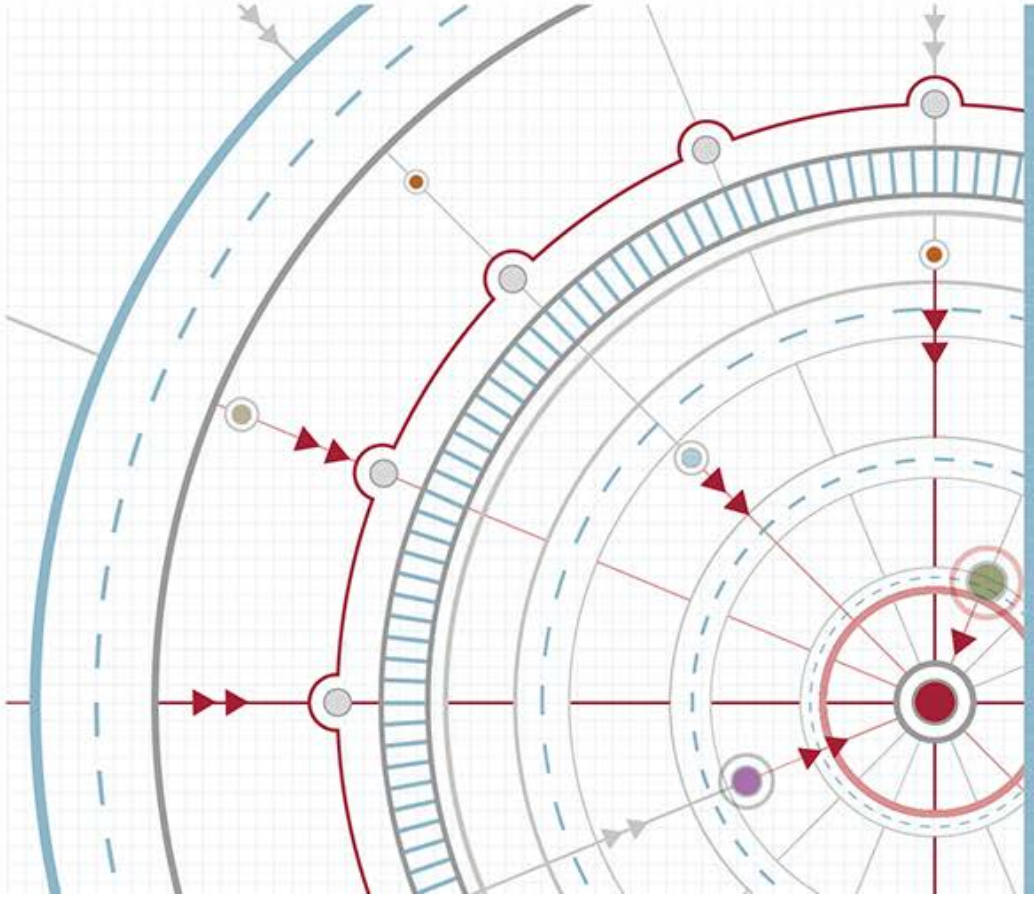
IFRS® Foundation

Agenda Paper 7



Targeted Standards-level Review of Disclosures

Joint CMAC-GPF Meeting

June 2019

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Purpose of this session

- For GPF and CMAC members to discuss example disclosures that might be used to satisfy user objectives relating to IAS 19 *Employee Benefits* and IFRS 13 *Fair Value Measurement.*
- We would like members' views on:

1. Whether the example disclosure is effective in meeting the stated objective? **[CMAC members]**
   i. How critical is the information to you?
   ii. Is it presented and disaggregated in a helpful way? If not, what changes would you make and why?

