STAFF PAPER

18-19 September 2012

IFRS Interpretations Committee Meeting

Project	IAS 19 *Employee Benefits*		
Paper topic	Accounting for contribution-based promises		
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Introduction

1. In March 2012, the IFRS Interpretations Committee (the Committee) received a request seeking clarification on how to measure the present value of the defined benefit obligation related to what the submitter described as contribution-based promises under IAS 19 *Employee Benefits*. The submitter describes contribution-based promises in his submission as post-employment benefit promises, by which the amount of benefits received by the employee depends on the actual return generated by the contributions. These promises may or may not have a guaranteed return.

2. The submitter's understanding is that many preparers are currently accounting for contribution-based promises that provide for a minimum return according to IFRIC Draft Interpretation D9 *Employee Benefit Plans with a Promised Return on Contributions or Notional Contributions*, despite the fact that no final interpretation was issued. This is, in the submitter's opinion, because the defined benefit methodology in IAS 19 was designed for benefits that do not depend on future returns on assets, and in the absence of specific guidance on the issue, some preparers apply the draft guidance in D9 to these contribution-based promises.

3. The submitter says that the issue of the revised IAS 19 in 2011 restarted a debate on how to account for contribution-based promises. More specifically, the submitter says that some hold the view that the clarifications made in 2011 on risk-sharing features in the revised Standard may affect the accounting for contribution-based promises. This is despite the fact that there were no fundamental changes to the general methodology for measuring defined benefit obligations.

4. According to the submitter, there are two views on how to measure the present value of the defined benefit obligation related to contribution-based promises. In summary those two views are:

   (a) View 1: measure the defined benefit obligation as the whole of the expected benefit arising from the contribution-based promise, using the projected unit credit method set out in IAS 19. This is done by projecting the benefit on the basis of current assumptions of future investment performance, and discounting those amounts using the discount rate specified by IAS 19 (generally a high quality corporate bond rate).

   (b) View 2: apply the projected unit credit method set out in IAS 19 only to the part that has been guaranteed by the employer. Any surplus in the assets above the guaranteed amount is included in the measurement of the defined benefit obligation at the amount of the surplus at the reporting date, ie the employee will only obtain a right to the surplus once the benefit plan has achieved that surplus.

5. The Committee discussed this issue at the May 2012 meeting. In its discussions the Committee noted that the 2011 amendments to IAS 19, which clarified the treatment of risk-sharing features, address arrangements in which the cost of a pension promise is shared between the employee and the employer. It did not intend to address elements that are specific to contribution-based promises.

6. Accordingly, the Committee did not expect the 2011 amendments to cause changes to the accounting for contribution-based promises, unless such

promises also include elements of risk-sharing arrangements between employees and employers. The Committee also noted that the amendments in 2011 might affect how changes in contribution-based promises are presented.

7. Finally, the Committee noted that the Board expressed, in paragraph BC148 of the revised standard, that addressing concerns about the measurement of contribution-based promises and similar promises was beyond the scope of the 2011 amendments.

8. On the basis of the above, the Committee tentatively decided that it should not take this issue onto its agenda. The Committee did, however, decide to consider, at a future meeting, whether to address the accounting for contribution-based promises. Our full analysis, which was presented to the Committee meeting in May 2012, was set out in agenda paper 14[1] which can be found on the IASB's website www.ifrs.org.

9. We received four comment letters on the tentative agenda decision. We analyse the comment letters in the following paragraphs.

Comment analysis

10. All the four respondents agree with the decision not to take this issue onto the Committee's agenda. However, three of the respondents say that the Committee needs to clarify further some of its comments in the tentative decision. These are:

    (a) its inclusion of comments on risk-sharing in the tentative agenda decisions; and

    (b) that the changes to IAS 19 in the 2011 should not affect the accounting for contribution-based promises if they do not include risk-sharing arrangements.

[1] http://www.ifrs.org/Documents/141205AP14to14CIAS19.zip

Risk-sharing

11. The main problem identified by in the responses, in regard to the comments on risk-sharing, is that because ‘risk-sharing’ is not a defined term in the Standard it is therefore not clear to what this risk-sharing relates. There is therefore a need to clarify to what the risk-sharing relates and in the respondents’ opinion it would be helpful to make reference to the wording of paragraph BC144 of the revised IAS 19, specifically the statement that says “Some defined benefit plans include features that share the benefits of a surplus or the cost of a deficit between the employer and the plan participants”.

12. What also makes this unclear in the respondent’s opinion is the fact that the contribution-based promises as described in the original submission to the Committee do not include risk-sharing features as described above.

> We understand that contribution-based promises as we had described them in the potential agenda item request do not include risk-sharing features as described above. This is because all assets, including the returns generated by them, will be used to provide employee benefits so that no surplus can arise. Also, there is no risk-sharing in the context of a deficit – should the return generated on the contributions fall short of the guaranteed minimum return, the employer fully covers any balance. Put differently, there is no risk which will be shared between the employer and the plan participants.

