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30 June, 2004

CL 47

Dear Sir

Request for Comment on IASB ED Proposed amendments to IAS 19, *Employee Benefits: Actuarial Gains and Losses, Group Plans and Disclosures*

Thank you for the opportunity to provide comments on the above Exposure Draft, IASB ED Proposed Amendments to IAS 19.

The following are our responses to the requests for comment made by the IASB.

Question 1 – Initial recognition of actuarial gains and losses

IAS requires actuarial gains and losses to be recognised in profit or loss, either in the period in which they occur or on a deferred basis. The Exposure Draft proposes that entities should also be allowed to recognise actuarial gains and losses as they occur, outside profit or loss, in a statement of recognised income and expense.

Do you agree with the addition of this option? If not, why not?

We agree with the addition of this option. We believe that the provision of this option provides the most practical and effective means of reporting of actuarial gains and losses as they occur whilst the Board is still considering the issue of reporting financial performance.

Question 2 – Initial recognition of the effect of the limit on the amount of a surplus that can be recognised as an asset

Paragraph 58(b) of IAS 19 limits the amount of a surplus that can be recognised as an asset to the present value of any economic benefits available to an entity in the form of refunds from the plan or reductions in future contributions to the plan (the asset ceiling). The Exposure Draft proposes that entities that choose to recognise actuarial gains and* *losses as they occur, outside profit or loss in a statement of recognised income and expense, should also recognise the effect of the asset ceiling outside profit or loss in the same way, ie in a statement of recognised income and expense.*

Do you agree with the proposal? If not, why not?

We agree with the proposal.

Question 3 – Subsequent recognition of actuarial gains and losses

The Exposure Draft proposes that, when actuarial gains and losses are recognised outside profit or loss in a statement of recognised income and expense, they should not be recognised in profit or loss in a later period (ie they should not be recycled).

Do you agree with the proposal? If not, why not?

We agree with the proposal.

Question 4 – Recognition within retained earnings

The Exposure Draft also proposes that, when actuarial gains and losses are recognised outside profit or loss in a statement of recognised income and expense, they should be recognised immediately in retained earnings, rather than in a separate component of equity and transferred to retained earnings in a later period.

Do you agree with the proposal? If not, why not?

We do not agree with the proposal. We believe actuarial gains and losses should be recognised as a separate component of equity and transferred to retained earnings in a later period.

Paragraph BC3 states that actuarial gains and losses are "(a) experience adjustments (ie the effects of differences between actuarial assumptions and what occurred) and (b) the effects of changes in actuarial assumptions. They include unexpected changes in the value of the plan assets and can be large and volatile." It appears to us that actuarial gains and losses arise primarily from revaluation of:

a. the benefit obligations due to changes in actuarial assumptions; or
b. the fund assets due to the use of market values.

In both cases, these revaluations are subject to market forces. In the case of benefit obligations, IAS 19 requires the discount rate to be based on the yields on high quality fixed interest securities (which in the past have shown significant volatility). In the case of assets, market values, with equity investments, being the case in point are highly volatile. This volatility means that actuarial gains and losses are temporary. For example, in the period 1999 to 2000, yields on fixed interest securities rose significantly. Consequently, fund liabilities were reduced resulting in significant actuarial gain on liabilities. However, such gains were subsequently reversed as interest rates fell during the period 2001 to 2003.

As actuarial gains and losses are temporary in nature, we do not believe it is appropriate to classify actuarial gains and losses as retained earnings. Further, users of financial statements may wish to separately identify actuarial gains and losses. Such users may include regulators of financial institutions who may wish to exclude actuarial gains and losses from their assessment of the regulatory capital of a financial institution. Investment analysts may also wish to discount or exclude actuarial gains and losses from their assessment of a company's financial position.

The need to separately identify actuarial gains and losses also arises from legal and practical constraints that reporting entities' may face in accessing the surpluses of defined benefit funds (which were recognised during the last revision of IAS 19 in 2000). For example, in Australia, legislation requires trustees' approval of repatriation of surplus of pension funds. In such cases, the trustees are required to act in members' interest.

Question 5 – Treatment of defined benefit plans for a group in the separate or individual financial statements of the entities in the group

(a) The Exposure Draft proposes an extension of the provision in IAS 19 relating to multi-employer plans for use in the separate or individual financial statements of entities within a consolidated group that meet specified criteria.

Do you agree with this proposal? If not, why not?

(b) The Exposure Draft sets out the criteria to be use to determine which entities within a consolidated group are entitled to use those provisions.

Do you agree with the criteria? If not, why not?

We agree with both the proposal and the criteria. However, we do not believe that they go far enough. The proposal merely extends the multi-employer reporting requirements to subsidiaries. If adopted, subsidiaries would not be required to prepare defined benefit reporting if:

1. they meet the criteria in paragraph 34; **and**

2. there is no consistent or reliable basis of allocating assets and liabilities amongst reporting entities.

