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THE ASSOCIATION OF INTERNATIONAL ACCOUNTANTS

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IASB opens discussion on proposals to increase transparency in the accounting for post-employment benefits

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Introduction

These comments are submitted by the Association of International Accountants, with input from a technical committee and members of the Association. AIA would like to thank Mr Bob Greenwood for his input in this response.

About AIA

AIA is one of six statutorily Recognised Qualifying Bodies (RQBs) in the United Kingdom for statutory auditors under the Companies Act 2006. The AIA professional qualification is recognised throughout the European Union and in other major financial centres around the world.

The Association promotes and supports the advancement of the accountancy profession both in the UK and internationally. Whilst supporting international accounting and auditing standards the AIA seeks to ensure that its examinations and membership requirements support the development of the accountancy profession in the countries in which it examines.

The AIA's examinations for membership have been held half-yearly on a world wide basis for 80 years. The examinations are based on International Financial Reporting and International Auditing Standards and are complimented by a range of variant papers applicable to local tax and company law in key jurisdictions together with an optional paper in Islamic Accounting. As an RQB under the UK Companies Act 2006 the AIA offers to students who take its examinations commencing in or after June 1991 and go on as members to complete special audit-based practical training under the AIA, an accountancy qualification which is recognised by the UK Government under that Act as a recognised professional qualification for statutory auditors in the UK.

AIA members are fully professionally qualified to undertake accountancy employment in the public and private sectors.

Opening Comments

AIA supports the IASB's preliminary views on how to address the inconsistencies and implementation difficulties arising from the multiple options available currently in IAS 19 which hinders comparability between entities.

AIA agrees that accounting for post-employment benefits is a very complex area which would benefit in the short term from improvements to several issues such as the deferred recognition of gains and losses arising from defined benefit plans.

We further support the IASB's preliminary views that no corridor approach should be used and the value of the plan assets and post employment benefit obligations should be recognised in full and immediately; however, AIA does not agree with the proposed definition for contribution-based benefit promises neither do we agree that the effect of the proposal will have a radical effect on existing practice.

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?

AIA considers the proposed solution of categorising many existing defined benefit promises as contribution-based plans is both too complex and inconsistent with the current requirements of IAS 19.

Question 2

Chapter 2 describes the Board's deliberations on the recognition of defined benefit promises. The Board's preliminary views are summarised in paragraphs PV2–PV4. 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?

AIA agrees with the IASB's preliminary view (PV2) that all changes in the value of the post-employment benefit obligation and plan assets should be recognised in the period in which they occur and that the measurement of the plan assets and the pension obligation must take into account the long-term nature of the items.

The current approach of IAS 19 to present actuarial gains and losses in the statement of comprehensive income should be retained as this would reduce smoothing income statement movements and permit the expected return on assets to continue to be presented in the profit or loss. This approach is appropriate for the short term, but for the long term, consideration needs to be given to the impact of recognising actuarial gains and losses on the entity's asset allocations.

Question 3

Chapter 3 sets out alternative approaches for the presentation of components of the defined benefit cost and analyses the relative merits of each approach. These approaches are summarised in paragraph PV5.

(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?

Approach 1: An entity presents all changes in the defined benefit obligation and in the value of plan assets in profit or loss in the period in which they occur are the most simple and transparent and therefore the most desirable.

Approach 3 introduces more rather than less complexity.

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?

By requiring entities to report the actual return on assets and the disclosure in the notes of the types and expected return of assets held in the plans; users will be provided with improved and relevant information about what the entity considers to be the requisite funding levels for the plans.

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?

AIA does not agree with the proposed definition of a contribution-based benefit promise (paragraph 5.3). We believe that existing IAS 19 deals adequately with such promises whereby it is the entity's obligation to underwrite the liability of the investment risk.
A post employment benefit promise should be measured at the amount of the accumulated notional or actual contribution for the period of service that is known at the end of any reporting period except for the effects of any vesting or demographic risks (5.27, 5.52 and 5.53).

This approach is consistent with the current requirements for plans that IAS 19 classify as defined contribution plans.

Question 6 – Definition of contribution-based promises

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?

It is likely that promises that are associated with 'higher of' options will be affected.

Question 7 – Definition of contribution-based promises

Contribution-based promises, as defined in this paper, include promises that IAS 19 classifies as defined contribution plans. The Board does not intend this proposal to lead to significant changes in the accounting for most promises that meet the definition of defined contribution plans in IAS 19. Do the proposals achieve that goal? If not, why not?

The AIA agree that the proposal should not lead to significant changes in the accounting for most promises that meet the definition of defined contribution plans in IAS 19. However, by adopting the methodology of the three building blocks (estimated future cash flows, the effect of the time value of money and the effect of risk) may change the values and timing of the recognition of some defined-contribution promises.

Question 8 – Recognition issues related to contribution-based promises

Chapter 6 discusses recognition issues related to contribution-based promises. 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?

No comments.

Question 9- Measurement of contribution-based promises

(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 AIA agree the above measurements using estimated future cash flows, the effect of the time value of money and the effect of risk would meet the objective. However the Discussion Paper is unclear as to how to measure the risk of changes in demographic assumptions and on the attributes of credit risk.

Question 10 - Measurement of contribution-based promises

(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?

The AIA agree with the IASB's preliminary view is that the liability for benefits should be measured in the same way during the deferment and payment phases as during the accumulation phase because we think that it adds to the complexity if there is a change in measurement as employees pass into the deferment or payment phase of the promise.

Question 11 - Disaggregation, presentation and disclosure of contribution-based promises

(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?

The AIA are not in favour of the introduction of the new category of contribution-based promises and that defined benefit promises should remain the default category of post employment benefit promises.

Cash balance plans should continue as defined benefit plans and not the residual category for all promises that were not deemed contribution-based.

Question 12 – Disaggregation, presentation and disclosure of contribution-based promises.

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?

Following the answer to Question 11 option (b) would be more useful as there will be consistency in the presentation of defined-benefit and those contribution-based promises that are currently treated as defined-benefit promises.

Question 13 – Benefit promises with a 'higher of' option

(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?

There is the continuing issue of how easy is it to value such options in practice.

Question 14 – Other matters

The Board intends to review the disclosures required about post-employment benefit promises in a later stage of this project. As part of that review, the Board intends to consider best practice disclosures in various jurisdictions. For example, explicit requirements to disclose information about the mortality rates used to measure postemployment benefit liabilities could be introduced to allow users to understand the inherent uncertainties affecting the measurement of those liabilities. What disclosures should the Board consider as part of that review?

The AIA believe that the disclosure requirements of existing IAS 19 provide useful and relevant information. Further disclosures of the assumptions used to measure mortality rates and the strategies and risks inherent in the pension provisions will enhance user understanding.

Question 15 – Other matters

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

No further comments.