Project **Post-employment benefits**

Topic **Disclosures: New disclosures**

Objective

1. The objective of this paper is to provide an overview of the responses together with staff analysis and a staff recommendation for the following new disclosure requirements that were proposed in the ED:
   (a) information about risk, including sensitivity analysis (paragraphs 3 – 27)
   (b) disclosure about demographic assumptions (paragraphs 28 – 34)
   (c) disclosure of alternative measures of the defined benefit obligation (DBO) (paragraphs 35 – 44)
   (d) information about asset-liability matching strategies (paragraphs 45 – 53)
   (e) information about the amount, timing and uncertainty of future cash flow (paragraphs 54 – 62)
2. The staff recommends that the Board:
   (a) limit a narrative description of the extent of the risks to which the plan exposes the entity to the risks that are specific to the entity or unusual;
   (b) confirm the proposal in the ED to disclose how the effect of a change to each significant actuarial assumption that is reasonably possible at the end of the reporting period would have affected the 'defined benefit obligation';

(c) remove the proposal in the ED to disclose how the effect of a change to each significant actuarial assumption that was reasonably possible at the beginning of the reporting period would have affected current service cost;

(d) remove the proposal in the ED to disclose a brief description of the process used to determine demographic actuarial assumptions;

(e) replace the proposal in the ED to disclose the present value of the defined benefit obligation (adjusted to exclude the effect of projected growth in salaries) with the disclosure of a disaggregation of the defined benefit obligation into the vested benefits, accrued but unvested benefits, future salary increases and other conditional liabilities;

(f) confirm the proposal in the ED to disclose details of any asset-liability matching strategies used by the plan; and

(g) replace the proposal in the ED to disclose a narrative discussion of factors that could cause contributions over the next five years to differ significantly from current service cost over that period with the disclosure of:

  (i) a narrative description of any funding arrangement and funding policy, and

  (ii) the amount of expected benefit payments over the next five years and the amount of expected contribution in the next year.

Information about risk, including sensitivity analysis

3. Paragraphs 125C(b) and 125I of the ED stated:

> 125C An entity shall disclose:
>
> …
>
> (b) a narrative description of the extent of the risks to which the plan exposes the entity and of any concentrations of risk. For example, if plan assets are invested primarily in one class of investments, eg property, the plan may expose the entity to a concentration of property market risk.
>
> 125I An entity shall disclose:

(a) how the effect of a change to each significant actuarial assumption that:

   (i) is reasonably possible at the end of the reporting period would have affected the defined benefit obligation at the end of the reporting period; and

   (ii) was reasonably possible at the beginning of the reporting period would have affected current service cost that was determined for the reporting period

(b) the methods and assumptions used in preparing the sensitivity analyses required by (a) and the limitations of those methods.

(c) changes from the previous period in the methods and assumptions used in preparing the sensitivity analyses, and the reasons for such changes.

Comments received on the ED

4. Question 9(a) of the ED asked:

> To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:
>
> (a) information about risk, including sensitivity analyses (paragraphs 125C(b), 125I, BC60(a), BC62(a) and BC63–BC66);
>
> Are the proposed new disclosure requirements appropriate? Why or why not? If not, what disclosures do you propose to achieve the disclosure objectives?

5. There was much support for including disclosures about exposure to risk, however there was a mixed response for the specific sensitivity requirements proposed by the Board.

6. Some noted that the narrative disclosure about risk should be limited to any risks that are specific to the entity or unusual so that it does not result in boiler plate, irrelevant disclosure, such as 'plans offering benefits as annuities are exposed to longevity risk' or 'plan assets invested in equity instruments are subject to the corresponding market risk'.

7. There were varying levels of support for the sensitivity analysis requirements, from those that supported the requirements in full, to those that supported part of the requirements, those that would prefer if the requirements were permitted but not required or those that would prefer if the requirements would be deleted. One respondent noted that sensitivity analysis is suggested in paragraph 129(b) of IAS 1 as an example of the type of disclosure to help a user understand the 'judgments that management makes about the future and about other sources of estimation uncertainty'. This respondent supported the proposed disclosure in the ED on the basis that it was additional guidance in applying the requirements in IAS 1 to defined benefit plans.

