

Department of Treasury and Finance

**ED187 sub 8**



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Mr Kevin Stevenson  
Chairman  
Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
MELBOURNE Vic 8007

Dear Mr Stevenson

### EXPOSURE DRAFT 187 DISCOUNT RATE FOR EMPLOYEE BENEFITS

The Heads of Treasuries Accounting and Reporting Advisory Committee welcomes the opportunity to provide comments to the Australian Accounting Standards Board on ED 187 *Discount Rate for Employee Benefits (proposed amendments to AASB 119)*.

HoTARAC supports the AASB's tentative decision to retain Paragraph Aus78.1 of AASB 119 *Employee Benefits* for the not-for-profit public sector but believes that the application of the Paragraph should be expanded to all entities.

In HoTARAC's opinion, the government bond rate is conceptually superior to high quality corporate bonds. The principles set out in AASB 119 *Employee Benefits* Paragraphs 79 to 80 to determine the discount rate require the discount rate to reflect the time-value of money, but not risks such as actuarial or investment risk, or entity-specific credit risks. For the Australian economy, it is generally accepted that the government bond rate is the best indicator of a risk-free rate, as high quality corporate bonds typically include a higher element of risk.

HoTARAC is also not convinced that the proposed amendments will achieve the level of consistency the IASB would like. The application of the principles and approach in IAS 39 *Financial Instruments: Recognition and Measurement* and subsequently the *Fair Value Measurement* Standard (presently an Exposure Draft) will result in judgement being applied to determine the discount rate. Inevitably, judgement will lead to different rates being applied across jurisdictions, industries and entities. With the AASB previously stating that Australia does not have adequate high quality corporate bonds to apply the rate, an even greater amount of judgement will need to be applied by Australian entities.

From a practical point of view, HoTARAC is of the opinion that the application of the government bond rate is relatively straightforward and less problematic than using high quality corporate bonds to determine the discount rate.

HoTARAC is not aware of any regulatory impediments to implementation of the changes.

HoTARAC offers no comment about whether the changes are in the best interests of the Australian economy.

Comments by HoTARAC on questions from the Exposure Draft are attached.

If you have any queries regarding HoTARAC's comments, please contact Peter Gibson from the Australian Department of Finance and Deregulation on 02 6215 3551.

Yours sincerely



D W Challen

**CHAIR**

**HEADS OF TREASURIES ACCOUNTING AND REPORTING ADVISORY COMMITTEE**

16 September 2009

Encl

Contact: Amy Huxley  
Phone: 6233 3411  
Our Ref: D/14418 AH/TG

## HoTARAC Response to IASB ED 2009/10 Discount Rate for Employee Benefits

### AASB Specific Matters for Comment

1. The IASB Exposure Draft contains proposals to eliminate the use by preparers of different discount rates by deleting from paragraph 78 of AASB 119 *Employee Benefits* the reference to using market yields on government bonds. Paragraph BC7 of the IASB Exposure Draft explains that the IASB has not yet considered whether the measurement of employee benefit obligations could be improved more generally and, in particular, the IASB has not yet considered whether the yield on high quality corporate bonds is the most appropriate discount rate for post-employment benefit obligations. The IASB's objective for publishing these proposals is only to introduce more consistency into the existing requirements.

2. The AASB would particularly value comments on whether:

(a) there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to not-for-profit entities;

HoTARAC is not aware of any regulatory impediments to implementation of the changes.

b) overall, the proposals would result in financial statements that would be useful to users; and

Based on the comments set out in response to AASB Question 3 and IASB Questions 1 and 2, HoTARAC is of the opinion that the proposed amendments will not improve the usefulness of financial statements.

(c) the proposals are in the best interests of the Australian economy.

HoTARAC offers no comment about whether the changes are in the best interests of the Australian economy.

**3. Paragraph Aus78.1 of AASB 119 requires not-for-profit public sector entities to discount post-employment benefit obligations denominated in Australian currency using market yields on government bonds. The AASB has tentatively decided to retain paragraph Aus78.1. The AASB would value comments on:**

**(a) its decision to retain paragraph Aus78.1; and**

**(b) in the limited context of the IASB's objective to have greater consistency, the manner in which not-for-profit public sector entities should discount long-term employee benefit liabilities and the basis for any suggestions.**

As HoTARAC considers the application of the government bond rate to be conceptually superior to the application of a high quality corporate bond rate, HoTARAC supports the AASB's tentative decision to retain Paragraph Aus78.1 of AASB 119 *Employee Benefits* for the not-for-profit public sector and believes that the application of the Paragraph should be expanded to all entities. Refer to IASB Question 1 for further information.

The majority of HoTARAC members strongly believe that differential treatment should remain for the public sector. The borrowing rate for Australian public sector entities is generally less than for private sector entities and therefore the time value of money for public sector entities should reflect this. HoTARAC does not believe that the corporate bond market has any direct relevance in measuring public sector superannuation liabilities.