2. How costly would the disclosure be to prepare? **[GPF members]**

3. Are there any alternative disclosures that would meet the objective and/or be less costly to prepare? **[CMAC and GPF members]**

4. Overall, does this disclosure pass the cost-benefit test? **[CMAC and GPF members]**

Breakout discussion

Background

- Staff have prepared examples of the following disclosures:

For defined benefit plans …	
1	Expected contributions into the plan **and** expected future benefit payments from the plan
2	Wider sensitivity analysis of significant actuarial assumptions
3	Information about differences between defined benefit plan valuations
4	Reconciliation from opening to closing balance of the net defined benefit liability (asset)

For fair value measurement …	
1	Additional disclosures for Level 2 fair value measurements
2	Explanation of how an entity has determined the level to which its assets and liabilities belong
3	Wider sensitivity analysis of Level 3 fair value measurements
4	Reconciliation from opening to closing balance of Level 3 fair value measurements

- We will ask each break out group to prioritise two items to discuss in detail (see **slide 4**) and then use any remaining time to discuss the others. The breakout discussion will be based on the detailed example(s) for each disclosure in the subsequent slides.

Breakout discussion

- Four breakout sessions with a mix of users and preparers.
- We would like each break-out group to prioritise discussion of the following examples:

Group 1	Group 2	Group 3	Group 4
1. Explanation of how an entity has determined the level to which its assets and liabilities belong—slides 22-23	1. Expected contributions into the plan **and** expected future benefit payments from the plan—slides 12-13	1. Wider sensitivity analysis of significant actuarial assumptions—slide 14	1. Additional disclosures for Level 2 fair value measurements—slides 19-21
2. Wider sensitivity analysis of Level 3 fair value measurements—slides 24-25	2. Reconciliation from opening to closing balance of the net defined benefit liability (asset)—slide 17	2.Information about differences between defined benefit plan valuations—slides 15-16	2. Reconciliation from opening to closing balance of Level 3 fair value measurements—slide 26

Background

Project background

The issue

There are three main concerns about disclosures in financial statements:

- not enough relevant information
- too much irrelevant information
- ineffective communication of the information provided

Project objective and focus

To help stakeholders improve the usefulness of disclosures for the primary users of financial statements:

develop guidance for the way the Board develops and drafts disclosure objectives and requirements in *future*

use IAS 19 *Employee Benefits* and IFRS 13 *Fair Value Measurement* to test the draft Guidance

Project timeline

2018

March … **May - Sep** **Nov - March**

Project added to agenda in response to Discussion Paper

- Board developed draft guidance
- IAS 19 and IFRS 13 selected to test the draft Guidance

Meetings with users to understand their objectives and ideal information set(s)

2019

March … June … Dec

- Meetings with consultative groups and other stakeholders
- Board discussion on feedback

Board technical decisions

2020

Publish exposure draft

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Past discussion with CMAC and GPF

- At the separate March 2019 meetings of CMAC and GPF:
  - We sought members' views on the feedback from our outreach with users about employee benefits and fair value measurement disclosures.
  - CMAC members provided feedback on whether they agreed with user objectives and their suggested items of information that could be used to meet those objectives.
  - GPF members shared their views on costs and other consequences of the suggested items of information.
- The Board discussed feedback received at those meetings in May 2019. (May 2019 Agenda Paper 11B and Agenda Paper 11C).

May Board Meeting

- Board members shared their views on factors they will need to consider when analysing the feedback received. These include:

Employee Benefits	What is within the remit of IFRS Standards? For example, is it appropriate for IFRS Standards to require: ✓ forward looking information (such as expected future contributions); ✓ information about alternative valuations (such as funding valuations).
Fair Value Measurement	Whether existing IAS 1 requirements already address some of the feedback? For example: ✓ is explanation of how an entity determines the level to which its assets and liabilities belong already captured by the requirement to disclose information about significant estimates and judgements?

Today's discussion

- In future meetings, the Board will discuss potential amendments to the disclosure sections of IAS 19 and IFRS 13.
- The staff will use feedback from today's meeting to help develop recommendations and detailed analysis in preparation for those Board discussions.
- Staff have prepared examples of disclosures to facilitate discussion:

Employee Benefits *Focus: Defined Benefit Plans*	Slides 11-17
Fair Value Measurement	Slides 18-26

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IAS 19 *Employee Benefits*

Examples for discussion

1a Expected contributions into the plan

User objective	• Expected contributions (as agreed with trustees or internally budgeted by management) would allow users to better evaluate the impact of the obligation on cash flows. ✓ The information is considered more useful if it differentiates between 'ordinary' (payroll deductions) contributions and other contributions to reduce existing deficit.