8. Respondents noted the following concerns regarding the sensitivity disclosures:

   (a) The sensitivity disclosure would be misleading as it would not take into account the correlations between various actuarial assumptions. A few suggested that a scenario analysis would be more useful, however this would be more costly to produce.

   (b) Not providing a sensitivity analysis of plan assets will reduce the usefulness of the disclosure. There is potentially greater variability in plan assets than for the defined benefit obligation (DBO) and the sensitivity analysis for the DBO would provide more useful information if the sensitivity of plan assets to the same variables were also disclosed.

   (c) Many believed that the disclosure should be more specific to increase comparability and reduce the range and amount of sensitivities disclosed.

      (i) Some requested that the sensitivity analysis should be limited to the assumptions that have a significant effect on the financial statements.

      (ii) Some suggested that the scope of sensitivity analyses should be limited to the discount rate, which is the most relevant assumption because it is the main reason for the volatility of the DBO. They also requested that there should be no separate sensitivity analysis conducted for the service cost because, from their view, separate sensitivity analyses for the service cost would not offer enough additional useful information to justify this disclosure requirement. They noted that changes in actuarial assumptions impact not only the service cost but also other components of the total compensation.

(iii) Some raised a concern that the notion of a 'reasonably possible change' is open to subjectivity and thus suggested that a quantitative range should be set thereon.

(d) Some are concerned about the role of sensitivity analyses:

(i) in financial reporting in general, because they believe sensitivity should be disclosed outside the financial statements; and

(ii) in defined benefit plan accounting specifically, because the measurement of the DBO is based on management’s single best estimate and is not a range of possible values.

9. Many members of the EBWG raised a concern over the correlation between multiple actuarial assumptions in that it would be impracticable to capture the correlation in any sensitivity analysis and, if practicable at all, the information would be useful only for sophisticated users with actuarial background. Also, some members suggested that the sensitivity analysis should be limited to the assumptions that have a significant effect on the financial statements.

Staff analysis and recommendation

Exposure to risk

10. Paragraph BC60(a) of the ED provided the following explanation on the reason that the paragraph 125C(b) was proposed.

> *Exposure to risk (paragraph 125C(b))*: The exposure draft proposes that entities should provide a narrative description of exposure to risk arising from their involvement with the plan. This responds to the requests in the comment letters that entities should provide more disclosures about the risks inherent in a defined benefit plan and the risks associated with plan assets held to fund the benefit.

11. The staff observes that there is little challenge to that reason. However, the staff agrees with the suggestion that exposure to the risks that are specific to the entity or unusual should be disclosed because only those risks will be relevant for users to make a decision regarding that entity. Requiring disclosure of all material risks that the entity would be exposed to would result in extensive generic disclosures that would not be particularly useful.

12. Consequently, the staff recommends that the Board limit a narrative description of the extent of the risks to which the plan exposes the entity to the risks that are specific to the entity or unusual.

Sensitivity analysis

13. Paragraph BC63 of the ED provided the following explanation on the reason that paragraph 125I was proposed.

> The exposure draft proposes that entities should disclose how the effect of reasonably possible changes to significant actuarial assumptions affect the defined benefit obligation and service cost. Users of financial statements have consistently emphasised the fundamental importance of sensitivity analyses to their understanding of the risks underlying amounts included in the financial statements.

14. In developing the staff recommendation, the staff have considered the following concerns raised by respondents:

    (a) whether to require entities to provide sensitivity analysis on the net defined benefit liability (asset) or on the defined benefit obligation (paragraphs 15 – 17)

    (b) whether to require entities to provide sensitivity analysis on service costs (paragraphs 18– 20)

    (c) whether to limit the possible actuarial assumptions (paragraphs 21 – 23)

    (d) whether to specify a quantitative range of sensitivity (paragraphs 24 – 27)

Exclusion of plan assets

15. The Board proposed to limit the sensitivity analysis to the defined benefit obligation for the reasons described in paragraphs BC64-65 of the ED, which states:

> BC64 The Board considered whether to require entities to provide sensitivity analyses of the effect of changes in actuarial assumptions on the net defined benefit liability (asset). However, the Board concluded that this would be difficult to do because:
>
> (a) it is unclear how a change in market interest rates would apply to plan assets. If plan assets were invested in equities and in bonds, an analysis showing only direct effects of changes in market interest rates would show the effect on the bonds, but show no effects on the equities. This might not provide very meaningful information. On the other hand, a more complex sensitivity analysis showing the effect of changes in interest rates on equity investments would be difficult to perform because there may be no reasonable basis on which to estimate the interrelationships between interest rates, inflation rates and equity values.
>
> (b) the net defined benefit liability (asset) includes the effect of the asset ceiling. It would be difficult to determine how changes in the assumptions change the effect of the asset ceiling.
>
> BC65 Because these issues relate to the plan assets, which are measured at fair value, the exposure draft proposes to require sensitivity analyses only for the defined benefit obligation and not for the net defined benefit liability (asset).

16. The staff agrees with the views that providing a sensitivity analysis on the net defined benefit liability (asset) would be more useful than providing a sensitivity analysis on the defined benefit obligation only. However the staff does not believe this view invalidates the Board's reasons in paragraph BC64 for limiting the sensitivity analysis to the defined benefit obligation.

17. Consequently, the staff believes that the Board should not change its conclusion to exclude plan assets from the sensitivity analysis.

Inclusion of service costs

18. The Board proposed to require that entities provide a sensitivity analysis on service costs for the reasons in paragraph BC66 of the ED.

> The Board intends that the sensitivity analyses for service cost should give an indication of the variability of the service cost recognised in the statement of comprehensive income. However, service cost is determined at the beginning of the period. Some might therefore argue that there is no effect from changes in assumptions at the end of the period. Consequently the exposure draft proposes that entities should perform the sensitivity analyses for service cost using changes in assumptions that were reasonably possible at the start of the reporting period.

19. Some respondents did not see the relevance of disclosing how the effect of a change to each significant actuarial assumption that was reasonably possible at the beginning of the reporting period would have affected current service cost that was determined for the reporting period. Service cost is determined based on assumptions at the beginning of the period, and therefore the sensitivity provided is not a sensitivity of the cost during the period. The staff agrees with this view.

20. Consequently, the staff recommends that the Board remove the proposal in the ED to disclose how the effect of a change to each significant actuarial assumption that was reasonably possible at the beginning of the reporting period would have affected current service cost.

Scope of sensitivity analysis

21. Many respondents were concerned that carrying out a series of sensitivity analyses on multiple actuarial assumptions would be onerous. Many of these respondents suggested that the sensitivity analysis should be limited to the discount rate assumption (including the effect of a change in discount rate on related assumptions). These respondents noted that the discount rate:

    (a) is qualitatively different from other assumptions because it is more of a current market measure than an assumption about future events;

(b) tends to have the most significant impact on the defined benefit obligation and service cost;

(c) is likely to affect and drive other actuarial assumptions; and

(d) unlike the mortality assumption, has a significant effect even for plans that pay a lump sum at retirement.

22. The staff thinks that in most cases the discount rate will be the most significant assumption. However, depending on the plan and other facts and circumstances, other assumptions may be more significant. The ED proposed that the sensitivity analysis should apply only to 'significant actuarial assumptions'.

23. Consequently, the staff recommends that the Board confirm the proposal in the ED to disclose how the effect of a change to each significant actuarial assumption that is reasonably possible at the end of the reporting period would have affected the defined benefit obligation.

Quantitative range

24. Some suggest that the Board should specify a quantitative range for sensitivity analysis.

25. Although setting the range to a particular percentage will improve comparability, the staff is concerned that a quantitative range may not reflect the reasonably possible ranges that may vary depending on different circumstances in which entities find themselves. Furthermore, requiring users to extrapolate a sensitivity to reflect a reasonably possible range may not be ideal as the relationship may not be linear. However, setting the range based on what is reasonably possible will require users to extrapolate a sensitivity (which may not be linear) in order to compare the sensitivity of the DBO of two different entities (or two different time periods).