HoTARAC also notes that the application of a high quality corporate bond rate would result in an inconsistency between AASB 119 and ED 179 *Superannuation Plans and Approved Deposit Funds*. Paragraph 19 of ED 179 requires a risk-free rate to be applied by superannuation funds. Application guidance AG31 in ED 179 states that "The discount rate adopted by a superannuation plan is not intended to reflect the risks inherent in the liability cash flows, which might be allowed for by an adjustment to the discount rate in a fair value measurement...." AG32 in ED 179 goes on to say that "typically, yields on government bonds may represent appropriate discount rates for the purpose of this Standard, or they may be an appropriate starting point in determining such discount rates."

## IASB Matters for Comment

### Question 1 – Discount rate for employee benefits

**Do you agree that the Board should eliminate the requirement to use government bond rates to determine the discount rate for employee benefit obligations when there is no deep market in high quality corporate bonds? Why or why not? If not, what do you suggest instead, and why?**

Disagree.

HoTARAC does not agree to the elimination of the requirement to use government bond rates to determine the discount rate for employee benefit obligations when there is no deep market in high quality corporate bonds for the following reasons:

1. The government bond rate is conceptually superior to high quality corporate bonds.

In HoTARAC's opinion, the government bond rate is conceptually superior to high quality corporate bonds. The principles set out in IAS 19 Paragraphs 79 to 80 to determine the discount rate require the discount rate to reflect the time-value of money, but not risks such as actuarial or investment risk, or entity-specific credit risks. For most economies, the government bond rate is the best indicator of a risk free rate, as high quality corporate bonds typically include a higher element of risk.

For this reason, HoTARAC is of the opinion that the IASB should consider omitting the application of high quality corporate bond rate instead of omission of the government bond rate.

2. The IASB stated objective for greater consistency will not be achieved.

In HoTARAC's opinion, the application of the principles and approach in IAS 39 *Financial Instruments: Recognition and Measurement* and subsequently the *Fair Value Measurement* standard (presently an Exposure Draft) will result in judgement being applied to determine the rate. Inevitably, judgement will lead to different rates being applied across jurisdictions, industries and entities.

3. Inadequate justification for the proposed amendments.

In HoTARAC's opinion, the proposed amendments were not adequately justified in the ED and the IASB has not sufficiently analysed the implications of the amendments. The amendments, in HoTARAC's opinion, are reactive and piecemeal in light of the IASB's planned comprehensive review of IAS 19. HoTARAC therefore encourages the IASB to defer consideration of this issue to form part of the IAS 19 project, to prevent any further medium-term inconsistencies arising.

BC7 mentions that "... the Board has not yet considered whether the yield on high quality corporate bonds is the most appropriate discount rate for post-employment benefit obligations ...", and "The Board's objective in publishing these proposals is only to introduce more consistency into the existing requirements" BC7 does not provide adequate justification for the removal of the requirement to use government bond rates to determine the discount rate for employee benefit obligations when there is no deep market in high quality corporate bonds. This is especially the case when entities currently within the same jurisdiction would apply the same rate, i.e. in Australia they would use the government bond rate. Also, it is HoTARAC's opinion that the proposal does not achieve this objective.

## **Question 2 – Guidance on determining the discount rate for employee benefits**

**For guidance on determining the discount rate, do you agree that an entity should refer to the guidance in IAS 39 Financial Instruments: Recognition and Measurement for determining fair value?\* Why or why not? If not, what do you suggest instead, and why?**

Agree, subject to the concerns below.

In HoTARAC's opinion, guidance needs to be provided to assist entities to determine which corporate bonds are deemed to be high quality bonds.

The guidance provided in IAS 39 and the hierarchy system in the *Fair Value Measurement* Exposure Draft is sufficient to determine a rate once the high quality corporate bonds have been identified.

However, it is HoTARAC's view that the guidance from IAS 39 or the *Fair Value Measurement* Exposure Draft would not achieve the IASB's objective of consistency for this Exposure Draft.

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\* In May 2009, the Board published an exposure draft *Fair Value Measurement*. That exposure draft contains proposals to replace guidance on fair value in IAS 39. The Board will update this reference to be consistent with paragraphs 38–54 of *Fair Value Measurement* when it issues an IFRS resulting from the proposals in that exposure draft.

### Question 3 – Transition

The Board considered whether the change in the defined benefit liability (or asset) that arises from application of the proposed amendments should be recognised in retained earnings or as an actuarial gain or loss in the period of initial application (see paragraph BC10). Do you agree that an entity should:

(a) apply the proposed amendments prospectively from the beginning of the period in which it first applies the amendments?

(b) recognise gains or losses arising on the change in accounting policy directly in retained earnings?

Why or why not? If not, what do you suggest instead, and why?

