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Dear Anne

Exposure draft of proposed amendments to IAS 19 *Employee Benefits*

We appreciate the opportunity to respond to the International Accounting Standards Board's exposure draft of its proposed amendments to IAS 19 *Employee Benefits*. This letter expresses the views of KPMG International and its member firms.

We acknowledge the Board's reservations about the option in IAS 19 to defer recognition of actuarial gains and losses. However, introducing the additional option of immediate recognition in a statement of recognised income and expense does not solve the problem with deferred recognition. The proposal is not in line with the spirit of the Improvements Project, which was to reduce the number of accounting options within the same standard. Further, it seems inconsistent to have two different recognition approaches, recognition directly in equity and immediate recognition in profit or loss, for the same item.

We would prefer that all of the proposed changes to IAS 19, other than the change in respect of participation in group plans, be considered as a part of a comprehensive project on post-employment benefits covering all areas, preferably as a joint project with other standard setters, including the US FASB and the UK ASB, both of whom have expressed interest in such a project. We also believe that it would be preferable to link such a comprehensive pension project to a performance reporting project. Therefore we believe that the Board should defer moving forward with this limited scope amendment, other than permitting use of a multi-employer approach for group plans.

We encourage the IASB to consider, in a comprehensive project, the recent work of national standard setters who have considered the issue of employee benefit accounting. This includes both the UK ASB, which issued FRS 17 *Retirement Benefits* in 2000, and the Dutch Council for

Annual Reporting (CAR), which recently modified its guidance for employee benefit accounting (see the most recent codification in CAR Guideline 271 (2004)).

As noted above, a pension project clearly overlaps the performance reporting project. If this limited scope project is pursued in the short term we strongly encourage minimising its impact on the outcome of the performance reporting project. This includes not making the proposed consequential amendments to IAS 1 *Presentation of Financial Statements* regarding the statement of recognised income and expense.

The proposed revisions would be effective for annual periods beginning on or after 1 January 2006, with the Board encouraging early adoption. Knowing whether further changes will be made to IAS 19 has created some uncertainties for entities working on their conversion to IFRSs from 2005. Therefore we suggest that the Board resolve as soon as possible whether it will proceed with this limited scope amendment in order to reduce this uncertainty.

We have responded to the invitation to comment in case the Board decides to progress the issues covered in this Exposure Draft in the short term.

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?

As explained above, we do not support introducing an additional option into IAS 19. If the Board decides to pursue an interim project to introduce such an option we would not support making the changes proposed to IAS 1. IFRSs currently do not require a statement of recognised income and expense. We do not believe that this is the appropriate time or place to reach a conclusion regarding what kind of "performance reporting" should be adopted for IFRSs. Therefore, we disagree with the proposed changes to the statement of changes in equity even if the immediate recognition option is introduced.

We welcome the clarification implicit in the first sub-clause of paragraph 93A that the "faster recognition" permitted by paragraph 93 of IAS 19 includes recognition in the year that the gains/losses arise. This is an issue that has been raised in practice, and this is a conclusion that we had reached based in part on the reference in paragraph 92 to "the end of the previous reporting period".

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?

If the limited scope project moves forward as proposed, we agree that if immediate recognition of actuarial gains and losses is permitted, any consequential impact of the asset ceiling should be reported consistently. We do not see any reason for treating the impact of the asset ceiling in a different way than related actuarial losses or gains.

We believe that the reference in paragraph 93B to IAS 1.100 should be to IAS 1.101.

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?

IFRSs require recycling for some transactions (e.g. realised gains or losses on financial instruments classified as available for sale) and prohibit recycling for other transactions (e.g. revaluation of fixed assets).

As we noted in our introductory comments, we have significant concerns in pursuing this limited scope project without completing a more fundamental debate about performance reporting, including recycling. We believe that any conclusion reached in the limited scope amendment that IFRSs should prohibit recycling would be a premature conclusion.

However, if the limited scope project moves forward we believe that actuarial gains and losses should not be recycled as this currently is the practice under FRS 17 *Retirement Benefits* and the limited scope project seeks to achieve convergence with FRS 17. Therefore divergence should not be introduced and the gains and losses should not be recycled.

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?

Generally IFRSs do not specify any particular classification of gains and losses within equity. For example IFRS 2 *Share-based Payment* does not specify which equity classification should be used for an option premium. Whilst we do not object to the presentation proposed, we do not believe that the IASB should start mandating, in this project, classifications within equity. Further, we believe that separate classification or footnote disclosure of actuarial gains or losses should not be prohibited. In our view, the IASB should limit its classification guidance to a requirement that all actuarial gains and losses be included in the same component of equity.

