plan assets in a symmetric manner. However, it does not consider the individual asset management strategy of a plan sponsor and thus, it does not present an entity-specific and realistic picture of the (expected) return on plan assets. Compared to Approach 3/1, the information provided by Approach 3/3 is less useful for the users of financial statements. Consequently, we prefer Approach 3/1 over 3/3.

(c) Accounting for benefits that are based on contributions and a promised return (PV6 to PV15 / Question 5 to 12):

- PV6 to PV8, PV12: In item 5.3 of the DP the Board provides preliminary views on the new categorization of post-employment benefit arrangements including new definitions for defined benefit promises as well as for contribution-based promises (PV6 to PV8). Item 7.2 of the DP expresses the Board's preliminary view on the measurement of liabilities for contribution-based promises using the intended measurement attribute "Fair Value" (PV12).

We strongly disagree with the proposed new categorization of post-employment benefit arrangements and in particular, the concept of contribution-based promises as well as the associated measurement attribute "Fair Value" for contribution-based promises.

The currently adopted categorization of post-employment benefit plans (defined contribution plans and defined benefit plans) is based on the so-called "risk approach" (i.e. determination of existing risk to the plan sponsor once granted a pension benefit). In our view, it is comprehensible and provides the user of financial statements with appropriate information about the different economic substance, e.g. risk, of the various benefit plans. The new proposed categorization (contribution-based promise and defined benefit promise), on the other hand, is based on a rather artificial criterion. Contribution-based promises are defined as post-employment benefit promises in which, during the accumulation phase, the benefit can be expressed as a) an accumulation of actual or notional contributions known at the end of any reporting period and

b) as far as applicable, any promised return on the actual or notional contributions linked to the return from an asset, asset group or index. This definition and criterion does in no way offer users and preparers of financial statements sufficient support to consistently value the economic relevance and risk of post-employment benefit plans.

Instead, it is foreseeable that the new categorization will cause extensive effort and costs to map the existing defined pension plans on the new categories. On behalf of E.ON and presumably all other affected companies we assume that the Board will prudently consider the cost-benefit ratio in its further discussions of this topic.

Under the proposed regime, benefit plans which will produce identical benefit payments in the payment phase would be differently categorized, measured and accounted for. This happens on the basis of e.g. the method of accumulation of actual or notional contributions in the accumulation phase. From an economic point of view, we consider this approach as inconsistent and not understandable for the users of our financial statements.

Both contribution-based promises and defined benefit promises are based on nearly the same actuarial assumptions and exposed to several common risks, e.g. demographic risks, credit risks and asset-based risks. We do not see any convincing reason to apply different measurement and presentation of actuarial gains and losses to both categories, as intended. The current classification (defined contribution plan and defined benefit plan) largely avoids this inconsistency.

Considering the measurement attribute "fair value assuming the terms of the benefit promise do not change" for contribution-based promises, we find it difficult to derive a viable calculation concept for the "Fair Value" of contribution-based promises based on the general guidance provided, e.g. in item 7.34 of the DP. In addition, "the Board acknowledges that fair value assuming the terms of the benefit promise do not change may not be the fair value. This is a question that will be addressed in the fair value measurement" (see item 7.40 of the DP). The IASB's project "Fair Value Measurement" is still ongoing. Therefore, E.ON is of the opinion that as long as the "Fair Value Measurement" project is ongoing the Board should not consider the measurement attribute "Fair value" in the first phase of its project "Post-employment benefits". This would avoid premature changes in the measurement attribute with unforeseeable consequences in the first phase.

It is our understanding that the Board's original intention was to improve the accounting and measurement approach for the so-called "troublesome plans". The proposed solution of a new categorization goes far beyond this intention. In our opinion, the existing classification (defined contribution plan and defined benefit plan) should remain in place. Additionally, for a more realistic accounting/measurement of the real "troublesome plans", it could be sufficient to make adjustments to the current accounting/measurement approach "Projected Unit Credit Method".

- PV15 ("An entity should present in profit and loss all changes in the value of the liability for a contribution-based promise and all changes in the fair value of any plan assets."):

As we generally disagree with the Board's new definition of contribution-based promises and the intended measurement attribute "Fair Value" for contribution-based promises we also disagree with PV15. For arguments to our adverse opinion see our comments to PV2 in paragraph (a) and PV5 in paragraph (b).

(d)Accounting for benefit promises with a 'higher of' option (PV16 to 18 / Question 13)

- PV16 ("When a post-employment benefit promise is the higher of a defined benefit promise and a contribution-based promise, an entity should recognise and account for the 'host' defined benefit promise in the same way as a defined benefit promise. The entity should recognise separately the 'higher of' option."):

In principle we support the Board's PV16. However, we have serious concerns for reasons of practicability due to the unquestionable complexity resulting from the new categorization of post-employment benefit plans (defined benefit promises vs. contribution-based promises).

Therefore we clearly prefer the existing classification (defined benefit plan and defined contribution plan) which allows a pragmatic measurement of 'higher of' options.

Other issues (Question 14: What disclosures should the Board consider as part of that review?):

Basically we support any improvement of disclosures that will bring additional benefit to the preparers and the users of financial statements. Though again, on behalf of E.ON and presumably all other affected entities we assume that the Board will prudently consider the cost-benefit ratio in its discussions of further disclosure requirements.

As pointed out in our comment to PV3 in paragraph (a) more precise disclosures with regard to the estimation of the expected rate of return on plan assets could reasonably enhance the explanatory power of the presented information.

If you have any queries or questions on our comments, please feel free to contact us.

Yours sincerely,

E.ON AG

Michael C. Wilhelm Rainer Hinzen