Example disclosure

The Group has agreed a funding plan with the Plan Trustees that addresses the funding deficit over a maximum period of 15 years. The funding deficit as at 30 June 2017 was £8.6 billion demonstrating that the market value of the plan assets are not sufficient to meet the expected future benefit payments. The deficit will be met over a period of 10 years. The deficit contributions have three components:

- payments *by the Group* over 3 years to March 2020 totalling £2,100 million. £850 million of this was paid in March 2018 and the remaining £1,250 million is to be paid by March 2020.
- a further £2,000 million is due to be contributed by March 2019 from the *proceeds of the issuance of bonds* which will be held by the Group.
- for the 7 years from April 2021 to March 2027, the Group will make annual payments of around £900 million.

The Group is scheduled to make future deficit payments to the pension scheme in line with the table below:

Year to 31 March	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Deficit Contribution (£m)	850	2,000	1,250	900	900	907	907	907	907	907

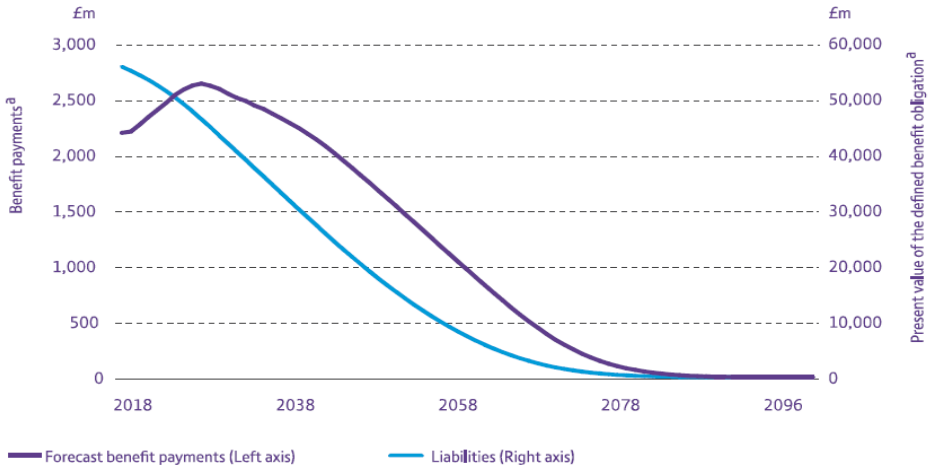
Ordinary cash contributions to the scheme of £264 million have been made in the current year, £303 million will be made in 2019 and then rising by 3% per annum to 2027.

1b Expected future benefit payments from the plan

User objective	• Users want to understand the time period over which the remaining obligations are expected to wind down and the associated expected payments.

Example disclosure

The Group's defined benefit plans are closed to new members. The estimated duration of the pension scheme liabilities, which is an indicator of the weighted average term of the liabilities, is around 16 years although the benefits payable by the scheme are expected to be paid over more than 70 years. The chart below illustrates the estimated benefits payable from the pension scheme using the IAS 19 assumptions:



£m	Total
Number of plan participants	293,000
Actual benefit payments 2018	£ 2,315
Benefits expected to be paid 2019	2,320
Benefits expected to be paid 2020	2,355
Benefits expected to be paid 2021	2,378
Benefits expected to be paid 2022	2,410
Benefits expected to be paid 2023	2,437

2 Wider sensitivity analysis of significant actuarial assumptions

User objective	• Users want to understand the range of values within which the defined benefit obligation might fall to determine appropriate adjustments for risk in their analysis. ✓ This is especially important for assumptions that do not move in a linear fashion[1].

Example disclosure

This sensitivity analysis is *wider* than todays' typical disclosure because it:

- ✓ covers *interrelationships* between the key assumptions; and
- ✓ displays *more than one deviation* from the base case assumptions.

