The Institute of
Chartered Accountants
of Pakistan

HEAD OFFICE

International Accounting Standards Board,
30 Cannon Street, London EC4M6XH,
United Kingdom

September 26, 2008

Subject: **COMMENTS ON DISCUSSION PAPER 'PRELIMINARY VIEWS ON AMENDMENTS TO IAS 19 EMPLOYEE BENEFITS'**

Sir,

The Institute of Chartered Accountants of Pakistan welcomes the opportunity to offer comments on the above mentioned discussion paper.

Please find enclosed the comments of the relevant Committee of the Institute for your perusal.

If you require any further clarification, please do not hesitate to contact us.

Yours faithfully,

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COMMENTS ON DISCUSSION PAPER 'PRELIMINARY VIEWS ON AMENDMENTS TO IAS 19 EMPLOYEE BENEFITS'

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?

Answer

In Chapter 1.11 some further issues that may be considered in a more comprehensive review have been identified. It has also been stated that The European Financial Reporting Advisory Group has recently published a discussion paper *The Financial Reporting of Pensions that considers some of these further issues.**

The Board may therefore consider addressing as part of this project the further issues considered by The European Financial Reporting Advisory Group (TEFRAG) in its recently-published discussion paper *The Financial Reporting of Pension. We regard these issues as a matter of priority mainly because the TEFRAG has considered them to be of sufficient importance to already address them in a discussion paper.**

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?

Answer

The Board has rejected the view that immediate recognition of gains and losses in Plan assets and obligations (that are long-term and subject to many varying factors such as long-term economic outlook, the introduction of increasingly complex financial instruments, salary changes, length of service) will introduce volatility in reported earnings in annual financial statements – a volatility that may be self-adjusting over a period of several years.

In such case it may be too alarmist or too optimistic to immediately recognise losses and gains. The Board may therefore reconsider its preliminary views.

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?

Approach 1 - Entities present all changes in the defined benefit obligation and in the value of plan assets in profit or loss - provides the most useful information to users of financial statements because it does not differentiate between remeasurement changes and other costs thus avoiding the need for any arbitrary and potentially complex rules about the allocation of cost to profit or loss and in other comprehensive income. Moreover IAS 19 permits approach 1, and the Board too regards approach 1 as the least complex to implement and understand.

(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?

None.

(i) presentation of some components of defined benefit cost in other comprehensive income requires a clear distinction to be drawn between the operating and financing components of post-employment benefit promises by recognising only service costs in profit or loss and

recognising financing costs in other comprehensive income. Such a distinction is not useful to users.

(ii) disaggregation of information about fair value requires entities to divide actuarial gains and losses identified in IAS 19 into those arising from interest rate changes and other changes. It also requires some method, yet to be determined, of identifying interest income on plan assets. This may result in inconsistency in the calculation of such divisions.

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

In our environment the difficulties would be the ensuring of a consistent basis for actuarial valuations of plan assets and liabilities, and of their fair value.

Question 4

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

Obtain feedback from regulators and bodies representing the 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?

We have no alternative approach. In our view the three approaches discussed are sufficiently exhaustive and leave no room for the introduction of an alternative approach.

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?

We agree.

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?

Yes. The practical difficulties facing entities affected by these proposals relate to the management of the transition from defined benefit to contribution based promises and to reduce the uncertainty over the adequacy of the liability for post-employment benefits in annual financial statements during the transition period.

Question 7

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

Yes they do.

Question 8

Do you have any comments on those preliminary views? If so, what are they?

PV11 dispenses with the requirement to recognise an additional amount determined by the benefit that an employer would have to pay when an employee leaves employment immediately after the reporting date. Where however the additional amount is material it may be prudent to draw attention through a note to the accounts.

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.

No there are not.

(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?

At this stage of the Board's post-employment benefit promises project it is feasible to include the effect of risk as a component of the measurement approach without consideration of the risk that the terms of the benefit change.

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?

No. As per chapter 8.8 it is stated that the Board itself acknowledges both that

- **the same obligation should be accounted for in the same way, and that**
- **an obligation should be accounted for consistently throughout its life.**

The Board admits further that these two beliefs are incompatible in the quoted examples but is unable to resolve the contradiction in this project as it has limited the scope of the improvements in measurement to contribution-based promises to avoid delaying the project. We suggest that this aspect be deferred for consideration until the aforementioned contradiction is resolved and reconciled.

(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?

The Board has itself noted practical difficulties viz that if market prices were not available for annuities, the measurement of a contribution-based promise during the payout phase would require that entities determine a risk margin that includes the effect of demographic risk, particularly longevity risk. The Board recognises that there may be practical difficulties in determining that margin. This is a major practical difficulty.

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?

We agree with the Board's preliminary view that an entity should disaggregate changes in the value of the liability for a contribution-based promise into only

- **a service cost, and**
- **other value changes.**

We endorse the Board view that further disaggregation of changes in the fair value of the liability for a contribution-based promise would be difficult to achieve in an objective way. A subjective approach would not be useful for users of financial statements.

(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 that it is indeed difficult.

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?

Changes in the liability for contribution-based promises should be presented in profit or loss, along with all changes in the value of any plan assets because if they are to mirror the presentation of changes in the liability for defined benefit promises it defeats the very purpose of looking at contribution-based promises and defined-benefit promises as two different concepts.

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?

(i) The "higher of" options are defined benefit promises. Thus, they would be measured using the projected unit credit method in IAS 19. However, the projected unit credit method uses point estimates to calculate the expected value of the liability, and thus ignores the value of the option to obtain the higher benefit.

(ii) Another measure of a 'higher of' option is its intrinsic value which is represented by the amount of the difference at the end of the reporting period between the liability for the defined benefit promise and the liability for the contribution-based promise. However, measuring the option at its intrinsic value would:

- **ignore the value of any option that is out of the money at the reporting date, and would**
- **require comparison of two numbers that reflect different measurement approaches (projected unit credit for defined benefit promises and fair value assuming the terms of the benefit promise do not change for contribution-based promises).**

(iii) The 'higher of' option is similar to an embedded option written by the employer. IAS 39 requires entities to measure embedded derivatives, including options, at fair value. This is the best measure as it would:

- **incorporate both the intrinsic value and the time value of the option, thus better representing the obligation.**
- **not require the employer to determine the value of both the defined benefit promise and the contribution-based promise because the value of the option could be determined directly.**
- **result in promises in which the 'higher of' option is insignificant being measured at an amount similar to the host defined benefit promise, and promises in which the 'higher of' option has a large value reflecting the larger liability.**
- **be consistent with the treatment of financial options in IAS 39.**

(b) Do you have any other comments on the proposals for benefit promises with a 'higher of' option? If so, what are they?

No

Question 14

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

Introduction of explicit requirements to disclose information about the mortality rates used to measure post-employment benefit liabilities to allow users to understand the inherent uncertainties affecting the measurement of those liabilities.

Question 15

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

No

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