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Sir David Tweedie
Chairman of the
International Accounting Standards Board
30 Cannon Street

London EC4M 6XH
United Kingdom

Düsseldorf, July 30, 2004
541/511/520

Dear Sir David

**Re.: Exposure Draft of Proposed Amendments to IAS 19 Employee Benefits: Actuarial Gains and Losses, Group Plans and Disclosures**

We are pleased to have the opportunity to comment on the Exposure Draft mentioned above and would like to submit our comments as follows:

## Actuarial Gains and Losses

We disagree with the Board's belief, as stated in IN3, that a third option should be available as an alternative to deferred recognition or immediate recognition in profit or loss at this point in time. In our opinion, it is imperative that a sound framework for accounting for employee benefit obligations be determined as well as completion of the project on "Reporting Comprehensive Income" prior to effecting significant revisions to isolated areas of the standard. In our comment letter regarding the IASC Foundation Constitution Review dated February 13, 2004 we have previously argued the need for each IFRS to be robust so as to remain valid for an extended period and for subsequent changes to be kept to an absolute minimum. We explain further reasons for our opinion as follows:

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- *Comparability*

We have serious reservations as to the wisdom of introducing a third option because this decreases the comparability of financial statements for which the IASB strives. Concerning this matter it has to be brought to mind that one of the objectives of the IASB's improvements project was to reduce or eliminate alternatives.

- *Recognition of actuarial gains or losses outside profit and loss*

We agree that the recognition of actuarial gains and losses in full as they occur and hence recognition of the entire pension benefit obligation in the balance sheet provides a more faithful representation of the entity's financial position at the balance sheet date than deferred recognition. We also agree that it is not appropriate to recognize actuarial gains and losses in full in profit or loss for the period in which they occur since this would cause volatile fluctuations of profit or loss (see the arguments presented in BC6). In our view these fluctuations would contradict the objective to give a fair presentation of the entity's performance particularly because changes in the financial position induced by changes of market interest rates would be recognized for pension liabilities whereas corresponding changes of the values of other balance sheet items (e.g. intangibles, property, plant and equipment) are not recognized. In order to avoid this mismatch-problem the Board concluded that actuarial gains and losses should be recognised outside profit and loss directly in the retained earnings and that they should not be recycled to profit or loss.

We do not agree with these proposals. In our view, it is not acceptable for elements of income to be shown directly and definitely as inclusion within retained earnings. The presentation of retained earnings implies that there has been a prior effect on profit or loss, which is not the case if the method proposed by the Board would be applied. In this context the Board states that the issue of recycling must be resolved in the project on reporting comprehensive income. In our opinion this project has to be finalized before a new approach for recognition of actuarial gains and losses can be introduced. Otherwise there would be a lack of conceptual basis if an isolated solution would be established in IAS 19.

Furthermore it has to be mentioned that accounting for employee benefits is an important issue for convergence with US GAAP. Thus, care must be taken that a new solution in IFRS is in line with US GAAP.

- *Corridor approach*

Until the issues mentioned above are resolved in the project on reporting comprehensive income the current corridor approach should be retained as the only alternative to full recognition of changes in actuarial gains and losses in the income statement.

In accordance with the accrual basis of accounting the income statement should ideally reflect the costs of future pensions during the period the individual is actually working. Given stable levels of staff turnover and salary increments, under the going concern premise, these costs would not normally be particularly volatile from year to year, as pension obligations are long-term and therefore normally would follow a general trend rather than being affected by any large temporary swings in the financial markets. In putting forward the current proposals the Board is however following the alternative "balance sheet oriented approach" under which liability values are calculated as a priority and the full obligation at balance sheet date is to be recognised on the face of the balance sheet and changes of this obligation are to be reflected in comprehensive income.

We would like to question the Board's contention in IN2 that deferred recognition "results in amounts presented in the balance sheet that do not meet the definition of an asset or a liability" and would refer to paragraph 64 of the framework which clarifies that a pension obligation is a liability. The issue in question is rather one of measurement. Actuarial gains and losses are changes in accounting estimates actually and, therefore, should be recognised prospectively by including them in profit or loss in the period of the change and future periods, if the change affects both. In our view, the user of financial statements is not given information that is more useful if significant volatility is introduced into the measurement of a long-term liability as it may be ultimately settled in an entirely different amount. However, we agree that the user should have access to such information by means of disclosure in the notes.

Therefore, in our opinion the current corridor approach provides adequate recognition of employers' obligations, as its application results in an acceptable estimate of the long-term liabilities avoiding the impact of excessive volatility and does not result in excessive volatility in respect of the entities results. Further relevant information is provided as note disclosures.

### Disclosures

The financial impacts of risks need to be understandable and assessable to the users of financial information. We therefore support the proposals for an enhanced disclosure of employer obligations for employee benefits which increases the transparency and enhances the users understanding of both the nature of and the economic effects of employee benefit plans. In this respect we also support convergence with US GAAP.

However, as currently drafted, paragraph 120 does not provide guidance as to how entities are to disclose more than one pension plan. It is not clear whether plans can be grouped together or have to be disclosed individually. The latter could lead to an excessive volume of disclosure resulting in an informational overload detrimental to usefulness. Furthermore, in our view the disclosure requirements in paragraph 121 are too widely drafted in stipulating “<u>all the terms</u> of the plan that are used in the determination of the defined benefit obligation”, as it cannot realistically be deemed necessary for users to be given all the information to enable them to calculate the liabilities themselves. Therefore, paragraph 121 should be clarified in this respect.

We would be pleased to answer any questions that you may have or discuss any aspect of this letter.

Yours sincerely

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