Considering the other concerns expressed in this response, HoTARAC agrees with the IASB's justification for this decision in its Basis for Conclusion.

16 September 2009

Mr Kevin Stevenson  
Chairman  
Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
Victoria 8007

Email: [standard@asb.gov.au](mailto:standard@asb.gov.au)

Dear Kevin

### Comments on ED 187 Discount Rate for Employee Benefits

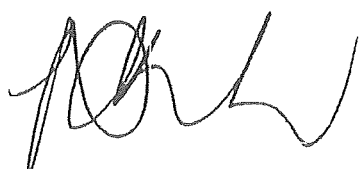
Thank you for the opportunity to comment on the AASB Exposure ED 187 *Discount Rate for Employee Benefits*. CPA Australia, The Institute of Chartered Accountants (The Institute) and the National Institute of Accountants (the Joint Accounting Bodies) have considered the above [proposed] Standard and our comments follow.

The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government, academia throughout Australia and internationally.

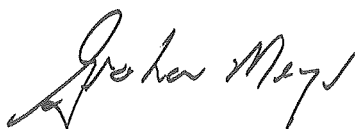
Our response to matters on which Australian comment is requested is included in the attached Appendix. Also attached for your consideration is our submission to the IASB that includes our responses to the specific IASB questions for comment.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at [mark.shying@cpaaustralia.com.au](mailto:mark.shying@cpaaustralia.com.au), Kerry Hicks (The Institute) at [kerry.hicks@charteredaccountants.com.au](mailto:kerry.hicks@charteredaccountants.com.au) or Tom Ravlic (NIA) at [tom.ravlic@nia.org.au](mailto:tom.ravlic@nia.org.au).

Yours sincerely



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The Institute of  
Chartered Accountants  
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[nia.org.au](http://nia.org.au)

## Question

- (a) **Are there any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to not-for-profit entities?**

The Joint Accounting Bodies understand that concerns have been expressed by the Heads of Treasuries and the Treasurer of Victoria regarding the continuing requirement that the public sector use the market yields on government bonds to discount employee benefit obligations (and some other liabilities). We encourage the Australian Accounting Standards Board (AASB) to research this issue with the International Public Sector Accounting Standards Board (IPSASB), rather than immediately moving to the same outcome for both profit entities and not-for-profits.

- (b) **Overall, would the proposals result in financial statements that would be useful to users?**

Refer to our response to Question (a).

- (c) **Are the proposals in the best interests of the Australian economy?**

Refer to our response to Question (a).

- (d) **Is it appropriate that paragraph Aus78.1 be retained?**

Refer to our response to Question (a).

- (e) **In the limited context of the IASB's objective to have greater consistency, do you have any suggestions as to the manner in which not-for-profit public sector entities should discount long-term employee benefit liabilities?**

The Joint Accounting Bodies do not support a change to achieve increased comparability to the detriment of relevance and reliability. Were the AASB to amend AASB 119.Aus78.1, we suggest the AASB should consider adopting the requirements of IPSAS 25 *Employee Benefits* paragraph 94. IPSAS 25.94 refers to the discount rate being approximated by reference to market yields at the reporting date on government bonds, high quality corporate bonds or by another financial instrument. IPSAS 25.94 asserts that in some jurisdictions, market yields at the reporting date on government bonds will provide the best approximation of the time value of money. However, there may be jurisdictions in which this is not the case, for example, jurisdictions where there is no deep market in government bonds, or in which market yields at the reporting date on government bonds do not reflect the time value of money. In such cases, the reporting entity determines the rate by another method, such as by reference to market yields on high quality corporate bonds.

Alternatively, the AASB might consider amending AASB 119.Aus78.1 to introduce a rebuttable presumption that the discount rate be based on an estimate of market yields on high quality corporate bonds. This presumption could be rebutted only on initial adoption of this amendment to IAS 19, and the government bond rate could be used, only when use of the government bond rate would result in information about employee benefits that is more relevant and reliable than that which would occur from using an estimate of market yields on high quality corporate bonds.

16 September 2009

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
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Email: [CommentLetters@iasb.org](mailto:CommentLetters@iasb.org)

Dear Sir David

### **Comments on ED 2009/10 Discount Rate for Employee Benefits**

Thank you for the opportunity to comment on the IASB Exposure Draft 2009/10 *Discount Rate for Employee Benefits*. CPA Australia, The Institute of Chartered Accountants (The Institute) and the National Institute of Accountants (the Joint Accounting Bodies) have considered the above [proposed] Standard and our comments follow.

The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government, academia throughout Australia and internationally.

