



24 September 2008

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Comments on IASB's discussion paper *Preliminary Views on Amendments to IAS 19 Employee Benefits*

Dear Sir David,

The Japanese Society of Certified Pension Actuaries is a professional organization consisting of all the certified pension actuaries in Japan, and The Institute of Actuaries of Japan is an academic and professional organization consisting of all the actuaries in Japan. Both organizations engage in actuarial business activities in Japan, including establishing practice standards, investigative research, education, and training of actuaries.

We would like to express our respect for the efforts that the International Accounting Standards Board has made to develop a single set of high quality and understandable IFRSs, and appreciate the opportunity to submit our comments herewith to IASB's discussion paper *Preliminary Views on Amendments to IAS 19 Employee Benefits*.

It should be noted that we have submitted these comments based on our practical experience regarding the accounting for post-employment benefit of Japanese entities and not representing the interests of our members or their clients.

We will be pleased to accept any request to give further explanation about the issues presented in these comments.

1. General Comments

We hereby present our comprehensive views on the IASB's Discussion Paper *Preliminary Views on Amendments to IAS 19 Employee Benefits*.

- A. For the purpose of reviewing the accounting standards for post-employment benefits, we should fully consider overall consistency in our reflection on the significance of accounting for post-employment benefit obligations as a key factor and on the estimation method based on said obligations. Without these discussions, users of financial statements would be highly likely to misunderstand, if the accounting for defined benefit promises were changed to immediate recognition or if a new category of contribution-based promises were established and the current obligation measurement and accounting for those obligations were changed accordingly.
- B. Post employment benefit cost should be disaggregated and presented to the extent that IAS 19 currently requires, given the usefulness to users of financial statements.
- C. For post-employment benefits, there are differences in most essential characteristics of various countries' legal systems, such as the perspective of the priority of claims and nature of vested rights in past portions of benefits. To consider how we should implement measurement and accounting for obligations and reclassify benefit promises, we should fully reflect on the current circumstances of individual jurisdictions by examining these differences.

2. Comments on the Questions

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 we noted in the general comments above, for purposes of reviewing the accounting standards for post-employment benefits, we should fully consider overall consistency in our reflection on the significance of accounting for post-employment benefit obligations as a key factor and on the estimation method based on said obligations.

Having proposed a new category of contribution-based promises and changed the current methods of measurement and accounting for obligations in the absence of such argument about those issues, we are now facing several problems (see our comments regarding Questions 5 and 10). We believe these problems are material and could not be ignored.

With respect to the discussion procedures and preliminary views in the discussion paper, users of financial statements may well be puzzled, because we cannot rule out the following two possibilities. First, the possibility that gains and losses, having been recognized on financial statements according to the amendments of accounting procedures made in the first phase, will be re-amended in the second phase. Second, the possibility that an expected review of defined benefit promises, typically a final salary promise, in the second phase, would weaken the significance of the reclassification in the first phase into two categories.

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?

It is essential for us to fully discuss the measurement of defined benefit promise obligation before the immediate recognition approach is introduced.

Rationale

As the discussion paper noted, there has not been made any discussion about defined benefit promise obligation. We cannot decide the pros and cons of the proposed amendments if the significance of the accounting for post-employment benefit obligation and the estimation

method based on the latter are not firmly established. Without any conclusive views made through such deliberation, it would be impossible to decide whether or not to change the accounting treatment into immediate recognition.

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?

a) We do not agree with either approach 1, 2 or 3. Even if we were to introduce the immediate recognition approach, it would be desirable that changes in the first phase be limited only to the immediate recognition on the balance sheet without revising the current IAS 19 in terms of accounting for costs, and the latter be discussed anew in the second phase.

