



<b>To:</b>	<b>AASB Members</b>	<b>Date:</b>	2 September 2009
<b>From:</b>	<b>Dean Ardern</b>	<b>Agenda Item:</b>	13.1
<b>Subject:</b>	<b>Issues raised by constituents during the AASB roundtables on ED 179 <i>Superannuation Plans and Approved Deposit Funds</i></b>	<b>File:</b>	P19

## Action

For information only.

## Background

AASB roundtable discussions on the proposals in ED 179 *Superannuation Plans and Approved Deposit Funds* were held in Sydney on Wednesday 26 August 2009 and in Melbourne on Friday 28 August 2009. A list of the attendees at each of the roundtables is provided in Appendix A to this Agenda Paper.

Consistent with the approach adopted in other AASB roundtable discussions held recently, a number of participants were asked to lead the discussion on particular topics. The topics discussed were:

- (a) preparation and presentation of consolidated financial statements;
- (b) insurance contracts;
- (c) defined benefit obligations;
- (d) presentation of financial statements; and
- (e) disclosure of segregated information.

To facilitate discussions, AASB staff developed several questions on each topic. Some of these questions were based on issues raised in the Specific Matters for Comment section in ED 179. The remainder were developed from discussions with constituents in other forums attended by AASB staff in which ED 179 was discussed. Prior to the AASB roundtables, AASB staff attended a number of forums on ED 179 hosted by industry participants, including the Australian Institute of Superannuation Trustees, Ernst and Young and PricewaterhouseCoopers. Appendix B to this

Agenda Paper contains the questions and supporting material provided to participants in the AASB roundtables.

## **AASB Roundtables**

The following discussion provides a high level summary of the issues raised by participants in the AASB roundtables on ED 179.

### ***Preparation and presentation of consolidated financial statements***

While some participants noted that the superannuation industry still regards consolidated financial reporting as a contentious issue, most agreed that:

- (a) consolidated financial reporting is a fact of life in the context of general purpose financial reporting; and
- (b) is appropriate in most circumstances where a superannuation entity holds a controlling interest in another entity, particularly a special purpose entity.

Nevertheless, some participants raised concerns regarding the implications of preparing consolidated financial statements, including:

- (a) the usefulness of consolidated financial information for members. Some participants noted that, unlike shareholders in a company, members of a superannuation plan do not necessarily have a notional interest in each of the assets held by the plan. In addition, some members may have no investment exposure to subsidiaries because these types of investments tend to be in the nature of private equity and are not actively chosen as investment options by members. Accordingly, users experience difficulties in reconciling the assets presented in a plan's statement of financial position with the particular investment options offered by the plan;
- (b) the requirement to consolidate subsidiaries where:
  - (i) control is transitory;
  - (ii) the superannuation plan's ownership interest fluctuates around 50% as a consequence of the investment decisions of other investors; and/or
  - (ii) the information needed to prepare consolidated financial statements is not available; and

- (c) the manner in which the concept of control is interpreted. Some participants noted that control is sometimes interpreted in terms of a quantitative threshold rather than a qualitative threshold, and this can raise issues in circumstances where, for instance, a superannuation plan holds a significant interest in a wholesale trust but lacks the required level of ownership to affect a change in the management of the trust.

Accordingly, some participants suggested that ED 179 should include additional guidance to that which is currently provided in Australian Accounting Standards to assist superannuation entities in dealing with these issues.

With regards to the proposal that parent superannuation entities separately recognise any internally generated intangible assets, internally generated goodwill, contingent assets or contingent liabilities that are attributable to a subsidiary and arise subsequent to the subsidiary's acquisition by the parent, most participants agreed that goodwill (both acquired and internally generated) is generally not material for parent superannuation entities. However, most participants agreed that the amount of net assets reported in the parent's statement of financial position should be the same as the amount of net assets reported in the consolidated statement of financial position.

Accordingly, most participants favoured goodwill on consolidation being treated as a 'balancing' or 'plug' item because splitting the item up into its identifiable components would impose additional preparation and audit costs on parent entities and provide little or no benefits to users.