The Joint Accounting Bodies understand that the problems of market volatility and opaqueness for the discount rate for employee benefits present at the end of 2008 have largely dissipated. Further, we note that the International Accounting Standards Board (IASB) intends a fundamental review of the accounting for employee benefits (including the measurement of defined benefits) in due course. The fundamental review would include consideration of whether the yield on high quality corporate bonds is the most appropriate discount rate for post-employment benefit obligations. Accordingly, we strongly encourage the IASB not to make any amendment to IAS 19 at this time.

However, should the IASB decide to proceed to amend IAS 19, the Joint Accounting Bodies do not agree with the IASB proposal to eliminate the requirement to use government bond rates to discount the employee benefit obligations when there is no deep market in high quality corporate bonds. We consider that for those countries without a deep market in high quality corporate bonds a better approach is for the IASB to introduce into the [proposed] Standard a rebuttable presumption that the discount rate be based on an estimate of market yields on high quality corporate bonds. This presumption could be rebutted only on initial adoption of this amendment to IAS 19, and the government bond rate could be used, only when use of the government bond rate would result in information about employee benefits that is more relevant and reliable than that which would occur from using an estimate of market yields on high quality corporate bonds.

### **Representatives of the Australian Accounting Profession**



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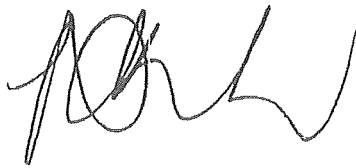
[nia.org.au](http://nia.org.au)

We would also like to see some improved clarity around the expression "high quality corporate bonds".

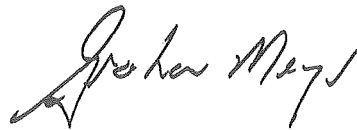
Our response to matters on which specific comment is requested are included in the attached Appendix.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at [mark.shying@cpaaustralia.com.au](mailto:mark.shying@cpaaustralia.com.au), Kerry Hicks (The Institute) at [kerry.hicks@charteredaccountants.com.au](mailto:kerry.hicks@charteredaccountants.com.au) or Tom Ravlic (NIA) at [tom.ravlic@nia.org.au](mailto:tom.ravlic@nia.org.au).

Yours sincerely



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Graham Meyer  
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Andrew Conway  
**Chief Executive Officer**  
**National Institute of**  
**Accountants**

cc: Australian Accounting Standards Board

### **Question 1 – Discount rate for employee benefits**

**Do you agree that the Board should eliminate the requirement to use government bond rates to determine the discount rate for employee benefit obligations when there is no deep market in high quality corporate bonds? Why or why not? If not, what do you suggest instead, and why?**

The Joint Accounting Bodies understand that the problems of market volatility and opaqueness for the discount rate for employee benefits present at the end of 2008 have largely dissipated. Further, we note that the International Accounting Standards Board (IASB) intends a fundamental review of the accounting for employee benefits (including the measurement of defined benefits) in due course. Accordingly, we strongly encourage the IASB not to make any amendment to IAS 19 at this time.

However, should the IASB decide to proceed to amend IAS 19, the Joint Accounting Bodies do not agree with the IASB proposal to eliminate the requirement to use government bond rates to discount the employee benefit obligations when there is no deep market in high quality corporate bonds. We consider that for those countries without a deep market in high quality corporate bonds a better approach is for the IASB to introduce into the [proposed] Standard a rebuttable presumption that the discount rate be based on an estimate of market yields on high quality corporate bonds. This presumption could be rebutted only on initial adoption of this amendment to IAS 19, and the government bond rate could be used, only when use of the government bond rate would result in information about employee benefits that is more relevant and reliable than that which would occur from using an estimate of market yields on high quality corporate bonds.

### **Question 2 – Guidance on determining the discount rate for employee benefits**

**For guidance on determining the discount rate, do you agree that an entity should refer to the guidance in IAS 39 *Financial Instruments: Recognition and Measurement* for determining fair value?\* Why or why not? If not, what do you suggest instead, and why?**

The Joint Accounting Bodies do not agree with the proposal. We have been told by our constituents that it will not always be straightforward for an entity determine the discount rate using the guidance in IAS 39 *Financial Instruments: Recognition and Measurement* for determining fair value. Accordingly, we would prefer guidance specific to IAS 19.

### **Question 3 – Transition**

**The Board considered whether the change in the defined benefit liability (or asset) that arises from application of the proposed amendments should be recognised in retained earnings or as an actuarial gain or loss in the period of initial application (see paragraph BC10). Do you agree that an entity should:**

- (a) apply the proposed amendments prospectively from the beginning of the period in which it first applies the amendments?
- (b) recognise gains or losses arising on the change in accounting policy directly in retained earnings?

**Why or why not? If not, what do you suggest instead, and why?**

The Joint Accounting Bodies agree with the proposals. However, we suggest the need for further clarity in the [proposed] paragraph 156A(b) for entities that currently apply the corridor method.

### **Other comments**

The Joint Accounting Bodies would like to see some improved clarity around the expression "high quality corporate bonds".