Rationale

As we noted previously, it would be necessary to consider how defined benefit promise obligations should be evaluated, as well as the accounting significance thereof, before we shift to the proposed immediate recognition type accounting treatment. If the change to immediate recognition is given priority over other issues, it would be more realistic that immediate recognition on the balance sheet should be let go first, and accounting for costs be discussed anew in the second phase.

b) Post employment benefit costs related to defined benefit promise should be disaggregated to the extent that IAS 19 currently requires, which would be useful for users of financial statements.

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?

a) Any discussion about the presentation of costs needs to consider relations between entities and pension schemes (e.g. the scope of control and the possibility that entities are allowed to make an investment decision of pension assets) which vary within each individual jurisdiction.

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 do not agree. It would not be appropriate to reclassify defined benefit promises and contribution-based promises based on the definitions shown in the present preliminary views.

Rationale

Since we have the pension plans indicated below in Japan, it would be impossible to consider, for some promises, that contribution-based promises are fundamentally different from defined benefit promises.

Example 1. There are some promises in which salary is defined not by the total amount of the salary, but by a portion of the salary (such as accumulation of ability evaluation), for the purpose of calculating the benefit amount, though such promises are classified into the final salary plan if they are based on post-employment benefit provisions.

Example 1 is regarded as defined benefit promise in appearance, but we may also consider that such promises include a cash balance pension-like component based on the salary used for benefit calculation. Therefore, it is not obvious how we should classify such promises into defined benefit or contribution-based promises.

Example 2. There are also some promises in which the benefit amount is calculated by multiplying the accumulation of credit points awarded annually based on ability evaluation by unit price at severance.

Based on the category of promise proposed in the preliminary views, Example 2 may be classified into contribution-based promise. However, unit price is expected to increase under the influence of, but not necessarily linked to, price and wage increases. Increased unit price also have an effect to credit points having accumulated in the past, which could comprise a risk of being similar with a salary increase risk in the final salary plan. This means that such promise has a feature that conflicts with the basic nature of contribution-based promises in that it does not carry a salary increase risk. Therefore, this example demonstrates an instance that negates the view that a defined benefit promise is fundamentally different from a contribution-based promise.

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, many promises would be. Under the Board's proposals, many promises in Japan would be reclassified from defined benefit promises in the current IAS 19 to contribution-based promises. One of the practical difficulties entities may suffer from these proposals in Japan is that there is a substantially large number of promises for which it would be difficult to draw a clear distinction between contribution-based and defined benefit promises (See Question 5), though there exist differences in the obligation evaluation methods and the accounting methods between defined benefit and contribution-based promises.

Question 7

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

We believe that a pure defined contribution plan based on definitions in the current IAS 19 should be separately classified into an independent category of promise.

Rationale

A pure defined contribution plan based on definitions in the current IAS 19 has an outstanding feature in which “an entity will not carry any risk after it has made contribution payments”, thus the presentation and disclosure of the accounting for such a pension plan will have to be set apart from those of the other promises included in contribution-based promises. Therefore, there is no substantial meaning in reclassifying the defined contribution plan into the same category

as the cash balance plan. Instead, it should be classified into an independent category of promises.

Question 8

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

If the benefit payment amount exceeds the obligation value when an employee leaves service immediately after the reporting date, disclosure of such information would be important.

Rationale

As noted in the discussion paper, such an additional amount would not have to be recognized in the financial statement. However, it may possibly be useful information for users of the financial statement.

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?

- b) It will be difficult to incorporate a credit risk in obligation estimation.

Rationale

Under the practice of corporate pension plans in Japan, entities are allowed to reduce even the past service portion of benefits if they meet certain conditions, such as poor business performance, and undertake necessary procedures, such as making an agreement with the labor union. Such amendment of the benefit amount serves to avoid defaults. In this context, it would be illogical to reflect only default risks in obligation estimation without considering implications of a change in the terms of the benefit promises. However, it would be even more difficult to estimate obligations by taking risks of such changes into consideration.

