MONASH University

Department of Accounting and Finance

9 June 2004

Ms Anne McGeachin
Profect Manager
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Ms McGeachin

Proposed Amendments to IAS 19 *Employee Benefits: Actuarial Gains and Losses, Group Plans and Disclosures*

My comments on the proposed amendment to IAS 19 are attached. I must say that I was deeply disappointed that the Board decided to tinker with the standard rather than undertake a comprehensive review. I do not support the proposed new alternative for past service costs. The proposal does nothing to improve financial reporting of employee benefits.

I appreciate the token attempt to improve the drafting of IAS 9, however, from a user standpoint the drafting style makes it extremely difficult to understand the requirements though the undisciplined intermingling of editorial comment and substantive requirements. I must say that I find it inexplicable that the Board, despite numerous complaints, has done nothing to reform its drafting practices. An unavoidable consequence of the present drafting style is the effective exclusion of those with reading disabilities. In many jurisdictions this would amount to an unlawful discrimination against those with reading disabilities. While it was not, one presumes, the Board's intention when adopting the current drafting style to discriminate against those with reading disabilities, its failure to do anything to improve the drafting style changes the character of Board's conduct from inadvertent to wilful. It is time for the Board to adopt international best practice for drafting rather than clinging to a style that can reasonably be described as an exemplar of international worst practice for drafting accounting standards. The best starting point

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in developing an improved drafting style would be to look at the style adopted by the Australian Accounting Standards Board.

If you, or the Board's technical staff, wish to discuss the issues raised in this submission please do not hesitate in contacting me by telephone (+61 3 9905 2701) or email (ian.langfield-smith@buseco.monash.edu.au).

Best wishes

Ian Langfield-Smith FCPA

Response to ED 131: Request for Comment on IASB ED Proposed Amendments to IAS 19 *Employee Benefits: Actuarial Gains and Losses, Group Plans and Disclosures*

Response by Ian Langfield-Smith

Introductory comments

The change in the carrying amount of an asset or liability recognised by an employer in relation to its defined benefit plan obligations clearly meets the definition of either an expense or income under the IASB's Framework. The excluding the impact of such a change (be it an expense or income), in determining the amount of net profit is an exception to the general rule in IAS 1, and accordingly *must* be supported by compelling a justification. An argument could be put forward that the existing alternative are defective; however, one would have though the logical consequence of any such argument would be their banning. However, this is not proposed. Deferral and amortisation can only, in my view, be described as financial reporting shonk, and should not be permitted under any circumstances. It is an exemplar of the financial reporting practices that have rightly brought the accounting profession into disrepute. Fortunately, I can see no conceptual problems with immediate recognition of the change in the carrying amount of the liability (asset) arsing from the employers' obligations under a defined benefit plan in determining the amount of net profit. Indeed to me it is nothing more than the application of common sense.

Reponses to IASB questions

Question 1 - Initial recognition of actuarial gains and losses

IAS 19 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?

I do not support the proposal. I doubt that it is ever appropriate to recognise an item of expense or income directly in equity. I do not see how excluding such expenses and revenues can enhance the discharge of accountability of management or result in users of financial reports being better informed. If we have a general rule that all revenues and expenses are to be included in determining the amount of net profit – and we have such a rule in IAS 1 paragraph 78 – then a test must be put forward by which we can determine if it is proper to depart from that rule. As yet the IASB had been either unable or unwilling to provide such a test. Resort to existing practice in some countries or an unwillingness of management to accept responsibility for the consequences of their stewardship cannot, in my view, justify departure from the general rule in paragraph 78. Further, it has not been established that users of financial reports will be better off under this alternative than under the exiting alternatives. While the proposed alternative is likely to result in users being better off than if the alternative of deferral and amortisation were adopted, I cannot see how they would be better off than they would be under the initial recognition in determining the amount of net profit.

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?

Given the answer to Question 1, this question is not applicable.

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 this proposal? If not, why not?

Given the answer to Question 1, this question is not applicable. However, I believe that recycling should never be permitted.

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 recognised in a separate component of equity and transferred to retained earnings in a later period.
Do you agree with this proposal? If not, why not?

Given the answer to Question 1, this question is not applicable.

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

At this stage I make no comments on these proposals.

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

I do not wish to make any comment on this question at this time. However, the redrafted disclosure provisions are (in terms of their drafting) an improvement over the existing provisions.

Question 7 - Further disclosures

Do you believe that 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.

I believe this information would be potentially useful to users of financial reports.

Comments on proposed drafting changes

The proposed wording, like the current wording, in the introductory part of paragraph 61 is misleading. The use of "recognise the net total" suggest to me that this paragraph requires a netting of revenues and expenses as described in paragraphs 32 to 35 of IAS 1 (December 2003 version; paragraphs 33 to 37 of prior version). However, paragraph 119 indicates that this is not the intention. If paragraph 119 reflect the true intention underlying paragraph 61 then the use of the word "net" is completely inappropriate. Surely it would be sufficient to state that "the following amounts must be included in profit or loss"? I note also that the usage "included in profit and loss" is extremely poor; clarity of expression (something that the IASB appears to put at the bottom of its priorities when drafting standards) would suggest that a more appropriate form of words would be "included in determining the amount of profit or loss". While decomposing the change in the amount of an asset or liability recognised for an employers' obligations under a defined benefit plan may provide useful insights, nothing is gained by pretending that there is more than one expense.

I note that some ill informed commentators have suggested that the interest component can form part of an entity's borrowing costs. Such a proposition is clearly nonsense as the definition of borrowing in IAS 23 is not satisfied; there is no borrowing of funds, thus the interest cost cannot be a component of borrowing costs. One could argue that such interest costs are a component of the undefined term finance costs used in paragraph 81(b) of IAS 1. It is unclear to me on what basis one would differentiate borrowing costs from finance cost; at first sight a reasonable person would, in absence of any guidance, be entitled to assume that "borrowing costs" and "finance costs" were the same. This inconsistency in usage is a further example of the lack of attention to detail taken by the IASB when drafting its standards.