### ***Insurance contracts***

Most participants agreed that the insurance arrangements a superannuation plan offers its members could expose the plan to risks, including insurance risk and credit risk. However, many participants expressed concerns with the proposal that, where significant, superannuation entities quantify such risks and recognise them as liabilities.

Several participants argued that insurance risks are unlikely to be material in the context of the overall risks faced by superannuation plans. These participants suggested that the risks associated with:

- (a) insurance arrangements backed by group life policies would be limited to the credit risk and operational risk of the reinsurer and any risks associated with the plan administering the policy (such as the risk of higher than expected claims administration expenses). However, the risks attributable to reinsurers might be significant in some circumstances, including:

- (i) where the reinsurer is domiciled overseas and subject to less stringent capital requirements than insurers domiciled in Australia;
  - (ii) the plan's excesses and/or the reinsurers deductibles under the group policy leave the plan exposed to some or all of the its members' insurance claims; and/or
  - (iii) the reinsurer is in 'run off' and is unwilling to pay claims;
- (b) 'self-insured' arrangements would include the credit risk of the employer sponsor, particularly where there exists a shortfall in the amount of assets necessary to meet members' benefits, including insurance benefits.

A number of participants also expressed concerns regarding some of the potential financial reporting implications of a superannuation plan recognising any obligations and assets arising from the insurance arrangements it offers its members, including:

- (a) 'self-insurance' arrangements are relatively common among public sector superannuation plans and these types of plans are often funded by the government on a 'pay-as-you-go basis'. Accordingly, if these types of plans were required to recognise obligations arising from self-insurance arrangements, they would appear to users to be in an unsatisfactory financial position. (It is relevant to note that the recognition of insurance obligations would not necessarily cause such plans to appear to be in an unsatisfactory financial position. Many of these plans already appear to be in unsatisfactory financial positions as a consequence of them holding little or no assets and recognising members' benefits as liabilities.) In addition, the government's obligation to fund such insurance arrangements is generally included in the government's net defined benefit liability recognised under AASB 119 *Employee Benefits*; and
- (b) while a superannuation plan would recognise all of its insurance obligations under the proposals, it would presumably only be permitted to recognise those reinsurance assets that it has a contractual right to receive. Accordingly, the plan might appear insolvent to some users, despite the plan having a reasonable expectation of receiving reinsurance receipts as and when claims are approved.

The participants noted that any need to recognise liabilities and assets arising from insurance contracts would depend on the facts and circumstances in each situation. In addition, most participants agreed that, if the replacement Standard for AAS 25 *Financial Reporting by Superannuation Plans* required obligations and assets arising from insurance contracts to be

measured in accordance with principles and requirements applicable to life insurance contracts under AASB 1038 *Life Insurance Contracts*, the replacement Standard should provide guidance on:

- (a) the types of circumstances in which a superannuation plan would be exposed to significant insurance risk;
- (b) the specific principles and requirements in AASB 1038 that would potentially apply to a superannuation plan with significant insurance risk; and
- (c) how a superannuation plan with significant insurance risk might measure the obligations and assets arising from the insurance arrangements it provides to its members in accordance with AASB 1038.

### ***Defined benefit obligations***

Some participants noted that measuring obligations for defined benefit members' benefits at the amount of such members' vested benefits is arguably inconsistent with the going concern assumption. However, most participants consider vested benefits to be a more appropriate measure of a superannuation plan's obligation for defined benefit members' benefits than accrued benefits because:

- (a) most members understand what vested benefits are (it is reported in their member statements) but have less understanding of what accrued benefits are and what they mean in the context of a superannuation plan's financial position;
- (b) accrued benefits are relevant to an employer sponsor that has promised a future benefit but arguably less relevant to a superannuation plan that is limited in its legal obligation to members to the amount of its assets;
- (c) requiring obligations for defined benefit members' benefits to be measured at the amount of such members' accrued benefits would cause some plans to recognise deficits in respect of these members, even when the members' benefits are fully funded on an appropriate actuarial basis. In addition, some participants noted that requiring obligations to defined benefit members to be measured at the amount of such members' accrued benefits might compel some employer sponsors to terminate their defined benefit arrangements rather than make additional contributions to eliminate any deficiency;