The defined benefit obligation as of December 31, 2018 was £115,357 million. The significant assumptions used to measure the liabilities are shown below:

At 31 Dec	%
Discount rate	2.65
Rate of increase in pensions	2.50

The sensitivity of significant assumptions upon the defined benefit obligations are detailed below. Sensitivities are calculated by changing the two significant assumptions simultaneously:

		Rate of increase in pensions		
		-1%	**2.5%**	+1%
Discount Rate	-100 basis points	£74,123.57	£123,539.28	£172,954.99
	2.65%	£69,214.22	**£115,357.03**	£161,499.84
	+100 basis points	£64,672.98	£107,788.29	£150,903.61

[1] That is, when the change in those assumption is not proportional to the resulting change in the defined benefit obligation.

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3 Information about differences between defined benefit plan valuations

User objective	
	• *If* plan valuations other than the IAS 19 valuation are described in the financial statements, users find it difficult to understand how and why they differ from the IAS 19 valuation. • An explanation of the difference between the IAS 19 valuation and other valuations will help users to determine, and forecast, the obligation they incorporate in their analysis.

Example disclosure

Buyout valuation (emphasis added on the suggested additional explanation to provide)

The most recent full actuarial valuation of the Plan's liabilities, obtained by the Trustee, was carried out at 31 March 2016 by the Plan's independent actuary. The result of this valuation is shown below:

£million	March 2016
Value of buyout liabilities	(214)
Value of buyout assets	95.6
Deficit	(118.4)

The buyout valuation uses the fair value of the defined benefit plan assets (adjusted for theoretical wind-up expenses) to measure the buyout assets. Although the defined benefit obligation recognised in the financial statements (the accounting valuation) and the buyout liabilities are calculated similarly, the assumptions used for each differ, primarily in respect of retirement ages and discount rate. The buyout liabilities, due to the assumption that each plan is terminated on the valuation date, do not reflect assumptions about future compensation levels whereas the obligation on the basis of the accounting valuation does. The buyout basis reflect composite weighted average discount rates of 3.00% while the discount rate used for the accounting valuation is based on high quality (AA) corporate bond yields of an appropriate return.

3 Information about differences between defined benefit plan valuations (continued)

Example disclosure

Funding valuation (emphasis added on the suggested additional explanation to provide)

The pension scheme is subject to a full actuarial valuation every three years using assumptions agreed between the Trustee and the Group. The purpose of this valuation is to design a funding plan to ensure that the pension scheme has sufficient funds available to meet future benefit payments. The results of the two most recent triennial valuations are shown below:

£m	March 2016	March 2013
Scheme liabilities	(4,856)	(4,009)
Market value of scheme assets	4,377	3,169
Funding deficit	(479)	(840)
Percentage of accrued benefits covered by scheme assets	90%	79%

The valuation calculated under the funding valuation basis of £479.0m is different from the accounting valuation which is presented on the Balance Sheet of £468.1m (at 26 January 2019). Differences arise between the funding valuation and accounting valuation, mainly due to the use of different assumptions to value the liabilities and changes in market conditions between the two valuation dates, of 31 March 2016 and 26 January 2019. For funding valuation purposes, the liabilities are determined based on assumptions set by the Trustee following consultation with the Group and scheme actuaries. The discount rate used for the most recent funding valuation is based on index linked gilt yields plus 1.6%. The discount rate used for the accounting valuation is based on high quality (AA) corporate bond yields of an appropriate return.

4 Reconciliation from opening to closing balance of the net defined benefit liability (asset)

User objective

- Users want to identify amounts to investigate further or adjust for in analysis. However,
  - ✓ some want the whole reconciliation; while
  - ✓ some others are *only* interested in contributions and benefit payments during the period.

Example disclosure

(i) Movements in the scheme surpluses and deficits

Movements in the pension schemes' surpluses and deficits comprise:

2018	Fair Value of Scheme Assets £m	Present Value of defined benefit obligation £m	IAS 19 Pensions net surplus/ (deficits) £m
Net IAS 19 surplus in the schemes at 1 January	18,678	(16,043)	2,635
Past service costs – amendments[1]	—	(63)	(63)
Administrative expenses[2]	—	(19)	(19)
Total pension cost charged to net operating expenses	—	(82)	(82)
Net interest credited/(charged) to investment income/(finance costs)[3]	442	(375)	67
Total recognised in income	442	(457)	(15)
Remeasurements:			
Actual return on these assets	(182)	—	(182)
Less: Interest income on scheme assets	(442)	—	(442)
Return on scheme assets excluding amounts in interest income	(624)	—	(624)
Gains from change in financial assumptions	—	622	622
Losses from change in demographic assumptions	—	(185)	(185)
Experience losses	—	(93)	(93)
Total recognised in other comprehensive income	(624)	344	(280)
Acquisitions	87	(96)	(9)
Employer contributions	236	—	236
Plan participant contributions	9	(9)	—
Benefits paid	(724)	724	—
Administrative expenses paid from scheme assets[2]	(23)	19	(4)
Foreign exchange rate movements	2	(2)	—
Net IAS 19 surplus in the schemes at 31 December	18,083	(15,520)	2,563

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IFRS 13 *Fair Value Measurement*

Examples for discussion

1 Additional disclosures for Level 2 fair value measurements

User objective

- Users want to understand the sensitivities of Level 2 items and assess the appropriateness of the inputs, techniques and amounts underlying their measurement.
  - ✓ For some entities, including many banks, their most significant assets and liabilities are categorised as Level 2.

Example disclosure

The table below shows the movement between the opening and closing balances of the fair values at Level 2:

£ million	2018	2017
Balance at 1 January	**3,674**	**2,883**
Purchases	30	551
Sales	(273)	(16)
Transfer from Level 1 to Level 2	30	-
Transfer from Level 3 to Level 2	18	37
Realised gain included in profit or loss	50	10
Unrealised loss included in profit or loss	-	-
Unrealised gain/(loss), net, included in other comprehensive income	367	209
Balance at 31 December	**3,896**	**3,674**

Reconciliation

Additional disclosures for Level 2 (continued)

Example disclosure

Sensitivity analysis

Determination of fair value of financial instruments.

Level 2 fair values of investments have been generally derived using the Market approach. Below is a table showing the sensitivity analysis of material unquoted investments categorised as Level 2 fair values

Investment	Fair value at 21 December 2018 £'000	Valuation technique	Observable inputs	Fair value of inputs increased by 5% £'000	Fair value of inputs decreased by 5% £'000	Relationship of observable inputs to fair value
Investments in A	637,875	Fair value through quoted share price as at last trade date	'Share price from last trade No of units owned by the Group'	669,769	605,981	The higher the share price as at the last traded date, the higher the fair value
Investments in B	49,876			52,583	47,377	
Investments in C	98,835			103,777	93,893	
Investments in D	282,508	Fair value through quoted unit price as at last trade date	'Unit price from last trade No of units owned by the Group'	296,633	268,382	The higher the unit price as at the last traded date, the higher the fair value

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Additional disclosures for Level 2 (continued)

Example disclosure

Valuation and processes and techniques

Valuation approach for Level 2 fair valued assets and liabilities

A significant proportion of the Group's level 2 assets are corporate bonds, structured securities and other non-national government debt securities. These assets, in line with market practice, are generally valued using independent pricing services or third-party broker quotes. These valuations are determined using independent external quotations from multiple sources and are subject to a number of monitoring controls, such as monthly price variances, stale price reviews and variance analysis on prices achieved on subsequent trades.

Pricing services, where available, are used to obtain the third-party broker quotes. Where pricing service providers are used, a single valuation is obtained and applied.

When prices are not available from pricing services, quotes are sourced directly from brokers. The Group seeks to obtain a number of quotes from different brokers so as to obtain the most comprehensive information available on their executability. Where quotes are sourced directed from brokers, the price used in the valuation is normally selected from one of the quotes based on a number of factors, including the timeliness and regularity of the quotes and the accuracy of the quotes considering the spreads provided. The selected quote is the one which best represents an executable quote for the security at the measurement date.

Generally, no adjustment is made to the prices obtained from independent third parties. Adjustment is made in only limited circumstances, where it is determined that the third-party valuations obtained do not reflect fair value (e.g. either because the value is stale and/or the values are extremely diverse in range). These are usually securities which are distressed or that could be subject to a debt restructure or where reliable market prices are no longer available due to an inactive market or market dislocation. In these instances, prices are derived using internal valuation techniques. The techniques used require a number of assumptions relating to variables such as credit risk and interest rates. Examples of such variables include an average credit spread on the corporate bond universe and the relevant duration of the asset being valued. The Group determines the input assumptions based on the best available information at the measurement dates.