It is recognised that the disclosures under IAS 19 are complex and often requires actuarial skills. As such, they are costly and time consuming to prepare. In view of this, we do not believe that it is practical to require a subsidiary to prepare IAS 19 disclosures when the parent company has already prepared these disclosures on a consolidated basis, especially when the subsidiaries' financial statements are only prepared for legislative purposes and there are no external users of these statements. We request the IASB to consider amending IAS 19 to exempt subsidiaries from IAS 19 disclosures as long as the criteria set out in paragraph 34 are met.

Question 6 – Disclosures

The Exposure Draft proposes additional disclosures that (a) provide information about trends in the assets and liabilities in the defined benefit plan and the assumptions underlying the components of the defined benefit cost and (b) bring the disclosures in IAS 19 closer to those required by the US standard SFAS 132 Employers' Disclosures about Pensions and Other Postretirement Benefits.

Do you agree with the additional disclosures? If not, why not?

The majority of the additional disclosures are in line with the new requirements of US accounting standard SFAS 132 "Employers' Disclosures about Pensions and Other Postretirement Benefits". Hence, we agree with the additional disclosures. However, the following requirements go beyond the additional requirements of SFAS 132 introduced in December 2003:

A. The requirement in Paragraph 120(g) to disclose the expected rate of return for each major category of plan assets. At their meeting on 11 November 2003, the US Financial and Accounting Standards Board (FASB) considered this additional disclosure and decided not to proceed with it. The minutes of that meeting stated:

   "They noted that expected returns by individual categories could mislead users, who might try to re-calculate the overall expected return based on these individual categories."

   We concur with the US FASB's reason.

   Further, disclosures of these assumptions will encourage comparisons of these assumptions. We do not see any point in such comparisons or the disclosures of these assumptions when the assumptions depend largely on individual judgment and may vary significantly from one reporting entity to another.

   The economic assumptions (in particular return on asset assumption) may vary between different countries because of differences in investment market conditions or economic factors. As such, it is generally necessary to disclose the different assumptions for countries with material obligations. Inclusion of the return on asset assumption for individual sector will make the disclosures for these entities unwieldy.

We acknowledge that there is a concern that reporting entities may vary their return on asset assumption to manage their reported earnings. We believe that the requirement for reporting entities to disclose the basis for determining the return on asset assumption would alleviate much of these concerns without the consequences of disclosing the return on asset assumption for the individual sector.

B. The requirement in Paragraph 120(j)(ii) to disclose the property occupied by, or other assets used by, the reporting entity is also beyond the requirement of SFAS 132. The investments of a defined benefit fund should be independent of the reporting entities' financial performance. If not, then these should be disclosed. We believe that this is only appropriate for equity investments where the value of the investments may be zero in the event of a corporate collapse. However, this is less likely to occur with other investment such as property which could be re-leased or sold to another user in the event of a corporate collapse. As such, we do not believe there is additional value with these additional disclosures.

C. The requirement of paragraph 120(l) to disclose the actual returns on asset is a repeat of the requirement to disclose the expected return on assets and the actuarial gains and losses on assets in the reconciliation of fair value of assets (paragraph 120(e)). As such, we do not believe paragraph 120(l) is necessary.

D. The requirement under paragraph 120(o) is a repeat of the current and previous years' disclosures of the fair value of assets and defined benefit obligations. As such, we do not consider that it is necessary as users of financial statements can reproduce this information.

Question 7 – Further disclosures

Do you believe any other disclosures should be required, for example the following disclosures required by SFAS 132? If so, why?

(a) a narrative description of investment policies and strategies;

(b) the benefits expected to be paid in each of the next five fiscal years and in aggregate for the following five fiscal years; and

(c) an explanation of any significant change in plan liabilities or plan assets not otherwise apparent from other disclosures

SFAS 132 also encourages disclosure of additional asset categories if that information is expected to be useful in understanding the risks associated with each asset category.

We support the inclusion of the requirement to disclose the benefits expected to be paid in each of the next five fiscal years and in aggregate for the following five fiscal years but on a voluntary basis.

Currently, there is no means under the current IAS 19 disclosures to gauge the expected cash outflows due to the defined benefit obligations. In the end, the defined benefit obligations are obligations to pay benefits in the future. Hence, the ability of a reporting entity to meet the future cash outflows is as important as the impact of any net surplus or deficit on its balance sheet.

However, these disclosures require actuarial skills which are costly. It follows that we do not believe that this requirement should be compulsory for all reporting entities (especially with small to medium sized reporting entities).

We do not support the requirement to disclose investment policies and strategies. Disclosures of investment strategies and policies will encourage comparison of investment policies and strategies. Investment policies and strategies are formulated according to assessment of long term factors such as the risk/return trade-off and the profile of the benefit obligations. Many of these factors are different from one fund to another. Further, there is also a significant degree of individual judgment in the formulation of investment strategies and policies. As such, comparisons of investment strategies and policies are invalid.

Further, we believe that it would be difficult to derive conclusions based on the short succinct disclosures in financial statements, especially when there is no descriptive disclosure of the liabilities.

It should also noted that reporting entities may not have any legal power to influence or determine the investment strategies and policies of funds. As such, they are not in any position to report to queries from users if they (the users) raise any queries on the fund’s investment strategies and policies.

Please do not hesitate to contact me if you would like to discuss our submission in more detail.

Yours sincerely,

Louise Thomson