- (d) the proportion of defined benefit members' benefits that are fully vested has increased over time and is likely to continue to increase. Consequently, the difference between the amount of such members' vested and accrued benefits has narrowed, especially for members of plans that are closed to new defined benefit members (which is the majority of defined benefit plans in Australia); and
- (e) not all superannuation plans with defined benefit members have employer sponsors that apply AASB 119. Accordingly, the benefits associated with aligning the measurement requirements for accrued benefits with the requirements applicable to defined benefit obligations under AASB 119 are unlikely to be significant for these superannuation plans

Accordingly, most participants favoured the replacement Standard for AAS 25 requiring obligations for defined benefit members to be measured at the amount of such members' vested benefits and, if necessary, the amount of such members' accrued benefits should be disclosed in the notes.

Participants noted, however, that if the replacement Standard for AAS 25 required obligations for defined benefit members' benefits to be measured at the amount of such members' accrued benefits, they would favour accrued benefits being measured on exactly the same basis as defined benefit obligations are measured under AASB 119. Participants favoured the same measurement requirements for defined benefit obligations and defined benefit members' accrued benefits for a number of reasons, including:

- (a) it would avoid confusion among users that might arise from the recognition of different amounts for the same defined benefit obligation in the employer sponsor's and superannuation plan's financial statements; and
- (b) requiring superannuation plans to apply a modified version of the approach under AASB 119 would impose additional preparation and audit costs on all plans with defined benefit members. However, requiring superannuation plans to measure defined benefit members' accrued benefits in accordance with the requirements applicable to defined benefit obligations under AASB 119 would impose no significant additional costs on superannuation plans that have employer sponsors that apply AASB 119.

Participants also noted that:

- (a) the benefits of defined benefit members in Australia are not subject to externally imposed requirements, such as the level of state retirement benefits. Superannuation arrangements

that include externally imposed requirements are more likely to be found in jurisdictions where minimum superannuation entitlements are not provided;

- (b) ‘higher of’ benefit options are usually measured at their intrinsic value under AAS 25 as:
  - (i) the difference between the defined benefit members’ accrued benefits and their account balances when the account balances are greater than accrued benefits; and
  - (ii) at nil when the account balances are less than accrued benefits; and
- (c) requiring a superannuation plan to measure and recognise separately a ‘host promise’ and any ‘higher of’ option would impose costs on the plan without a commensurate increase in the usefulness of the plan’s financial statements.

### ***Presentation of financial statements***

Participants were generally supportive of the proposal for a statement of changes in member benefits. However, some participants were concerned that five separate statements (income statement, statement of financial position, statement of cash flows, statement of member benefits and statement of changes in equity) would be excessive and that four financial statements might be sufficient to present the same information. Accordingly, some participants suggested that the statement of changes in member benefits could be merged with:

- (a) the statement of changes in equity because equity in a superannuation plan would normally be relatively small (in many cases immaterial) and in most cases would comprise reserves which will ultimately be used for the benefit of defined contribution members; or
- (b) the income statement to provide a ‘comprehensive’ income statement that distinguishes revenues and expenses from contributions and benefit payments.

Other participants suggested that the information in a statement of changes in member benefits and/or a statement of changes in equity could be disclosed in a note.

Some participants also expressed concerns with the proposal that a difference between a superannuation plan’s or approved deposit fund’s total assets and total liabilities be presented in the statement of financial position. These participants noted that presenting such a difference in the financial statements might be misleading in circumstances where, for instance, a plan has several groups of defined benefit members and the difference is attributable to only one of these groups. Accordingly, these participants suggested that the statement of net assets in AAS 25 be retained and plans and funds should be required to provide note disclosures explaining, among

other things, any surpluses or deficiencies in relation to particular groups of members and, if applicable, the members of the plan or fund as a whole.

