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International
Accounting Standards
Board

INFORMATION FOR OBSERVERS

Board Meeting: **20 March 2007, London**

Project: **Post-employment benefits**

Subject: **Presentation alternatives (Agenda paper 4)**

INTRODUCTION

1. At its February 2007 meeting, the Board confirmed its preliminary view that all gains and losses on defined benefit post-employment plans should be recognised in profit or loss. The Board also asked the staff to develop two alternative approaches to the presentation of defined benefit costs and describe the objectives and justification for each approach.

2. At that meeting, a Board member suggested that the Board's preliminary view might be restricted to immediate recognition in comprehensive income with no preliminary view on presentation. Although some Board members appeared to support this proposal, no vote was taken.

3. This paper:

   (a) discusses the suggestion that the Board's preliminary view might be restricted to immediate recognition in comprehensive income with no preliminary view on presentation.

(b) describes the rationale and justification of recognising all gains and losses in profit or loss, together with two alternative approaches requested at the last meeting.

STAFF RECOMMENDATIONS

4. The staff recommends:

   (a) the Board's preliminary view for the discussion paper is that all gains and losses should be recognised in comprehensive income in the period in which they occur.

   (b) the Board does not express a preliminary view on presentation.

   (c) that the discussion paper would discuss the following approaches in a neutral, consistent manner:

      (i) all gains and losses recognised in profit or loss.

      (ii) financing costs recognised outside profit or loss.

      (iii)remeasurement changes recognised outside profit or loss.

IMMEDIATE RECOGNITION IN COMPREHENSIVE INCOME

5. At the last Board meeting, a Board member suggested that the Board's preliminary view might be restricted to immediate recognition in comprehensive income with no preliminary view on presentation. The staff supports this suggestion.

6. [Not included in observer notes]

7. [Not included in observer notes]

8. [Not included in observer notes]

9. [Not included in observer notes]

10. [Not included in observer notes]

11. [Not included in observer notes]

12. The staff recommends that:

(a) the Board's preliminary view for the discussion paper is that all gains and losses should be recognised in comprehensive income in the period in which they occur.

(b) the Board does not express a preliminary view on presentation.

PRESENTATION ALTERNATIVES

13. The rest of this paper describes three approaches to the presentation of defined benefit plan components, including some observations on their rationale, advantages and disadvantages, as they might be set out in the Discussion Paper. One of the approaches would present all components of the defined benefit cost in profit or loss. The other approaches would present some components outside profit or loss. Although there are many possible approaches that present some components outside profit or loss, the staff does not see any merit in exploring other variations individually. As requested by the Board, the staff has developed two approaches that attempt to draw a basis for distinguishing items presented in profit or loss from those presented outside profit or loss.

14. The staff recommends that the discussion paper would discuss the following approaches in a neutral, consistent manner:

(a) all gains and losses presented in profit or loss (see paragraph 17-19).

(b) financing costs presented outside profit or loss (see paragraphs 20-24).

(c) remeasurement changes presented outside profit or loss (see paragraphs 25-29).

An illustration of these approaches is included in the appendix. If Board members agree that we have the descriptions correct, we will work more to buttress the arguments in favour of each (as promised at the February meeting).

15. In discussing how components of pension cost should be presented, the staff considered the following:

(a) Employee benefit plans involve deferred payment of a current benefit. Thus, the components of the defined benefit cost for each period includes both the current benefit and the effects of deferring payment of benefits from the current and previous periods. Some users favour separate presentation of the financing costs and the costs relating to employee service in the period. Although they regard information about financing as useful and relevant to the financial statements, they consider it different from information about the operating and business activities of entities.

(b) Some constituents argue that, if some components of post-employment benefit cost are presented outside profit or loss, it is important to examine potential interrelationships between different components. Those most often suggested by constituents are the interrelationship between (i) the interest cost on the post-employment benefit obligation and interest income on plan assets, and (ii) between the total return on plan assets and the change in the post-employment benefit obligation. This is discussed further in paragraph 23.

(c) The Board decided at its November 2006 meeting that the requirement to divide the return on assets into an actual and expected return should be eliminated.

(d) The Board decided at its November 2006 meeting that it would not require recognition of gains and losses in profit or loss that had been recognised outside profit or loss in an earlier period (recycling) in Phase 1 of this project.