26. IFRS 7 *Financial Instruments: Disclosures*, which also requires the disclosure of sensitivity analysis for financial instruments, does not set a quantitative range for sensitivity analysis. Paragraph 40 of IFRS 7 states [emphasis added]:

> Unless an entity complies with paragraph 41, it shall disclose:

(a) a sensitivity analysis for each type of market risk to which the entity is exposed at the end of the reporting period, showing how profit or loss and equity would have been affected by **changes in the relevant risk variable that were reasonably possible** at that date;

(b) the methods and assumptions used in preparing the sensitivity analysis; and

(c) changes from the previous period in the methods and assumptions used, and the reasons for such changes.

27. Therefore, the staff thinks that it should be left to the entity to determine to what extent a change to the discount rate would be reasonably possible.

Question 1
Does the Board agree: (a) to limit a narrative description of the extent of the risks to which the plan exposes the entity to the risks that are specific to the entity or unusual; (b) to confirm the proposal in the ED to disclose how the effect of a change to each significant actuarial assumption that is reasonably possible at the end of the reporting period would have affected the defined benefit obligation; and (c) to remove the proposal in the ED to disclose how the effect of a change to each significant actuarial assumption that was reasonably possible at the beginning of the reporting period would have affected current service cost?

Disclosure about demographic assumptions

28. Paragraph 125G of the ED proposes:

An entity shall disclose:

(a) quantitative information about actuarial assumptions used to determine the defined benefit obligation (see paragraph 73). Such disclosure shall be in absolute terms (eg as an absolute percentage, and not just as a margin between different percentages and other variables). When an entity provides disclosures in total for a grouping of plans, it shall provide such disclosures in the form of weighted averages or relatively narrow ranges.

(b) a brief description of the process used to determine demographic actuarial assumptions to supplement the disclosures provided in accordance with (a).

Comments received on the ED

29. Question 9(b) of the ED asked respondents the following:

> To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:
>
> (b) information about the process used to determine demographic actuarial assumptions (paragraphs 125G(b) and BC60(d) and (e));
>
> Are the proposed new disclosure requirements appropriate? Why or why not? If not, what disclosures do you propose to achieve the disclosure objectives?

30. There was not much support for the requirement to disclose the process used to determine demographic assumptions. Respondents noted the following concerns:

(a) The requirement may lead to boilerplate disclosure that would not be particularly useful. The process often consists of experts performing experience studies and making professional assessments.

(b) It is not clear what disclosure objective this requirement is achieving and how this information would be used. For instance, without understanding the demographics of the members it is difficult to see a user benefiting from the disclosures.

(c) Disclosure of the assumptions should be adequate. Evaluating the process to determine the appropriate assumptions would be a normal part of an audit, and users rely on the entity, its actuaries and auditors to ensure the demographic assumptions are reasonable.

Staff analysis and recommendation

31. Paragraph BC60(e) of the ED provided the following explanation on the reason that paragraph 125G(b) was proposed.

> *Actuarial assumptions and the process used to determine them (paragraph 125G)*: The Board proposes to retain the requirement in IAS 19 for entities to provide quantified disclosures about actuarial assumptions (paragraph 125G(a)). However, the Board acknowledges that such quantified disclosures could be difficult to interpret without extensive supplementary information that would be impracticable to provide. For example, disclosure of mortality rates without supporting information could be misleading and it is not practicable for entities to provide users with the detailed knowledge about the demographic profile of a plan that would be needed to make a meaningful assessment of the information provided by disclosures of mortality rates. Therefore, the exposure draft also proposes that in those circumstances, the entity should explain how it determined those actuarial assumptions (paragraph 125G(b)). For example, if an entity has developed mortality assumptions using a standard table, it could disclose the source of that table and when it was compiled. Similarly, the entity could disclose the current estimate of the expected mortality rates of plan members.

32. Despite the reason mentioned in paragraph BC60(e) of the ED, the staff notes that many respondents questioned the objective of the proposed disclosure and were skeptical of its benefit for users of financial statements. In the light of that response, the staff thinks that the proposed disclosure either would be generic and not useful or beyond the knowledge or expertise of general purpose financial statement users to properly evaluate. In the staff's opinion it is appropriate for the audit process to include a discussion of the documentation, support, and rationale for the assumptions as opposed to general purpose financial statements.