## *Disclosure of segregated information*

Several participants noted that the proposals in relation to segregated information could facilitate the provision of information that is useful for users, particularly defined benefit members.

However, many participants expressed concerns that the proposals would:

- (a) make a superannuation plan's note disclosures excessively long and complex, thereby diminishing their usefulness to users; and/or
- (b) not facilitate the disclosure of information that would assist users in understanding the overall financial performance and financial position of a superannuation plan that 'pools' all of its assets for investment purposes and comprises groups of members with different entitlements.

Participants noted that some superannuation plans, particularly master trusts, might have in excess of one hundred 'sub-plans'. Accordingly, preparing note disclosures explaining the financial performance and financial position of each of these 'sub-plans' at each reporting date is likely to be onerous for these types of entities. Participants also noted that the disclosure of segmented information under the proposals would be made more difficult and lead to more complex disclosures by these types of plans in circumstances where:

- (a) a significant proportion of the plans' expenses, including administration, actuarial and some investment expenses, is not able to be reliably attributed to particular sub-plans; and
- (b) the trustee of the plan uses a single investment manager for some or all of its member investment options (for instance, 'Balanced', 'Growth', 'Conservative' and 'Cash' options) and evaluates separate financial information about each investment option/manager regularly for the purpose of assessing performance and allocating resources.

Some participants expressed agreement with the principle underlying the segmented information disclosure proposals, particularly if the proposals facilitated improved disclosures about the risks that attach to different groups of members. However, most of these participants suggested that the proposals might not always facilitate such risk-based disclosures, particularly when the plan:

- (a) pools all of its assets for investment purposes; and

- (b) comprises different groups of members and some or all of these groups are entitled to different types of benefits, which imply different types and levels of risks (for instance, defined benefit, defined contribution and pension members).

Accordingly, participants argued that the existence of pooled groups of assets is not an appropriate basis for the disclosure of segmented information in all circumstances. In addition, any alternative principle would need to be capable of facilitating the disclosure of cost-beneficial information. Some participants suggested separate quantitative disclosures based on defined contribution and defined benefit groupings might be sufficient for some users. Other participants suggested that qualitative disclosures regarding, for instance, whether all of the plan's assets are available to fund all members' entitlements and how the trustee manages these arrangements might be a more appropriate approach.

## Appendix A – Attendees at the AASB Roundtables on ED 179 *Superannuation Plans and Approved Deposit Funds*

Attendees at the AASB Roundtable held in Sydney on 26 August 2009

Name	Institution/Affiliation
Senthamangalam Venkatramani	Australian Prudential Regulation Authority
Geoff Steele	Australian Prudential Regulation Authority
Diane Somerville	Deloitte Touche Tohmatsu/Institute of Actuaries of Australia
Richard Rassi	Deloitte Touche Tohmatsu
Keith Reilly	Grant Thornton
Andrew Reeves	KPMG
Dianne McHugh	NSW Treasury
Claire Keating	PricewaterhouseCoopers
Claire Locke	ICAA
Robert Hodge	Association of Superannuation Funds of Australia
Kevin Stevenson	AASB
Victor Clarke	AASB
Robert Williams	AASB
Angus Thomson	AASB
Dean Ardern	AASB

Attendees at the AASB Roundtable held in Melbourne on 28 August 2009

Name	Institution/Affiliation
Denis Thorn	Ernst and Young
Mark Shying	CPA Australia
Paul Vascotto	Australian Institute of Superannuation Trustees
Anna Adamidis	ICAA
Sean Hill	KPMG
Amy Jewel	KPMG
David Knox	Mercer
Paul Shallue	Mercer
David Coogan	PricewaterhouseCoopers
Natalie Gallery	Queensland University of Technology
Gerry Gallery	Queensland University of Technology
Al Fedone	SuperPartners
Andrew Boal	Watson Wyatt
Philip Collins	Watson Wyatt
John Rodd	Equisuper
Noelle Kelleher	Deloitte Touche Tohmatsu
Kevin Stevenson	AASB
John O'Grady	AASB
Bruce Porter	AASB
Angus Thomson	AASB
Dean Ardern	AASB
Chris Pang	AASB