13. Another respondent says that the tentative agenda decision can interpreted to apply only to contribution-based promises that do not contain elements of risk-sharing between the employee and the employer.

Changes in wording of IAS 19

14. One of the respondents says that although the IASB did not intend to change the accounting for contribution-based promises in the revisions to IAS 19 in 2011, the revisions may have inadvertently led to changes in the accounting

because of the changes that were made to paragraph 88(c) of IAS 19 and paragraphs BC143(c) and BC148.

The tentative agenda decision also states that the IASB did not intend to change the accounting for contribution-based promises arrangements. We are concerned that the accounting for many of the plans addressed by IFRIC D9 might have been changed inadvertently by some additional wording included in the 2011 amendments to IAS 19 and that the Board's intention is therefore not relevant. Paragraph 88(c) if IAS 19 now states, "The measurement of the obligation reflects the best estimate of the effect of the performance target or other criteria". This suggests that the measurement of the defined benefit obligation should reflect the present value of benefits to be paid on the basis of expected returns. This would be a change for those entities that have previously applied the guidance in IFRIC D9.

The basis for conclusions in paragraph BC143(c) now states that "any conditional indexation should be reflected in the measurement of the defined benefit obligation, whether the indexation or changes in benefits are automatic or are subject to a decision by the employer, the employee or a third party, such as trustees or administrators of the plan". Paragraph BC148 also states that "In the Board's view, projecting the benefit on the basis of current assumptions of future investment performance (or other criteria to which the benefits are indexed) is consistent with estimating the ultimate cost of the benefit, which is the objective of the measurement of the defined benefit obligation, as stated in paragraph 76". Both these statements appear to preclude applying the guidance in IFRIC D9.

Other matters

15. One respondent also thinks that the comments on presentation of contribution-based promises in the tentative agenda decision need further clarification.

16. Finally, one of the respondents expresses support for the reconsideration of the accounting for employee plans with a promised return on contributions and notional contributions, which were originally explored in draft interpretation D9.

17. The staff agrees that a further clarification is needed on what kind of risk-sharing the Committee was referring to in the tentative agenda decision. A description of risk-sharing arrangements described in IAS 19 and discussed by the Committee is added to the revised agenda decision in appendix A.

18. As to whether the changes in wording of IAS 19 in 2011 should affect the accounting for contribution-based promises, the staff think that in principle the changes in wording made by the revisions should not result in changes to how these promises are accounted for as IAS 19 already used best estimate in the measurement approach and the changes made in 2011 we made to make that clearer, not to change the accounting.

19. Consequently, we think that the wording of the tentative agenda decisions should be revised only to address the concerns raised on risk-sharing.

Staff recommendation

20. Given the support for the tentative agenda decision, we recommend that the Committee should finalise its decision not to add this issue to its agenda. However, on the basis of the comment analysis above, we propose changes to the wording of the tentative agenda decision as illustrated in Appendix A to this paper.

Question for the Committee

Question for the Committee—final agenda decision
Does the Committee agree with the staff recommendation?

Appendix A—Proposed wording for final agenda decision

A1. The staff propose the following wording for the final agenda decision (new text is underlined and deleted text is struck through):

IAS 19 *Employee Benefits*—Accounting for contribution-based promises – Impact of the 2011 amendments to IAS 19

The Committee received a request seeking clarification about the accounting in accordance with IAS 19 (2011) for contribution-based promises. An underlying concern in the submission was whether the revisions to IAS 19 in 2011, which for example clarified the treatment of risk-sharing features related to defined benefit obligations, affect the accounting for contribution-based promises.

The Committee noted that the 2011 amendments to IAS 19~~,~~ that clarified the treatment of risk-sharing features (described in paragraph BC144 as features that share the benefits of a surplus or the cost of deficit between the employer and the plan participants or benefit plans that provide benefits that are conditional to some extent whether there are sufficient assets in the plan to fund them) ~~address arrangements in which the cost of the pension promise is shared between the employee and the employer~~. It did not intend to address elements specific to contribution-based promises. Accordingly, the Committee does not expect the 2011 amendments to IAS 19 to cause changes to the accounting for contribution-based promises~~.~~ unless those contribution-based promises also include similar risk-sharing arrangements. ~~The Committee also noted that the amendments in 2011 might affect how changes in contribution-based promises are presented.~~ Finally, the Committee noted that the Board expressed, in paragraph BC148 of the revised standard, that addressing concerns about the measurement of contribution-based promises and similar promises was beyond the scope of the 2011 amendments.

On the basis of the analysis described above, the Committee ~~[~~decided~~]~~ not to add the issue to its agenda, it will however decide, at a future meeting, whether to address the accounting for contribution-based promises (see Committee work in progress below).