Of the total level 2 debt securities of £115,141 million at 31 December 2017 (2016: £116,257 million), £13,910 million are valued internally (2016: £12,708 million). The majority of such securities are valued using matrix pricing, which is based on assessing the credit quality of the underlying borrower to derive a suitable discount rate relative to government securities of a comparable duration. Under matrix pricing, the debt securities are priced taking the credit spreads on comparable quoted public debt securities and applying these to the equivalent debt instruments factoring in a specified liquidity premium. The majority of the parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

2 Explanation of how an entity has determined the level to which its assets and liabilities belong

User objective	• Users want to understand how an entity has assessed the boundaries between the levels of the fair value hierarchy—i.e., which level does an instrument belong in? ✓ An entity-specific explanation is especially important for complex financial instruments or where judgment has been applied.

Example disclosure

Determination of fair value

The determination of fair value requires judgment and is based on market information, where available and appropriate. The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

…continued

2 Explanation of how an entity has determined the level to which its assets and liabilities belong

...continued

Example disclosure

At the end of each reporting period, management estimates the fair value of investments based on the criteria below and reflects such valuations in the financial statements.

i. Securities including shares, options and warrants which are traded in an active market, such as on a recognized securities exchange and for which no sales restrictions apply, are presented at fair value based on quoted closing trade prices at the end of the reporting period or the closing trade price on the last day the security traded if there were no trades at the end of the reporting period. These are included in Level 1 of the fair value hierarchy (see Note 6).

ii. For options, warrants and conversion features which are not traded on a recognized securities exchange, no market value is readily available. When there are sufficient and reliable observable market inputs, a valuation technique is used. Valuation models such as the Black-Scholes valuation model ("Black-Scholes") and the Monte Carlo simulation ("Monte Carlo") are used when there are sufficient and reliable observable market inputs. These market inputs include risk-free interest rate, exercise price, market price at the date of valuation, expected dividend yield, expected life of the instrument and expected volatility of the underlying security based on historical volatility. These are included in Level 2 of the fair value hierarchy (see Note 6).

iii. Convertible debts and loans issued by investee companies are generally valued at the price at which the instrument was issued. The Company regularly considers whether any indications of deterioration in the value of the underlying business exist, which suggest that the debt instrument will not be fully recovered. The fair value of convertible debentures is measured using valuation techniques such as Black-Scholes and Monte Carlo.

The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment and assumptions provided by management is required in establishing fair values. Judgments include consideration of inputs such as credit risk, discount rates, volatility, probability of certain triggering events, and share price of private company borrowers. Changes in assumptions relating to these factors could affect the reported fair value of the financials instruments. These are included in Level 3 of the fair value hierarchy (see Note 6).

3 Wider sensitivity analysis of Level 3 fair value measurements

User objective	• Users want to understand the range of values within which the entity's fair value measurement might fall. ✓ This is especially important for assumptions that do not move in linear fashion[2].

Example disclosure

Positive and negative fair value movements of Level 3 financial instruments from using reasonably possible alternative assumptions

A financial instrument is classified as Level 3 in the fair value hierarchy if one or more of its unobservable inputs may significantly affect the measurement of its fair value. In preparing the financial statements, appropriate levels for these unobservable input parameters are chosen so that they are consistent with prevailing market evidence or management judgment. Due to the unobservable nature of the prices or rates, there may be uncertainty about the valuation of these Level 3 financial instruments.

The following table summarizes the impacts to fair values of Level 3 financial instruments using reasonably possible alternative assumptions. This sensitivity disclosure is intended to illustrate the potential impact of the relative uncertainty in the fair value of Level 3 financial instruments. In reporting the sensitivities below, we offset balances in instances where: (i) the move in valuation factors cause an offsetting positive and negative fair value movement, (ii) both offsetting instruments are in Level 3, and (iii) exposures are managed and reported on a net basis. With respect to overall sensitivity, it is unlikely in practice that all reasonably possible alternative assumptions would simultaneously be realized.