## Appendix B – Questions and Supporting Material Provided to Participants in the AASB Roundtables

### 1. Preparation and presentation of consolidated financial statements

Paragraph 30 of ED 179 *Superannuation Plans and Approved Deposit Funds* proposes that a parent superannuation plan or parent approved deposit fund prepare and present consolidated financial statements in accordance with AASB 3 *Business Combinations* and AASB 127 *Consolidated and Separate Financial Statements*, except that in preparing its consolidated financial statements the parent shall:

- (a) measure all of the assets and liabilities of a subsidiary that are recognised in the statement of financial position (except for tax balances) at their fair values adjusted for transaction costs at the end of the reporting period. Tax balances shall be measured in accordance with AASB 112 *Income Taxes*;
- (b) recognise any difference between:
  - (i) the sum of the parent's interest and the non-controlling interests in the subsidiary at the end of the reporting period; and
  - (ii) the amount of the net assets of the subsidiary that are recognised by the parent at the end of the reporting period;  
as goodwill or a remeasurement gain; and
- (c) present:
  - (i) any goodwill in the statement of financial position at the end of the reporting period; and
  - (ii) any remeasurement gain in the income statement in the period in which it occurs.

As a consequence of the consolidation proposals in ED 179, a parent plan or parent fund would recognise in its consolidated financial statements:

- (a) all of the assets and liabilities recognised by the subsidiary at the end of the reporting period in accordance with Australian Accounting Standards; and
- (b) all of the identifiable but not recognised assets and liabilities of the subsidiary at its acquisition date, including internally generated intangible assets and contingent liabilities.

Accordingly, the parent plan or deposit fund would, for instance, separately recognise an intangible asset that had been internally generated by the subsidiary prior to the subsidiary's acquisition by the parent, but would not separately recognise an intangible asset that had been internally generated by a subsidiary subsequent to the subsidiary's acquisition by the parent.

However, any goodwill or remeasurement gain recognised on consolidation by the parent would comprise movements in the values of any assets and liabilities of the subsidiary that have arisen subsequent to the date of the subsidiary's acquisition and are not permitted to be recognised under Australian Accounting Standards, including:

- (a) internally generated brands, mastheads, publishing titles, customer lists and items similar in substance;
- (b) internally generated goodwill;
- (c) contingent assets; and

- (d) contingent liabilities.

## Question 1.1

Are there any significant practical difficulties inhibiting the preparation of consolidated financial statements in accordance with ED 179? If so, describe the nature of these difficulties and how they might be overcome.

## Question 1.2

Should the replacement Standard for AAS 25 *Financial Reporting by Superannuation Plans*:

- (a) permit or require separate recognition of an acquiree's intangible assets, contingent assets and/or contingent liabilities that have arisen subsequent to the acquiree's date of acquisition?
- (b) require any excess of the amount of net assets of a subsidiary recognised by the parent over the sum of the parent's and non-controlling interests in the subsidiary to be treated as a remeasurement gain?

## **2. Insurance contracts**

ED 179 proposes that obligations and assets arising from insurance contracts issued by a superannuation plan would be measured by the plan in accordance with the principles and requirements applicable to life insurance contracts under AASB 1038 *Life Insurance Contracts*.

### Question 2.1

Apart from 'self-insurance' arrangements, whereby the plan assumes responsibility for any insurance benefits payable to members and the trustee pays insurance benefits to members out of the plan's assets, what other types of arrangements would expose plans to insurance risk? How prevalent are these arrangements among Australian plans?

### Question 2.2

Are there any significant practical difficulties that would inhibit the reliable measurement of obligations and assets arising from insurance contracts in accordance with the principles and requirements applicable to life insurance contracts under AASB 1038? If so, describe the nature of these difficulties and how they might be overcome.

