The South African Institute of Chartered Accountants

CL 56

31 July 2004

Ms Anne McGeachin
Project Manager
International Accounting Standards Board
30 Cannon Street
London EC 4M 6XH
United Kingdom

Email: CommentLetters@iasb.org.uk

Dear Ms McGeachin

EXPOSURE DRAFT OF PROPOSED AMENDMENTS TO IAS 19 *EMPLOYEE BENEFITS – ACTUARIAL GAINS AND LOSSES, GROUP PLANS AND DISCLOSURES*

In response to your request for comments on the Exposure Draft of *Proposed Amendments to IAS 19 Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures*, attached please find the comment letter prepared by the South African Institute of Chartered Accountants (SAICA). Please note that SAICA is not only a professional body, but is also secretariat for the Accounting Practices Board, which is the official standard-setting body in South Africa.

We would like to thank you for the opportunity to provide comments on this document.

Please do not hesitate to contact us should you wish to discuss any of our comments.

Yours sincerely

Desrae Lawrence
Project Director – Small and Medium Enterprises

cc: Doug Brooking (Chairman of the Accounting Practices Board)
Geoff Everingham (Chairman of the Accounting Practices Committee)

SAICA COMMENT ON PROPOSED AMENDMENTS TO IAS 19 EMPLOYEE BENEFITS – ACTUARIAL GAINS AND LOSSES, GROUP PLANS AND DISCLOSURES

GENERAL COMMENTS

1. SAICA is not in agreement with the proposed changes to IAS 19 in respect of actuarial gains and losses and would prefer these changes to be deferred until discussions have taken place under the Comprehensive Income Project. We believe that the IASB should not be issuing ad hoc interim changes whenever a problem relating to a standard arises, but rather propose that the relevant standard be comprehensively reviewed. The reasons for our disagreement with the proposed changes to IAS 19 are as follows:

   - The addition of a third option defeats the IASB's objective to reduce options.
   - The option appears to be a step towards full recognition of the benefit liability. This is achieved in relation to the balance sheet, but the income statement impact has been disregarded.
   - The recognition of actuarial gains and losses in a separate statement of recognised income and losses in a specified format, as well as the inclusion of these amounts in retained income, is not considered acceptable. Accounting standards generally do not specify which category of equity should be used. Furthermore, the proposed amendment to IAS 1 - *Presentation of Financial Statements*, should rather be dealt with in a holistic manner via the Comprehensive Income Project.
   - The exposure draft does not indicate a preference between options and the extent to which an entity can switch from one option to another is unclear. It is possible that entities could change their policy depending on whether the amount is a gain or loss. In addition, this proposed option will reduce comparability of financial information.
   - The proposed option negatively affects the objective of global convergence of accounting standards as it creates further divergence with US GAAP.

2. Should the IASB decide to address the problem with deferred recognition of actuarial gains and losses in IAS 19, we believe that consideration should be given to providing the following options:

   - Immediate recognition of actuarial gains or losses in profit or loss.
   - Recognition of actuarial gains or losses in equity and the recycling of these in profit or loss at a later period.

   This approach would address the concern of presenting amounts in the balance sheet that do not meet the definition of an asset or liability. It would also address the concern in connection with permanently excluding amounts from the income statement if the option proposed in the exposure draft is used, and thereby reducing the comparability of financial information. The elimination would also do away with the current 'corridor method' that is both complex to apply and confusing to users.

3. We are in agreement with the proposed extension of the provisions in IAS 19 relating to multi-employer plans for use in the separate or individual financial statements of entities within a consolidated group. However, we do not agree with the criteria listed in paragraph 34, as these are different from the criteria applied when a parent does not need to present consolidated financial statements (IAS 27 – *Consolidated Financial Statements and Accounting for Investment in Subsidiaries).*

   It is our view that defined benefit plans that pool assets contributed by various entities under common control, for example a parent and its subsidiaries, should be treated as multi-employer plans.

4. The additional disclosures proposed were considered to be acceptable.

SPECIFIC COMMENTS ON QUESTIONS RAISED

Question 1 - Initial recognition of actuarial gains and losses

IAS 19 requires actuarial gains and losses to be recognised in profit or loss, either in the period in which they occur or on a deferred basis. The Exposure Draft proposes that entities should also be allowed to recognise actuarial gains and losses as they occur, outside profit or loss, in a statement of recognised income and expense.

Do you agree with the addition of this option? If not, why not?

We do not agree with an additional recognition option for actuarial gains and losses in post-employment defined benefit plan. The reasons for this are as follows:

- An additional option is less likely to achieve comparability over time as an entity could switch from one option to another, depending on its positive or negative effect in a financial year.
- The consequential amendment of IAS 1, through the inclusion of a statement of recognised income and expenses presented in a statement of changes in equity is not seen as a necessary change. In addition, the recognition of actuarial gains and losses in a specified format of the statement in changes in equity as well as the required inclusion of these amounts in retained income, is not considered acceptable. Accounting standards generally do not limit options provided for in another accounting standard regarding formats that can be used, nor specify which category of equity should be used for various amounts.
- The proposed option further reduces convergence with US GAAP.

Question 2 - Initial recognition of the effect of the limit on the amount of a surplus that can be recognised as an asset.

Paragraph 58(b) of IAS 19 limits the amount of a surplus that can be recognised as an asset to the present value of any economic benefits available to an entity in the form of refunds from the plan or reductions in future contributions to the plan (the asset ceiling).