In addition, we often find it difficult to obtain credit risk information for entities, given that the markets of long-term and low credit-rated corporate debts are not large enough to make that information available. Moreover, measurement of fair value would require us to reflect the

vested nature and/or priorities of post-employment benefits. Discrimination in rights and obligations between post-employment benefit promises and corporate debts depends on the legislation in each country. It is obvious that we cannot obtain such information by taking such differences in corporate debt markets into consideration. Thus, if the corporate debt market size is large enough, it would be difficult to measure the fair value of post-employment benefit promises.

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?

a) We don't agree. The serious problem is that those benefits that remain economically identical in the deferment and payout phases are assessed as having two different amounts of liabilities.

Rationale

It is not appropriate that economically identical promises are presented at different liability values.

b) If plan amendments are made in such a way that a promise is reclassified from a defined benefit promise to a contribution-based promise, it would create a situation in which former employees who belong in the opposite category of promise are intermingled. There may also cases in which a former employee is classified separately into two categories according to their period of service. Estimation of the benefit liability for such former employees based on the respective categories requires us to maintain the beneficiary's data separately for those categories, which may eventually go beyond our ordinary administrative capacity to address them.

If any amendment of a plan had been previously made, former employees of different categories may be intermingled when the amended accounting standards are applied. Thus, there could also be cases in which it is practically impossible to determine which category the beneficiary belongs in.

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?

a) We do not agree that the reclassification of promises into contribution-based promises and defined benefit promises should be made according to the definitions provided in the preliminary views. However, if promises are to be reclassified in any manner, it will be useful to users of financial statements if the cost information is disaggregated to the same level of the current IAS 19.

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?

We do not agree that reclassification of promises into contribution-based promises and defined benefit promises should be made according to the definitions provided in the preliminary views. However, if promises are to be reclassified in any manner, presentation of the cost information should be made in the same way as for Question 11 a).

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?

Question 14

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

Question 15

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

With regard to the issue of the estimation of contribution-based promise obligation, the discussion paper refers to demographic risks, and specifically to longevity risk. The discussion paper indicates that those factors are of less importance for many promises. In Japan, however, there are many cases in which these factors are rather important. For your reference, we have provided below examples of promises that we often find in Japan.

In Japan, there are many examples of cash balance promises in which the balance of notional individual account is paid to an employee when the employee chooses a lump-sum benefit payment at severance. An employee may also elect to receive a fixed-term annuity terminable in a defined period, the amount of which is set equivalent to the balance of the notional individual account when the employee chooses annuity, and may continue over the employee's lifetime, even after the defined period has ended (This is also true for the relation between a lump-sum benefit and an annuity for many final salary plans). For those promises, the employee's choice of benefit type makes a considerable disparity in the value of benefit. Therefore, for the purpose of estimating the obligation of promises in the accumulation phase, additional costs for annuity payment must be reflected. If the longevity risk is taken into account, it should be reflected even in the accumulation phase.

We have exhibited the fact that those promises exist in Japan in our comments, which we submitted 21 September 2004, with respect to Draft Interpretation D9 of the International Financial Reporting Interpretations Committee.

In addition, it is common practice in Japan to pay an amount equal to the balance of a notional individual employee account multiplied by benefit rates that vary based on number of years of service and reason for severance. This means that the timing of the employee's severance in future will greatly affect the amount of benefits. Accordingly, emphasis is generally placed on past records of actual employees' turnover rate for each entity, where estimation of employee turnover is most widely practiced. However, further estimation of withdrawal risks or withdrawal volatility is not practiced.

As noted above, it is likely that there are highly important factors for estimation in individual jurisdictions in addition to those discussed in the discussion paper. We expect that those matters will be fully considered, and further discussions will be held to find a practically viable method to measure obligation.

Finally, we hope IASB will undertake field tests of the proposals in multiple legal jurisdictions, each of which are selected in consideration of geographical and cultural variances, in order to analyze and measure the influence and practical viability of the proposals before the Board publishes its draft.

Yours faithfully,

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