## **3. Defined benefit obligations**

ED 179 proposes that a superannuation plan:

- (a) recognise defined benefit members' accrued benefits as a liability; and
- (b) measure the accrued benefits of defined benefit members in manner consistent with the approach under AASB 119 *Employee Benefits* for measuring defined benefit obligations, except that:
  - (i) expected administration costs would not be included in the measurement of defined benefit members' accrued benefits;
  - (ii) if a plan's benefit formula prescribes that members accrue materially higher levels of benefits as they near retirement age, rather than attribute benefits to reporting periods on a straight-line basis, the plan would attribute member benefits to reporting periods on a basis appropriate to the plan's circumstances; and

- (iii) expected future benefit payments would be discounted for the time value of money using a risk-free discount rate based on current observable, objective rates that relate to the nature, structure and terms of the obligations for future payments.

ED 179 makes no specific proposals regarding the treatment of ‘higher of’ benefit option. A ‘higher of’ benefit option arises as a consequence of members being entitled to the higher of a defined benefit entitlement and a contributions-based amount upon their retirement from full-time employment or other event that qualifies as a condition for releasing superannuation benefits to members. Nevertheless, the AASB agreed that ED 179 should seek input from constituents on the accounting for ‘higher of’ benefit options.

### Question 3.1

Do you agree with the overall objective of ED 179 to more closely align the treatment of defined benefit obligations recognised in the statements of financial position of employer sponsors and plans? If not, why not?

### Question 3.2

Do you agree with proposed exceptions (items (i), (ii) and (iii) above) to the approach required under AASB 119 for measuring defined benefit obligations? If not, why not?

### Question 3.3

Are you aware of any plans that have defined benefit members whose level of benefits could be altered by externally imposed requirements (such as the level of state retirement benefits)? If so, what is the nature of these requirements and how are they currently being accounted for under AAS 25?

### Question 3.4

Should a ‘higher of’ benefit option be recognised separately from a defined benefit obligation? If so, how might the option be measured and recognised? If not, why not?

## **4. Presentation of financial statements**

ED 179 proposes that a superannuation plan or approved deposit present, among other things:

- (a) a statement of changes in member benefits; and
- (b) any difference between the plan’s or fund’s total assets and its total liabilities (including defined contribution members’ vested benefits, defined benefit members’ accrued benefits and any obligations to employer sponsors) as equity in accordance with applicable Australian Accounting Standards.

### Question 4.1

Do you agree with the proposal that a plan or fund present a statement of changes in member benefits? If not, why not?

### Question 4.2

Do you agree that any difference between a plan’s or fund’s total assets and total liabilities:

- (a) should be presented in the statement of financial position? If not, why not?
- (b) would be equity as defined in Australian Accounting Standard? If not, why not?

## 5. Disclosure of segregated information

Paragraph 36 of ED 179 proposes that a superannuation plan or approved deposit fund disclose information that provides users with a basis for understanding how the plan or fund arranges and manages assets attributable to different groups of members, and the related obligations to those members. In addition, for a plan or fund that manages its assets on a 'segregated' basis, paragraph 40 of ED 179 proposes that the plan or fund disclose information that provides users with a basis for understanding:

- (a) the type and nature of the assets within each segregated group of assets;
- (b) the financial performance and financial position of each segregated group of assets; and
- (c) the significant financial risks to which each segregated group of assets is exposed when the levels of such risks differ materially from the levels of the corresponding risks at the entity level.

### Question 5.1

The disclosure proposals in paragraph 40 of ED 179 and paragraphs AG77 – AG88 of Appendix B to ED 179 arguably presume that most of the risks associated with a plan holding the benefits of two or more distinct member groups, particularly groups of defined benefit members, derive from the risks attributable to the assets, including liquidity risk and market risk. Are you aware of any situations where this is not the case? For instance, where significant uncertainty surrounds the amount of a defined benefit member future entitlements and this uncertainty makes it difficult to reliably calculate the future benefits.

### Question 5.2

Are you aware of any significant practical difficulties that would inhibit a plan or fund disclosing information in relation to any segregated groups of assets attributable to different groups of members, and the related obligations to those members? If so, describe the nature of these difficulties and how they might be overcome.