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

(a) The Exposure Draft proposes an extension of the provisions 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 used 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 that the provisions in IAS 19 relating to multi-employer plans should be extended to plans of entities under common control. We also agree with the Board's conclusion set out in Basis for Conclusion, paragraph BC20, that it would not be appropriate to create an unqualified exemption for group entities from defined benefit accounting and that the exemption should, as in part proposed, rest upon the ability to make a consistent and reliable allocation of the assets and liabilities of the plan.

However, we do not believe that the proposed criteria necessarily will result in a basis of accounting that is meaningful. We believe that the criteria used to determine whether an entity may use the multi-employer plan exemption should be consistent with the conclusions reached in IFRIC D 6 *Multi-employer Plans*. While it may be appropriate to presume that each participating entity within a group can obtain the appropriate data, allocation of that data may not result in relevant and reliable defined benefit accounting. Criteria such as whether the participating entity has a stable proportion of the plan should be taken into consideration before concluding that the allocation of the defined benefit valuation provides relevant and reliable information an therefore is appropriate. We refer also to our response to IFRIC D6, dated 26 July 2004, which discusses this issue further (see copy, attached).

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?

On its own, each additional disclosure provides some incremental insight into the reporting entity's calculation of its IAS 19 obligation. However, we note that the disclosure requirements for IAS 19 are extensive, and we do not believe that the objective of disclosure should be to permit recalculation of the reported amounts. Therefore we encourage the Board to consider responses from preparers about the relative cost of such disclosures and ask users to explain how they will use such data as we have some concern that the cumulative requirements risk information overload.

We have some specific comments, which are set out by proposed paragraph number.

120(c): should "service cost" be "current service cost"?

120(g): the term "current service cost" appears to be used inconsistently. As defined, and as used in paragraph 120 (c), it is the gross increase in the present value of the obligation caused by service during the period – ie, gross of employee (participant) contributions. Presumably, the figure to be disclosed under 120(g) should be the income statement cost to the employer – ie, net of contributions by participants. Does this need some explanation in the paragraph?

120(o): no transitional relief is proposed in respect of this paragraph, which calls for five years of information. Entities that have not been applying IAS 19 for five years (eg, Australian companies adopting IFRSs from 2005) will not have this information readily available and to call for its disclosure is inconsistent with the exemption permitted to first-time adopters by IFRS 1 as they may elect to recognise the surplus or deficit on the balance sheet at the transition date. We believe that transitional relief should be granted to permit first-time adopters to increase their disclosure gradually to five years of data.

120(p): the phrasing seems unusual for an IFRS: "the next *fiscal* year beginning after the balance sheet date". Normally IFRSs refer to *financial* years.

120(p): this disclosure requirement covers the cash outflow expected in relation to funded plans but we wonder whether an equivalent disclosure should be introduced in relation to unfunded plans. For example, should disclosure be required of the employer's best estimate of benefits to be paid under such plans during the next financial year beginning after the balance sheet date?

Comparatives, etc

120(m): the proposed disclosures mirror those of SFAS 132 *Employer's Disclosures about Pension and Other Postretirement Benefits* and the approach of existing IAS 19 in calling for the income statement disclosures in respect of each period presented in the financial statements for items (ii) and (iii). It is not clear for what years the discount rate information in (i) should be stated; the implication of the introductory text "as at the balance sheet date" suggests disclosure of the rate that will affect the next year's income statement and, as a comparative, that which has affected the current year's, but this would be inconsistent with the other income statement assumption disclosures.

Paragraph 120(m) requires disclosure of the expected rates of return on plan assets for the periods presented (current and comparative) but paragraph 120(i) also requires disclosure of the expected rates of return as at the balance sheet date (ie, those which will affect next year's income statement). We presume that this is intentional, but it would be helpful to make this point clearer.

The disclosures required by FRS 17 *Retirement Benefits* with respect to all financial assumptions and the expected rates of return on assets include the assumptions and rates as at the balance sheet date since these assumptions and rates will form the basis for the following period's income statement amounts, with comparatives required for each balance sheet date. This means that three years of assumptions and rates are disclosed by an entity giving one comparative year of information within its accounts. If the project is moved forward we recommend the UK approach since it provides additional information to users but we accept that this may be too fundamental a change to make in this limited exposure draft.

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.

Some additional disclosures are suggested above in our response to question 6.

We agree with the IASB's omission of other SFAS 132 disclosures not currently proposed in the IASB's exposure draft. Some entities may want to present information voluntarily (e.g. along the lines of that in (b) of the question) if their defined benefit obligation is very significant in relation to their net asset value and they wish to demonstrate that the cash impact is a very long term one but we do not believe that this should be required in all cases.

* * *

Please contact Mark Vaessen at 020 7694 8089 if you wish to discuss any of the issues raised in this letter.

Yours sincerely

KPMG International

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Enclosed: IFRIC D6 response