33. The staff agrees with the views in the comment letters that disclosing the process used to determine demographic assumptions, such as mortality, would not help address the concerns the Board has that quantitative demographic assumptions would be difficult to interpret. Providing details of how those amounts were derived will not help users interpret the quantitative disclosures. Users will still not be able to make an assessment of the appropriateness of the demographic assumption unless detailed disclosures of the demographic profile are provided. Respondents noted that the example application of the disclosure requirement in

paragraph BC60(e), where an entity discloses the source of a mortality table and when it was compiled would not help users interpret the mortality assumptions any more or less.

34. Consequently, the staff recommends that the Board remove the proposal in the ED to disclose a brief description of the process used to determine demographic actuarial assumptions.

Question 2
Does the Board agree to remove the proposal in the ED to disclose a brief description of the process used to determine demographic actuarial assumptions?

Disclosure of alternative measures of the defined benefit obligation

35. Paragraph 125H of the ED stated:

> An entity shall disclose the present value of the defined benefit obligation, adjusted to exclude the effect of projected growth in salaries.

Comments received on the ED

36. Question 9(c) of the ED asked respondents the following:

> To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:
>
> (c) the present value of the defined benefit obligation, modified to exclude the effect of projected salary growth (paragraphs 125H and BC60(f));
>
> Are the proposed new disclosure requirements appropriate? Why or why not? If not, what disclosures do you propose to achieve the disclosure objectives?

37. Most respondents did not support this proposal, unless they are based in the jurisdiction (US) where a similar disclosure is already required.

38. Many stated that the proposal was not fully justified by the Board. Many noted that the relevance of such a disclosure would depend on the nature of the

benefits upon termination which would vary by country and by plan and commented that it would not be relevant in many jurisdictions. Many commented that it would be inappropriate to require a disclosure because it would be relevant to some users in very limited circumstances. The respondents who opposed this disclosure:

(a) disagreed with the presumption in BC60(f) of the ED that 'the present value of the defined benefit obligation, adjusted to exclude the effect of projected growth in salaries' is similar to the amount of the entity's obligation if the plan were to be terminated; and

(b) cautioned the Board that the disclosure of the alternative measure is likely to confuse and mislead users, undermining the credibility of the information in the statement of financial position, rather than be relevant additional information in decision-making.

39. Besides,

(a) Some pointed out that paragraph 125H does not directly relate to the disclosure objectives in paragraph 125A (specifically (b)), since it only supplements the amount of the defined benefit obligation recognised in its financial statements with an alternative measure but does not 'identify or explain' the amount recognised.

(b) Others believed that disclosing an alternative measure of the liability would contradict the measurement requirement of IAS 19.

(c) Many were not convinced that the albeit low cost of this benefit is outweighed by the limited user benefit, noting that this would apply to many other similarly low cost requirements that would just add to the volume of disclosures and only be useful in limited circumstances.

40. Some suggested that instead of the proposed disclosure, a disaggregation of the DBO would be better as it would break the amount down into parts such as the vested benefits, accrued but unvested benefits, future salary increases and other constructive obligations.

Staff analysis and recommendation

41. Paragraph BC60(f) of the ED provided the following explanation on the reason that the paragraph 125H was proposed.

> *Alternative measure of the long-term employee benefit liability (paragraph 125H)*: The Board proposes that entities should disclose the defined benefit obligation, excluding projected growth in salaries (sometimes referred to as the accumulated benefit obligation). In some circumstances, this amount is similar to the amount of the entity's obligation if the plan were to be terminated, and some users believe that is relevant additional information. Moreover, this amount is relevant to some who believe that the measurement of these liabilities should exclude projected salary growth. The elimination of the requirement to present an expected rate of return on plan assets reduces the usefulness of this disclosure because there is less subjectivity inherent in determining the amounts in profit and loss. Therefore, the Board does not think this information would be costly to provide because it uses inputs that are needed to determine the defined benefit obligation.

42. The staff agrees with respondents that it would be inappropriate to require the disclosure of the alternative measure because it would be relevant to some users in very limited circumstances.

43. Rather, the staff thinks that disaggregating the defined benefit obligation into the vested benefits, accrued but unvested benefits, future salary increases and other conditional liabilities as suggested by some respondents will produce an analytical information and might help users digest information for their own purpose. The staff believes that disclosing disaggregated information about the DBO:

    (a) will help explain the amount of the defined benefit obligation recognised in its financial statements, and thus meet one of the disclosure objectives; and

    (b) will be flexible enough to be useful under different circumstances depending on how the DBO is composed. In contrast, singling out a particular amount, such as future salary increases, for disaggregation, may not always be useful.