The Exposure Draft proposes that entities that choose to recognise actuarial gains and losses as they occur, outside profit or loss in a statement of recognised income and expense, should also recognise the effect of the asset ceiling outside profit or loss in the same way, i.e. in a statement of recognised income and expense.

Do you agree with the proposal? If not, why not?

We agree that this proposal is logical and in line with the proposals in the exposure draft. However, please note our comments in Question 1.

Question 3 – Subsequent recognition of actuarial gains and losses.

The Exposure Draft proposes that, when actuarial gains and losses are recognised outside profit or loss in a statement of recognised income and expense, they should not be recognised in profit or loss in a later period (i.e. they should not be recycled)

Do you agree with this proposal? If not, why not?

We have concerns with this proposal. It is our view that, should the IASB decide to address the problem with deferred recognition of actuarial gains and losses in IAS 19, consideration should be given to the standard only allowing the option of immediate recognition in profit or loss or the recognition of actuarial gains or losses in equity and the recycling of these in profit or loss at a later period. This will ensure comparability of financial information over time in that amounts will be always be included in the income statement, albeit in different periods. This would also be consistent with the treatment with that contained in other standards as regards items deferred in an equity category. In addition, it is argued that these gains and losses meet the definition of income and expenses as contained in the framework and so should accordingly be included in the income statement.

It is appreciated that the present method of amortising actuarial gains or losses to the income statement might be based on a fairly arbitrary period. The option we proposed of deferral and recycling also has pitfalls in that there are no rules controlling the process of recycling and a manipulated profit and loss could result. This is why we believe that the standard should be comprehensively reviewed rather than altered on an ad hoc basis.

Question 4 – Recognition within retained earnings.

The Exposure Draft also proposes that, when actuarial gains and losses are recognised outside profit or loss in a statement of recognised income and expense, they should be recognised immediately in retained earnings, rather than recognised in a separate component of equity and transferred to retained earnings in a later period.

Do you agree with this proposal? If not, why not?

We disagree with the proposal of requiring the recognition of actuarial gains and losses only in retained income. A particular class of equity should not be specified for this purpose as this is not required in other accounting standards. If the amounts are to be recycled through the income statement in the future it would be useful for such amounts to be recognised in a separate component of equity, in a manner similar to the fair value gains and losses on available-for-sale financial assets.

Question 5 – Treatment of defined benefit plans for a group in the separate or individual financial statement of the entities in the group.

(a) The Exposure Draft proposes an extension of the provision in IAS 19 relating to multi-employer plans for use in the separate or individual financial statements of entities within a consolidated group that meet specific criteria.

Do you agree with this proposal? If not, why not?

We agree with the proposal to extend the provisions in IAS 19 relating to multi-employer plans for use in the separate or individual financial statements of entities within a consolidated group. However, we wish to note that, in our view, defined benefit plans that pool assets contributed by various entities under common control, for example a parent and its subsidiaries, should be treated as multi-employer plans. Accordingly we believe that the first sentence of paragraph 34 should be amended to this effect and the wording added to this paragraph and paragraph 34A is not required.

(b) The Exposure Draft sets out criteria to be used to determine which entities within a consolidated group are entitled to use those provisions.

Do you agree with the criteria? If not, why not?

We do not agree with the criteria specified in paragraph 34 of IAS 19 as it is different from the criteria for which a parent does not need to present consolidated financial statements under IAS 27 – *Consolidated Financial Statements and Accounting for Investments in Subsidiaries.* There should be a broader set of criteria which should comply with the IFRIC D6 principles applicable to all multi-employer plans.

Question 6 – Disclosures.

The Exposure Draft proposes additional disclosures that (a) provide information about trends in the assets and liabilities in the defined benefit plan and the assumptions underlying the components of the defined benefit cost and (b) bring the disclosures in IAS 19 closer to those required by the US standard SFAS 132 Employers' Disclosures and Pensions and Other Postretirement Benefits.

Do you agree with this proposal? If not, why not?

We agree with the proposal that long-term trends should be disclosed. There should however be relief for first time adopters. We would prefer that paragraph 120(n) make reference to the *"most sensitive element"* rather than only specifying *"medical costs"* in order for the disclosure to be relevant in the particular circumstances. The proposed wording only affects post-retirement medical funds, whereas we believe it should also be required for other defined benefit plans.

Question 7 – Further disclosures.

Do you believe that any other disclosures should be required, for example the following disclosures required by SFAS 132? If so, why?

(a) a narrative description of investment policies and strategies;

(b) the benefits expected to be paid in each of the next five fiscal years and in aggregate for the following five fiscal years; and

(c) an explanation of any significant change in plan liabilities or plan assets not otherwise apparent from other disclosures.

SFAS 132 also encourages disclosure of additional asset categories if that information is expected to be useful in understanding the risks associated with each asset category.

In our view this disclosure would be acceptable as it will further assist users in understanding the information presented in the financial statements.

OTHER COMMENTS

1. In paragraph 120(c) it is not clear whether *"service cost"* differs from *"current service cost"* and whether this is net of *"contributions by plan participants"* or not. We suggest these issues be clarified.

2. It is our view that the word *"high inflation"* in paragraph 120(n) should be changed to *"hyperinflation"* as this is consistent with the terminology used elsewhere in the IFRS.

3. In paragraph 120(o) an explanation should be disclosed if the present value of the obligation and the fair value of the assets have changed significantly as a result of business combinations, discontinued operations, curtailments, settlements or changes to benefits.

4. It is our view that paragraph 120(p) should refer to *"the next financial year"* rather than *"the next fiscal year"*.