16. The three approaches discussed below set out different ways in which information about components of comprehensive income for pensions could be structured. The aim is to find an approach to presentation that provides clear, transparent and useful information to users.

APPROACH 1: ALL IN PROFIT OR LOSS

17. This approach presents all changes in the defined benefit obligation and in the value of plan assets in profit or loss in the period in which they are incurred.

18. [Not included in observer notes]

19. [Not included in observer notes]

APPROACH 2: FINANCING APPROACH

20. This approach presents the costs of service in profit or loss. All other costs are reported as consequences of deferring payment of employee remunerations and financing that deferred payment.

21. Accordingly:

    (a) service costs, and the gains and losses associated with them are recognised in profit or loss. Thus, service costs, and actuarial gains and losses on the defined benefit obligation except those arising from changes in the discount rate would be recognised in profit or loss.

    (b) all other changes are recognised outside profit or loss. This includes interest cost, changes in the discount rate and all changes in plan assets.

22. [Not included in observer notes]

23. [Not included in observer notes]

24. [Not included in observer notes]

APPROACH 3: REMEASUREMENT APPROACH

25. This approach presents changes arising from changes in financial assumptions outside profit or loss. Thus, changes in the computed "price"[1] of the pension obligation and fair value of plan assets are recognised outside profit or loss.

26. Accordingly, profit or loss would include:

    (a) service cost,

    (b) interest cost,

    (c) actuarial gains and losses on the defined benefit obligation except those arising from changes in the discount rate,

    (d) dividends received on plan assets, and

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[1] We use the word "price" here in a general sense, rather than the useage adopted in the discussion document on fair value measurement or the conceptual work on measurement. The application of present value "prices" the future benefit outflows. However, we note that the projected unit credit method does not produce fair value and that the discount rate is not necessarily the one that market participants would apply.

(e) interest earned on plan assets (using the current rate inherent in the fair value).

27. [Not included in observer notes]

28. [Not included in observer notes]

29. [Not included in observer notes]

APPENDIX: ILLUSTRATION OF APPROACHES

The following illustration shows the differences between the amounts recognised in profit or loss and in the statement of other recognised income and expense in each of the three approaches described in agenda paper 4.

Amounts recognised in the balance sheet, profit or loss and statement of recognised income and expense

	Approach 1		**Approach 2**		**Approach 3**	
Profit and loss	20x1	20x2	20x1	20x2	20x1	20x2
Current service cost	130	140	130	140	130	140
Interest cost	100	103			100	103
Return on plan assets						
- dividends and interest income	- 90	- 100			- 90	- 100
- changes in fair value	- 41	- 12				
Actuarial gains and losses on obligation						
- arising from effect of change in discount rate	159	190				
- other actuarial gains and losses on the obligation	- 98	- 197	- 98	- 197	- 98	- 197
Expense recognised in profit or loss	160	124	32	- 57	42	- 54
Statement of recognised income and expense						
Interest cost			100	103		
Return on plan assets						
- dividends and interest income			- 90	- 100		
- changes in fair value			- 41	- 12	- 41	- 12
Actuarial gains and losses arising from effect of change in discount rate			159	190	159	190
Other recognised income and expense	0	0	128	181	118	178
Expense recognised in profit or loss for period	160	124	32	- 57	42	- 54
Total recognised income and expense for the period	160	124	160	124	160	124

Assumptions

All transactions are assumed to occur at the year-end.

Present value of obligation	20x1	20x2
Present value of obligation, 1 January	1,000	1,141
Interest cost	100	103
Current service cost	130	140
Benefits paid	- 150	- 180
Effect of change in discount rate (estimated)	159	190
Actuarial (gain) loss for year - obligation	- 98	- 197
Present value of obligation, 31 December	1,141	1,197

Fair value plan assets	20x1	20x2
Fair value of plan assets, 1 January	1,000	1,092
Contributions received	75	85
Benefits paid	- 150	- 180
Dividends and interest income	90	100
Change in fair value of plan assets	41	12
Fair value of plan assets, 31 December	1,056	1,109

In each approach, the amount recognised in the balance sheet is:

Balance sheet	20x1	20x2
Present value of the obligation	1,141	1,197
Fair value of plan assets	- 1,056	- 1,109
Liability recognised in the balance sheet	85	88