44. Consequently, the staff recommends that the Board replace the proposal in the ED to disclose the present value of the defined benefit obligation (adjusted to exclude the effect of projected growth in salaries) with the disclosure of a disaggregation of the defined benefit obligation into the vested benefits, accrued but unvested benefits, future salary increases and other conditional liabilities.

Question 3
Does the Board agree to replace the proposal in the ED to disclose the present value of the defined benefit obligation (adjusted to exclude the effect of projected growth in salaries) with the disclosure of a disaggregation of the defined benefit obligation into the vested benefits, accrued but unvested benefits, future salary increases and other conditional liabilities?

Information about asset-liability matching strategies

45. Paragraph 125J of the ED stated:

> 125J An entity shall disclose details of any asset-liability matching strategies used by the plan, including the use of annuities and other techniques, such as longevity swaps, to manage longevity risk.

Comments received on the ED

46. Question 9(d) of the ED asked respondents the following:

> To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:
>
> (d) information about asset-liability matching strategies (paragraphs 125J and BC62(b));
>
> Are the proposed new disclosure requirements appropriate? Why or why not? If not, what disclosures do you propose to achieve the disclosure objectives?

47. Views on the proposals regarding asset-liability matching strategies were mixed. Some supported the disclosure, others believed that it should be part of a broader

disclosure regarding risk management and investment strategy and many argued that it should be removed. Those that believed it should be part of a broader discussion about risks suggested linking the disclosure with the requirement to describe the nature of risks that the plan exposes the entity to (proposed in paragraph 125C(b) of the ED), by requiring the entity to describe how it manages those risks. Respondents also noted that the disclosure could be better integrated with the disclosures on plan assets. Respondents that did not support the asset-liability matching disclosure were concerned that:

(a) any disclosure of strategy would be generic and boilerplate;

(b) a user will be able to perform a better assessment using the disclosures on plan assets and on the defined benefit obligation (ie the results of such a strategy are more relevant than a narrative discussion); and

(c) the requirement may imply that an entity should be doing asset-liability matching.

Staff analysis and recommendation

48. Paragraph BC62(b) of the ED provided the following explanation on the reason that paragraph 125J was proposed.

> *Asset-liability matching strategies (paragraph 125J)*: Respondents suggested that entities should disclose information about their investment strategies to match plan assets to plan liabilities. The Board considered broadening this requirement so that all entities with defined benefit plans would have been required to discuss their strategies for mitigating risks arising from defined benefit plans. However, because many entities would mitigate risks arising from defined benefit plans through their investment strategies, the Board concluded that such a requirement would result in generic disclosure that would not provide enough specific information to be useful to users of financial statements. Nonetheless, the Board believes that information about an entity's use of asset-liability matching investment strategies or the use of techniques, such as annuities or longevity swaps, to manage longevity risk, would be informative. Accordingly, the exposure draft proposes a requirement to disclose information about these items.

49. In the staff's opinion, the information about the asset-liability matching strategy may provide additional information on how the risk inherent in the entity's defined benefit plan is managed and thus it will be relevant information for users.

50. The staff thinks that the asset-liability matching strategy may tell more than an investment strategy the entity has adopted on its plan assets, because it aims to match the amount and timing of cash inflow from plan assets 'in a more direct and systematic way' with those of cash outflow from the defined benefit obligation than asset allocation. For asset allocation, a qualitative information and a quantitative information are already required in paragraphs 125C(b) and 125F of the ED respectively.

51. Therefore, the staff thinks that it will result in essential information being left out or watered down to remove paragraph 125J of the ED or integrate it into paragraph 125C(b) of the ED.

52. The staff notes that the ED proposed to require the entity to disclose details of 'any' asset-liability matching strategies used by the plan and it was not meant to imply that an entity should be doing asset-liability matching.

53. Consequently, the staff recommends that the Board confirm the proposal in the ED to disclose details of any asset-liability matching strategies used by the plan.