…continued

[2] That is, when the change in those assumption is not proportional to the resulting change in the far value measurement.

3 Wider sensitivity analysis of Level 3 fair value measurements

…continued

Example disclosure

This sensitivity analysis is *wider* than todays' typical disclosure because it:

- ✓ covers the key *inputs simultaneously*; and
- ✓ displays *more than one deviation* from the recognised fair value.

	IFRS 9			IAS 39		
	As at					
	October 31, 2018			October 31, 2017		
(Millions of Canadian dollars)	Level 3 fair value	Positive fair value movement from using reasonably possible alternatives	Negative fair value movement from using reasonably possible alternatives	Level 3 fair value	Positive fair value movement from using reasonably possible alternatives	Negative fair value movement from using reasonably possible alternatives
Securities						
Trading						
U.S. state, municipal and agencies debt	$ 66	$ –	$ (1)	$ –	$ –	$ –
Asset-backed securities	110	7	(10)	–	–	–
Corporate debt and other debt	21	–	–	29	–	–
Equities	1,148	12	(12)	425	–	–
Investment						
U.S. state, municipal and agencies debt	–	–	–	508	8	(20)
Asset-backed securities	–	–	–	203	15	(21)
Corporate debt and other debt	192	19	(16)	797	6	(6)
Equities	237	24	(26)	711	40	(24)
Loan substitute securities	–	–	–	4	2	–
Loans	551	5	(7)	179	2	(3)
Derivatives	577	20	(18)	747	34	(30)
Other assets	65	–	–	–	–	–
	$ 2,967	$ 87	$ (90)	$ 3,603	$ 107	$ (104)
Deposits	$ (385)	$ 12	$ (11)	$ (465)	$ 11	$ (11)
Derivatives	(1,143)	47	(54)	(1,378)	37	(48)
Other						
Other liabilities	(68)	–	–	(24)	–	–
	$ (1,596)	$ 59	$ (65)	$ (1,867)	$ 48	$ (59)

4 Reconciliation from opening to closing balance of Level 3 fair value measurements

User objective

- Users want to identify amounts to investigate further or adjust for in analysis. However:
  - ✓ some want the whole reconciliation; while
  - ✓ some others are *only* interested in line items representing transfers into and out of Level 3.

Example disclosure

(g) Further information on Level 3 assets and liabilities:

The table below shows movement in the Level 3 assets and liabilities measured at fair value.

	Assets										Liabilities
2018	Investment Property £m	Loans £m	Debt securities £m	Equity securities £m	Other investments (including derivatives) £m	Financial assets of operations classified as held for sale £m	Non participating investment contracts £m	Net asset value attributable to unitholders £m	Derivative liabilities £m	Borrowings £m	Financial liabilities of operations classified as held for sale £m
Opening balance at 1 January 2018	10,797	23,949	15,137	776	2,863	2,093	—	(13)	(358)	(1,180)	(3,306)
Total net gains/(losses) recognised in the income statement[1]	376	(530)	(363)	(102)	(69)	(73)	—	—	(136)	(81)	74
Purchases	1,185	3,451	3,175	189	1,761	201	(108)	—	(59)	—	(95)
Issuances	—	200	—	—	—	—	—	—	—	—	—
Disposals	(927)	(2,065)	(1,221)	(544)	(554)	(191)	108	(12)	20	36	189
Transfers into Level 3	—	—	1,242	95	77	20	—	—	—	—	(20)
Transfers out of Level 3	—	—	(503)	(2)	—	(58)	—	—	—	—	58
Reclassification to held for sale	—	—	—	—	—	—	—	—	—	—	—
Foreign exchange rate movements	51	3	111	2	29	—	—	—	(1)	—	—
Balance at 31 December 2018	11,482	25,008	17,578	414	4,107	1,992	—	(25)	(534)	(1,225)	(3,100)

1 Total net gains/(losses) recognised in the income statement includes realised gains/(losses) on disposals.

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Feedback from breakout discussions

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