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Dear Madam, dear Sir,

Discussion paper – Preliminary Views on Amendments to IAS 19 Employee Benefits

De Nederlandsche Bank (DNB) welcomes the opportunity to comment on the Discussion Paper – Preliminary Views on Amendments to IAS 19 Employee Benefits.

The Dutch pension fund industry is perceived to be one of the leading post-employment benefit industries in Europe. From an economic and financial stability point of view, adequate income provisions for elderly people are a major indicator of a society's wealth and well-being. Notably, DNB has an interest in the reporting of post-employment benefit promises by banks and insurers, to the extent that these may have a material impact on banks´ and insurers´ financial position and, potentially, on key components of prudential regulatory capital. As a central bank and prudential supervisory authority, we have a strong interest in promoting sound and high-quality accounting and disclosure standards for the banking, insurance and pension fund industries in the Netherlands. In this matter, the revision of IAS 19, we hereby offer the Board suggestions that may contribute to a significantly improved standard, a ´milestone´ on the convergence roadmap vis-à-vis the US Financial Accounting Standards Board (FASB) and last but not least an important ingredient for stronger support from constituents, not only in the Netherlands but also in Europe. The suggestions brought forward in this letter are the result of intensive discussions in the Netherlands, amongst others with our Ministries of Social Affairs, Finance and Justice and the Dutch Accounting Standards Board (RJ).

General Comments

As stated in the introduction of the Discussion Paper, the Board intends to work with the US Financial Accounting Standards Board (FASB) towards a common standard on post-employment benefit promises and the Board thinks that short-term improvements are needed to provide users with better information. We fully concur with this view and we would like to provide the Board with our comments. Our main comment refers to the proposed direction of the post-employment

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benefit calculation methods as outlined in the Discussion Paper. In our view this direction could be characterised as one of adding more rules to the standard. We believe, however, there is some merit in exploring whether a more principle-based approach would meet with the Board's objectives in revising this standard. We hold the view that inclusion of certain high-level principles that might guide constituents to the appropriate calculation method would by and large resolve the issues that constituents have brought forward. Such inclusion would in our view also be commensurate with objectives of the IFRS such as a true and fair view, based on economic reality, and efficient application of the IFRS standards by constituents. One of the issues we have encountered in practice relates to problems in reconciling the characteristics of so-called average-salary schemes that include conditional indexation clauses, with the definitions of the current standard. In most cases institutions qualify for application of the defined benefit calculation method, although in most cases, the economic reality would suggest application of the defined contribution calculation method. Important aspects of the average-salary scheme with conditional indexation clauses relate to risk-sharing between the pension fund, the employer and current and former employees and to recognition of promises concerning the years of service during the accumulation phase. Furthermore, it is useful to mention that the annual, mandatory contributions employers have to pay include elements intended to cover credit and market risks of the plan assets, which are legally fully separated from the employer's assets. Unless these aspects are recognised in the defined benefit calculation method, the resulting outcome is highly likely to lead to an overstated pension liability on the employer's balance sheet. We think we ought to bring this to your attention for we are not convinced that the proposals in the Discussion Paper address these issues adequately. We wonder whether the inclusion of the new definition of contribution-based promises will bring relief to these, in our view, rather fundamental issues.

Legislation in the Netherlands requires employers to arrange for their pension promises to be carried out by a legally separate entity (pension fund). To this end the pension fund and the employer are required to agree on a number of financial aspects. In practice such agreements define the employer's financial obligation vis-à-vis the pension fund, including in cases where the funding ratio of the fund declines below the regulatory minimum level. Although we acknowledge this could be regarded as a challenge we believe it is, in the short term, worthwhile to explore possibilities of designing principles based on the elements of employers' residual financial risk mentioned above. Of course, the proposed principles should be designed in such a manner as to limit abuse as much as possible. In that process we would be pleased in assisting the Board if that would appear convenient.