Question 4
Does the Board agree to confirm the proposal in the ED to disclose details of any asset-liability matching strategies used by the plan?

Information about the amount, timing and uncertainty of future cash flow

54. Paragraph 125K of the ED stated:

> An entity shall provide a narrative discussion of factors that could cause contributions over the next five years to differ significantly from current service cost over that period. For example, an entity shall disclose how it expects any surplus or deficit to affect the level and timing of its contributions over the next five years, and the period over which it expects the surplus or deficit to disappear.

Comments received on the ED

55. Question 9(e) of the ED asked respondents the following:

> To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:
>
> (e) information about factors that could cause contributions to differ from service cost (paragraphs 125K and BC62(c)).
>
> Are the proposed new disclosure requirements appropriate? Why or why not? If not, what disclosures do you propose to achieve the disclosure objectives?

56. Many did not support the disclosure of factors that could cause contributions to differ significantly from current service cost. Respondents noted the following:

    (a) There are many arbitrary factors why contributions would differ from service cost. In some jurisdictions, contributions are not regulated and are totally discretionary.

    (b) The disclosure would need to be prepared based on assumptions on the future (such as the volatility of the plan assets).

    (c) There is often no direct relationship between contributions and service cost. Contributions are usually determined based on local funding requirements. The DBO is measured using a different basis under funding requirements.

    (d) This disclosure only considers funded plans and does not consider plans that are closed (ie where service cost is zero). Disclosure about future cash flows is also relevant for unfunded plans.

57. The EBWG had mixed views regarding the underlying purpose of this disclosure. Some members of the EBWG argued that more focus should be put on the future cash flow, ie establishing what will potentially change the future cash flow. Others argued that more focus should be put on the funding agreement between the employer and the fund, ie establishing what will happen if there is deficit or surplus in the fund.

Staff analysis and recommendation

58. Paragraph BC62(c) of the ED provided the following explanation on the reason that paragraph 125K was proposed.

> *Factors that could cause contributions to differ from ervice cost (paragraph 125K)*: The comment letters suggested disclosure of information about an entity's best estimate of the contributions it expects to pay to the plan during the next year, distinguishing between required contributions, discretionary contributions and non-cash contributions. However, the Board believes that information is useful if it highlights possible differences between current service cost and cash contributions in the near future. This might be the case if a surplus or deficit affects the level and timing of an entity's contributions. Therefore the exposure draft proposes disclosure of factors that could cause contributions over the next five years to differ from current service cost. The Board believes that this is more useful than merely disclosing expected payments in the next year because those payments depend partly on estimated service cost and also because mere disclosure of the amount would not indicate likely trends beyond the following year.

59. The staff notes that there is generally no direct relationship between contributions and service cost because the objectives for local funding valuations are different to the objectives for financial reporting, therefore the assumptions required for local funding valuations are often much more conservative than the 'best estimate' assumptions used for financial reporting purposes. Therefore, the staff agrees with the views that disclosure of a narrative discussion as to why contributions over the next five years to differ significantly from current service cost over that period is unlikely to provide relevant information for users of financial statements.

60. Rather, the staff observes that many respondents including members of EBWG suggested that the focus of a disclosure about the effect of a defined benefit plan on an entity's future cash flow should be placed on:

    (a) the funding arrangement and funding policy; and

    (b) the amounts of expected contributions and benefit payments.

61. In the staff's opinion, those disclosures will be more relevant for users of financial statements in identifying the risk around changes in contribution and forecasting how much cash outflow will be incurred to cover the employee benefits.

62. Consequently, the staff recommends that the Board replace the proposal in the ED to disclose a narrative discussion of factors that could cause contributions over the next five years to differ significantly from current service cost over that period with the disclosure of:

    (a) a narrative description of any funding arrangement and funding policy, and

    (b) the amount of expected benefit payments over the next five years and the amount of expected contribution in the next year.

Question 5
Does the Board agree to replace the proposal in the ED to disclose a narrative discussion of factors that could cause contributions over the next five years to differ significantly from current service cost over that period with the disclosure of: (a) a narrative description of any funding arrangement and funding policy, and (b) the amount of expected benefit payments over the next five years and the amount of expected contribution in the next year?