Specific Comments

Question 1, additional issues to be addressed in the project's first phase
Elaborating on our suggestions set forth under the general comments, we believe that the Board could reconsider the recognition definition in the benefit formula (Projected Unit Credit Method) as currently included in the defined benefit calculation method. This applies especially to the recognition of the matching of future promises to future contributions. Usually, final salary

schemes include back service reimbursements by employers in the year the back service costs occur. These reimbursements constitute the funding of the increased defined benefit plan obligations (past service costs) and will in practice be added to the plan assets of the pension fund. We believe that matching these future cash flows is appropriate. When defining the recognition of future promises and funding, we see merit in cutting off this recognition at the measurement date – provided, of course, that the credit risk of future funding is to be considered very low.

As regards this recognition issue in relation to average salary schemes with conditional indexation clauses, we believe this matching issue is more critical because these schemes do not by nature lead to back service reimbursements.

At the moment the mentioned recognition effects are being smoothed by the corridor. Although in principle we are in favour of deleting smoothing instruments from this standard we strongly suggest that the Board take the above issues into account before deciding on the removal of the corridor.

Question 2, are there factors regarding the recognition of deferred changes in the liability which have not been considered by the Board
As previously stated we are, in principle, not against deletion of the corridor. However, due to identified recognition issues in the benefit formula of defined benefit plans we would not propose to increase the effects which in our view accompany the deletion. We suggest investigating the recognition matching features of the calculation method of defined benefit plans.

Question 3, which approach that replaces the corridor do you prefer
At this point in time we abstain from expressing any opinion on the proposed approaches.

Question 4, how could the Board improve the approaches
Further to our response under question 3, we recommend that this issue be addressed when the calculation method of defined benefit plans is revisited more fundamentally.

Question 5, has the Board identified the appropriate promises to be addressed in the scope of this project
We have suggested that the Board might reconsider the approach as outlined in the Discussion Paper, which in our view can be characterised as too much rule-based. In practice the range of schemes seems endless and it seems undoable to address each and every one of them in the standard. Instead we suggest including one or more high-level principles as indicated under our general comments and redesigning the calculation methods to become instrumental to the principles.

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Question 6, would many promises be reclassified from defined benefit to contribution based promises
We are not sure whether the majority of Dutch average salary schemes with conditional indexation clauses would be reclassified as contribution-based promises. One possibility to be considered to arrive at this goal would probably be to amend the definition of defined contribution promises. Such a new definition would then facilitate the use by fully outsourced schemes of the defined contribution calculation method.

Question 7, do the proposals meet the goal that the defined contribution definition would not be changed
Further to our response to question 6, we believe the proposals do not meet that goal. We believe that the defined contribution calculation method should be made instrumental to the high level principles mentioned under our general comments.

Question 8, do you have any comments on the recognition issues of contribution-based promises
In essence the recognition of contribution-based promises explained in paragraphs 6.6 to 6.9 seems inconsistent with paragraph 6.13. We would be in favour of the definition as stated in paragraph 6.13. We believe this definition aligns more closely with other recognition principles in the standards, such as IAS 37 (provisions) and IAS 36/39 (impairments). However, having this definition in the standard alongside the benefit formula could be regarded as confusing. We believe this issue needs further examination.

Question 9, are there alternative measurement approaches
Yes, we think so. We refer to our responses under general comments and under questions 1 and 8.

Question 10, should liability measurement for the deferment and pay-out phase be the same as for the accumulation phase
In our view this issue could be addressed appropriately when the more fundamental issues such as the inclusion of high-level principles are discussed.

Questions 11 and 12, how to present the changes in contribution-based promise liabilities
This issue could also be addressed when the more fundamental issues such as the inclusion of high-level principles are discussed.

Question 13, benefit promises with a 'higher of' option
No comments.

Question 14, disclosure requirements
If the Board should include one or more high-level principles in the revised standard, we could imagine that users of financial statements would need information about the legally separate entities (pension funds). Appropriate disclosure requirements would include information about the financial position of the pension fund. With these disclosures users of the financial statements

could establish the nature of the contributions paid by the employers and the possible effects in the future.

Question 15, any other comments
No comments.

Through this letter we also voice the intentions expressed by the ECOFIN in terms of IASB´s due process. We hope the Board will regard our suggestions as constructive and we would be pleased to answer any questions this letter could give rise to. We look forward to an interesting period of continued dialogue with the Board and its staff.

Yours faithfully,

Ms A.J. Kellermann
Executive Director

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